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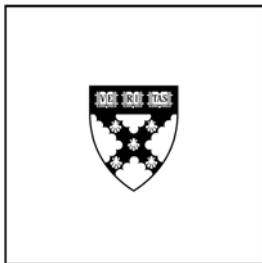
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ABSTRACT. We measure the value of shareholder proxy access by using a recent development in the ability of shareholders to nominate candidates for board seats. We use the SEC's October 4, 2010 announcement that it would significantly delay implementation of its August 2010 proxy access rule as a natural experiment. Because firms with substantial institutional ownership would have been most affected by the SEC's now-delayed changes, we use the share and composition of institutional investors to sort firms into those more and less affected by the October 4 news. Firms that would have been most affected by proxy access, as measured by institutional ownership, lost value on that day. The value drop was 55 basis points for a 10 percentage point change in activist institution ownership. These results suggest that financial markets placed a positive value on shareholder access, as implemented in the SEC's August 2010 Rule.

JEL codes: G14, G32, G34, G38

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Does Shareholder Proxy Access Improve Firm Value? Evidence from the Business Roundtable Challenge

Separation between the ownership and the control of large firms is a defining feature of modern capitalism (see Berle and Means (1932)). Corporate boards are shareholders' primary tool for exercising control over their companies. But boards may fail to pursue shareholders' best interests. These failures can come when boards' loyalties sit with management rather than shareholders; when board members lack necessary skills; or when their time horizons differ from investors' horizons (see, e.g., Jensen 1993 and Shleifer and Vishny 1997). The Securities and Exchange Commission (SEC), seeking to enhance shareholder's control over their firms, has considered changing the rules governing the nomination of corporate directors. The potential rule changes, often referred to as 'proxy access' changes, would give large shareholders the right to nominate new members to corporate boards.

The topic of proxy access has generated heated debate in the corporate governance community for some time.¹ Those who oppose broadening shareholder access to company proxy statements – a move that would make it easier for dissident shareholders to nominate new directors – argue that broadening access would shift a dangerous amount of power to certain kinds of shareholders, for example union pension funds, who could pursue objectives counter to shareholder value maximization (e.g, Bainbridge 2003). They also argue that high-quality directors may be less willing to serve on boards if they must face competition from shareholder-sponsored candidates (e.g., Lipton and Rosenblum 2003).² Proponents of shareholder access

¹ See, e.g., Business Roundtable and U.S. Chamber of Commerce v. U.S. Securities & Exchange Commission, Complaint filed Sept. 29, 2010 at 2 (“Few issues in corporate governance have generated more disagreement or stronger passions.”).

² This argument is related to the idea proposed by Burkart, Gromb and Panunzi (1997) that closer oversight may weaken managerial incentives.

argue that competition in the director election process is desirable, and that giving institutional investors more influence on the board will likely benefit all shareholders (Bebchuk 2003, Bebchuk and Hirst 2010).

This paper uses an unexpected development in the evolution of shareholder proxy access to provide direct evidence on the wealth effects of shareholders' ability to influence corporate decision-making through board representation. Our empirical results suggest that financial markets placed a positive value on shareholder access, as implemented in the SEC's August 2010 Rule. This result bears on many active debates within the corporate governance literature. For example, the result provides evidence on the value of boards. As Hermalin and Weisbach (1998) point out, identification problems make it difficult to estimate the economic impact of board characteristics. Our event study approach provides robust empirical evidence that board characteristics matter for firm value. Specifically, owner representation appears to have been value-increasing in the view of the stock market.

The event we employ as a natural experiment was the SEC's delay of a proposed proxy access rule. On August 25, 2010, under authority provided by Section 971 of the Dodd-Frank Act, the SEC enacted a shareholder proxy access rule. This rule was intended to go into effect on November 15, 2010. On September 29, the Business Roundtable filed a petition in the D.C. Circuit Court of Appeals challenging the new Rule, alleging that it was arbitrary and capricious, exceeded the SEC's authority, and would reduce overall shareholder wealth. In a move that surprised most observers, on October 4 the SEC announced that it would delay implementation of shareholder access until the Business Roundtable challenge was resolved. The delay means that shareholder access will not be required in the 2011 proxy season, as the marketplace had

previously anticipated, and that future access is uncertain. The rule withdrawal has at the very least delayed shareholder proxy access substantially.

This unexpected development provides the basis for an event study. If shareholder access increases shareholder value, then companies that would have been most exposed to the new rule should decline in value, relative to companies that would have been more insulated from the rule. If shareholder access decreases shareholder value, then companies that would have been most exposed to the rule should increase in value, relative to those what would have been more insulated. This natural experiment allows a rough quantification of the value of shareholder proxy access. In addition, the experiment allows testing of hypotheses about board influence. If there is heterogeneity across firms in the value of shareholder influence through the board of directors, or across different types of shareholders in their ability to improve the value of target firms, our natural experiment provides an opportunity to quantify those differences.

Using a 1-day event window around October 4, 2010, we find that share prices of companies that would have been most exposed to shareholder access declined significantly compared to share prices of companies that would have been most insulated from the rule. Specifically, we find a 42 basis point spread between firms with high institutional ownership and firms with low institutional ownership for that day's returns. The pattern of lower returns for firms with higher institutional ownership holds true for equal-weighted excess return portfolios (31 basis point differential), as well as portfolios based on activist ownership (38 basis point differential).³ All three of these estimates are statistically significant. In a regression setting, we confirm that institutional ownership, and especially activist institutional ownership, was

³ We rely on a classification of institutions into activists and others from Greenwood and Schor (2009). Their classification is based on observed prior activism, revealed in firms' 13D SEC filings. Schedule 13D must be submitted by any investor acquiring 5 percent or more of the shares of a public company. The filer is required to list the purpose of the acquisition, which allows Greenwood and Schor to identify investment managers who have demonstrated activism.

correlated with negative returns on October 4. These findings suggest that financial markets placed a positive value on shareholder access, as implemented in the SEC's August 2010 Rule.

Additional refinements and robustness tests support this conclusion. We examine alternative measures of ownership, such as the size of the largest activist institutional stake, an indicator for whether the firm has a single activist investor who has a large enough stake to be eligible under the proposed proxy rule, and the number of distinct owners with large enough stakes to be eligible under the proposed rule. Most of these measures give results consistent with the more simple measure. In our baseline regression, we estimate that each 10 percentage point increase in institutional ownership corresponded to a 9-16 basis point drop in value on October 4. This result is significant at the 10 percent confidence level. For activist ownership, we estimate that a 10 percentage point increase in activist ownership corresponded to a range is 51-59 basis point drop in value. We next compare the impact that different observed firm governance characteristics had on October 4 returns. For the most part, our results with respect to these governance measures are not statistically significant. The only significant result concerns Delaware: the estimated impact of institutional ownership on October 4 returns appears lower among Delaware firms. This finding is consistent with Delaware's earlier introduction of limited proxy access.

We also consider the length of holding periods. Under the withdrawn rule, this would have mattered because a three year holding period would have been required for an investor to nominate board candidates. A shorter holding period for a large stake would have implied proxy access at a later date, and only if the position was held. We find that long term holdings appear to have a somewhat higher impact on firm value, consistent with the details of the proposed rule. Finally, we differentiate among firms with good and poor performance, based on the idea that

activists have more room to improve firms with worse performance. The point estimates for the coefficients on institutional ownership are larger for the set of firms with worse lagged performance, but the differences in point estimates between poor-performance and good-performance firms are not statistically significant. Taken as a whole, our empirical results suggest that proxy access was assigned a positive value by the stock market, that this value was associated with both the presence of the large active owners (who are plausible users of proxy access) and with poor firm track records (indicating possible room for improvement).

These results point to a positive role for boards in corporate governance. There is, in the background, a more general question: how can proxy access enforced by regulation enhance welfare, when owners and firms would have been free to reach optimal agreements on proxy access before the passage of the proposed regulation? In other words, if enhanced proxy access would have increased firm value, why didn't shareholders and managers find a way to privately agree on proxy access, without the intervention of the SEC? Our results suggest not just that proxy access would have created value, but also that some friction prevents firms from achieving the optimal degree of shareholder democracy on their own. It may be impossible for shareholders to commit to compensate managers ex-post should they voluntarily relinquish some power by enhancing proxy access. The fact that we find a muted effect for Delaware, which allowed (but did not require) proxy access for firms incorporated there, suggests that private contracting might have a partial role.

The paper proceeds in six sections. Section 1 summarizes the evolution of shareholder access in the U.S. Section 2 reviews the existing related literature on proxy access and corporate governance more generally. Section 3 explains our empirical strategy. Section 4 describes our data and methodology. Section 5 discusses our results, and Section 6 concludes.

1. Background: Proxy access and boards of directors in the United States

Boards of directors are one of the main channels through which corporations' owners assure themselves of getting a return on their investment (Shleifer and Vishny 1997). However, boards may not necessarily always pursue shareholders' best interests. Boards may be populated by insiders, or outsiders who are allied with the CEO; they may lack the necessary skills; or they may have a time horizon that is different from the firms' owners (see, e.g., Jensen 1993 and Shleifer and Vishny 1997). In this case, reforming the way in which boards are chosen may improve corporate governance and firm value.

But reducing hurdles for shareholder access to board seats may come at a cost. For one thing, reducing hurdles too far may lead to 'nuisance' candidates proposed by shareholders with minimal holdings. Even without nuisance candidates, owner influence over firms may be costly because of reduced managerial effort. Burkart et al (1997) argue that "*even when tight control by shareholders is ex post efficient, it constitutes ex ante an expropriation threat that reduces managerial initiative and noncontractible investments*" (p 693). Second, there may be conflicts of interest between large and small owners, or between shareholders with different patterns of outside interests and agendas (see Shleifer and Vishny 1997). For example, Bebchuk (2007) points out that "*a shareholder might, for example, seek to protect labor interests, advance a 'social' agenda, or extract 'greenmail' benefits.*" Because of plausible arguments for both benefits and drawbacks to enhancing shareholder influence over firms, evaluating these competing predictions is an open empirical issue.

The corporate law of every U.S. jurisdiction requires that corporations hold an annual meeting to elect directors. In this election, the company will invariably nominate exactly the

number of candidates to fill the available seats – for example, seven candidates for seven seats. Shareholders of the corporation have the right to nominate their own candidates to the board, but the process for doing so is time-consuming and expensive. A shareholder who wants to nominate one or more candidates would have to file Schedule 14A with the SEC, hire a proxy solicitor, and often engage in an expensive public campaign to support their nominee or nominees. These expenses are only reimbursed if the shareholder gains control of the board.⁴ Moreover, the shareholder must share the benefits of any improvement in corporate performance *pro rata* with the other shareholders. As a result of these obstacles, contested director elections outside the context of a hostile takeover bid have been exceedingly rare in corporate America (Bebchuk 2003).⁵

Against this backdrop, many commentators have viewed shareholder access to the company's proxy statement as an essential step to make director elections more meaningful, and, by extension, to improve overall corporate governance. After decades of discussion,⁶ and not coincidentally in the wake of corporate scandals at Enron, Worldcom, and other large U.S. public companies, the SEC proposed a shareholder access rule in October 2003. Under the 2003 rule, shareholders would gain the right to place one or more nominees on the company's proxy statement after one of two trigger events had occurred: (1) "withhold" votes of more than 35% of votes had been cast for one or more directors; or (2) a majority vote for a 14a-8 shareholder access proposal, proposed by a shareholder or shareholder group that had held at least 1% of the

⁴ For the classic statement of this rule, *see* *Rosenfeld v. Fairchild Engine & Airplane Corp.*, 128 N.E. 2d 291 (N.Y. 1955)

⁵ In July 2007, the SEC promulgated its long-awaited "eProxy Rules," which allow insurgents to post their proxy materials on-line and simply mail shareholders a "Notice of Internet Availability of Proxy Materials." In theory, eProxy rules should reduce the costs of proxy solicitation and increase the number of contested director elections. However, the early empirical evidence suggests that the number of contested director elections did not increase substantially in the 2009 or 2010 proxy seasons.

⁶ See Proposed Rule, 74 Fed. Reg. at 29,029 n. 73 (June 18, 2009) (noting that the Commission first considered proxy access in 1942).

company's shares for at least one year. The Business Roundtable and other groups representing director and management interests engaged in a lobbying effort against the proposed Rule. By early 2005, the SEC issued a series of no-action letters permitting companies to omit shareholder proposals based on the proposed rule, effectively withdrawing its proposal.

In 2006, the American Federation of State, County, and Municipal Employees (*AFSCME*) submitted a shareholder proposal to American International Group (*AIG*) to amend *AIG*'s bylaws so that a 3% shareholder could place one nominee in *AIG*'s proxy materials – in effect, trying to do at *AIG* what the SEC's proposed Rule 14a-11 had tried to do more generally. Surprising many commentators, the Second Circuit Court of Appeals held that this proposal was *not* excludable under the Rule 14a-8(i)(8) exclusion, which at the time permitted companies to exclude proposals “relat[ing] to an election for membership on the company's board of directors.” The court found that the proposal related to board elections broadly, and not to “*an* election” of directors.⁷ The holding seemed to open up the possibility of proxy access on a company-by-company basis. But in December 2007, the SEC amended the Rule 14a-8(i)(8) exclusion to permit corporations to exclude proposals “relating to an election for membership on the company's board” or relating to “a procedure for such nomination or election.” This amendment was intended to reverse the Second Circuit's holding in *AFSCME v. AIG*.

Shareholder proxy access remained dormant until May 2009, when the SEC returned to the issue with a new shareholder access proposal. The SEC explained: “The nation and the markets have recently experienced, and remain in the midst of, one of the most serious crises of the past century. This crisis has led many to raise serious concerns about the accountability and responsiveness of some companies and boards of directors to the interests of shareholders, and

⁷ *AFSCME v. AIG*, 462 F.3d 121 (2nd Cir. 2006).

has resulted in a loss of investor confidence.”⁸ Under the proposed Rule 14a-11, a shareholder or shareholder group that owned more than 1% of a large U.S. public company (defined as market capitalization greater than \$700 million), more than 3% of a midsize public company (market capitalization \$75-\$700 million), or more than 5% of a small public company (market capitalization less than \$75 million) would have the ability to place nominees on the company’s proxy statement for up to one-quarter of the total board seats.

In an effort to preempt or at least shape the SEC’s consideration of shareholder access, Delaware amended its corporate code to confirm that shareholders could amend the company’s bylaws to permit proxy access. Section 112 of the Delaware General Corporation Law, enacted in May 2009, provides that: “The bylaws may provide that if the corporation solicits proxies with respect to an election of directors, it may be required . . . to include in its proxy solicitation materials . . . 1 or more individuals nominated by a stockholder.” Section 112 reflects one application of the Delaware Supreme Court’s holding in *CA v. AFSCME*,⁹ handed down in July 2008, which permits shareholders to regulate procedural aspects of corporate governance (e.g., how decisions are made) but not substantive aspects, which are left to the board. Thus Section 112 confirmed the shareholders’ right to opt-in to proxy access (a so-called “voluntary proxy access regime”).

In July 2010, the U.S. Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act. Notwithstanding Delaware’s efforts to preempt federal action, Section 971 of the Act amended Section 14(a) of the Securities Exchange Act to provide the SEC explicit authority to adopt proxy access rules. By confirming that the SEC had the authority to

⁸ Securities and Exchange Commission Proposed Rule Facilitating Shareholder Director Nominations (June 10, 2009).

⁹ 953 A.2d 227 (Del. 2008).

issue shareholder access rules and signaling Congress's support for such rules, Section 971 made shareholder proxy access inevitable, according to most observers.

On August 25, 2010, by a 3-2 vote, the SEC announced the adoption of a final Rule 14a-11, mandating proxy access at all U.S. public companies. Any shareholder or shareholder group that holds more than 3% of a U.S. public company's shares for more than three years is eligible to nominate candidates for up to 25% of the company's board seats. The new Rule 14a-11 was planned to go in to effect on November 15, 2010, well in time for the April/May 2011 proxy season.

On September 29, the Business Roundtable, along with the U.S. Chamber of Commerce, filed a complaint in the D.C. Circuit Court of Appeals, alleging that the SEC's proxy access rules were unlawful under U.S. securities laws and "arbitrary and capricious." The Business Roundtable complaint also asserted – but did not explain – that the SEC's proxy rules "do not promote efficiency, competition, and capital formation."¹⁰ Congress's authorization to the SEC under Section 971 of the Dodd-Frank was intended to largely shut down this kind of challenge; perhaps as a result, the Business Roundtable complaint did not attract significant media attention.

However, on October 4, the SEC unexpectedly announced that it would stay implementation of Rule 14a-11, pending resolution of the Business Roundtable litigation in the D.C. Circuit. The SEC explained: "Among other things, a stay avoids potentially unnecessary costs, regulatory uncertainty, and disruption that could occur if the rules were to become effective during the pendency of a challenge to their validity."¹¹ News accounts noted that the

¹⁰ Business Roundtable and U.S. Chamber of Commerce v. U.S. Securities & Exchange Commission, Complaint filed Sept. 29, 2010 at 2.

¹¹ In the Matter of the Motion of the Business Roundtable and the U.S. Chamber of Commerce for Stay of Effect of Commission's Facilitating Shareholder Director Nomination Rules, File No. S7-10-09 (Oct. 4, 2010).

SEC's announcement was a surprise.¹² Commentators also noted that the SEC's stay meant that proxy access rules would not go into effect for the 2011 proxy season.¹³

2. Literature

The delegation of control over firms to professional managers is a defining feature of modern capitalism (see Berle and Means 1932), and one that raises the possibility of agency problems. Boards are supposed to represent the interests of shareholders, but estimating the economic impact of boards and board structure has been difficult because of econometric identification challenges. Hermalin and Weisbach (1998) point out that one reason that much of the corporate governance literature finds weak correlations between board characteristics and firm performance may be that the board characteristics are “endogenous,” i.e. across firms, their characteristics are likely not assigned at random. This makes the effect of any board characteristic (e.g., the presence of outsiders, the number of directors) impossible to identify based only on the observed correlation between that characteristic and firm performance.

Shareholder access to the company proxy is one specific dimension of corporate governance that has been heavily debated over the years. As an illustration, more than 700 different comment letters were submitted to the SEC when proxy access was proposed in 2003, and more than 500 different comment letters were submitted when proxy access was proposed again in 2009. Proponents of shareholder access (e.g., Bebchuk 2003, Bebchuk and Hirst 2010) point out that proxy contests under the existing regime are exceedingly rare, and argue that a meaningful director election process would improve corporate governance. Opponents of

¹² See, e.g., Wachtell, Lipton, Rosen & Katz memorandum to clients (Oct. 5, 2010), SEC Stays Shareholder Access – For Now (noting “unexpected development”).

¹³ See, e.g., Wachtell memo (Oct. 5, 2010); Jesse Westbrook, SEC Delays Proxy-Access Rules Amid Legal Challenge, Bloomberg (Oct. 4, 2010).

shareholder access argue that shareholders already have sufficient voice in the election of directors (e.g., Bainbridge 2010), that shareholder access rules would likely shift too much power to shareholders or shareholders with specific agendas, and that high-quality directors may be less willing to serve on boards if they must face competition from shareholder-sponsored candidates (e.g., Lipton and Rosenblum 2003). A third set of commentators object to the “one-size-fits-all” approach of mandatory shareholder access (e.g., Grundfest 2009). These commentators propose that shareholders should be able to opt-in, or at least opt-out, of the SEC’s proxy access rules.

A recent theory paper by Harris and Raviv (2010) addresses the optimal extent of control to place in the hands of shareholders versus managers. Their model includes strategic communication between self-interested and potentially privately informed managers and shareholders as well as delegation. Harris and Raviv find that when shareholders seek to maximize firm value and are not misinformed, it is optimal to place the delegation decision in the hands of shareholders, allowing them to decide *ex ante* which decisions to leave to management and which to make directly. Owners will then delegate decisions where management’s information advantage outweighs its agency costs to managers. The authors view this result as being consistent with Bebchuk’s (2005) recommendation to allow shareholders to set the “rules of the game” regarding decision power and corporate governance.

The idea of empirically evaluating regulatory changes with stock market data was introduced by Schwert (1981).¹⁴ Two prior studies use this methodology to examine the wealth effects of shareholder proxy access. Akyol, Lim and Verwijmeren (2010) examines 14 events

¹⁴ See Hochberg, Sapienza and Vissing-Jorgensen (2009) for a recent example.

between September 2006 and December 2009 that, in their interpretation, increased¹⁵ or decreased¹⁶ the likelihood of shareholder proxy access. For each event date, they compare the return of a portfolio of U.S. firms to the return of a global market portfolio (excluding U.S. firms) and to a Canadian market portfolio. They also isolate U.S. financial firms from other U.S. firms, on the theory that financial firms might be more likely to be targeted by shareholders for proxy access. Six of the events taken individually produce statistically significant abnormal returns around the event dates (at 95% confidence), and when the events are aggregated the returns are highly significant and inversely correlated with shareholder proxy access. Specifically, the authors find that an increased likelihood of shareholder access reduced returns to the U.S. portfolio relative to the non-U.S. portfolios, and for U.S. financial firms relative to non-financial U.S. firms. The authors conclude that “increasing shareholder rights . . . may actually be detrimental to shareholder wealth,” and that the results “highlight the need for the SEC to further deliberate on the proposed rule, and to consider not implementing the proposed changes.”

Larcker, Ormazabal, and Taylor (2010) similarly use an event study approach to examine thirteen events between March 2007 and June 2009 that arguably increased¹⁷ or decreased¹⁸ the

¹⁵ The nine events that, according to the authors, increased the likelihood of shareholder proxy access were: the Second Circuit’s holding in *AFSCME v. CA* (Sept. 5, 2006), the SEC announcement of a roundtable discussion on proxy access (April 24, 2007), the SEC’s disclosure of a proposed rule on proxy access (July 27, 2007), a speech by SEC Commissioner Elisse Walter on proxy access (Feb. 18, 2009), a speech by SEC Chairwoman Mary Schapiro on proxy access (April 6, 2009), the SEC’s announcement that it would vote on a proposed rule (May 12, 2009), the SEC’s announcement of the content of the proposed rule (May 14, 2009), the introduction of the Schumer Bill in the U.S. Senate (May 19, 2009), and the SEC’s vote in favor of the proposed rule on proxy access (May 20, 2009).

¹⁶ The five events that, according to the authors, decreased the likelihood of shareholder proxy access were: the SEC’s publication of a final Rule 14a-8 with no substantial changes (Nov. 28, 2007), the SEC’s publication of a final Rule 14a-8(i)(8) with no substantial changes (Dec. 12, 2007), the introduction of an opt-in shareholder proxy access bill in the Delaware House of Representatives (Mar. 10, 2009), the passage of this bill in the Delaware House (March 18, 2009), the passage of the bill in the Delaware Senate (April 8, 2009), and the reopening of the comment period on the SEC proposed Rule on shareholder access (Dec. 14, 2009).

¹⁷ The eight events that, according to the authors, increased the likelihood of shareholder proxy access are: first mention of the Schumer Bill in the press (April 25, 2009), introduction of the Schumer Bill in the U.S. Senate (May 19, 2009), first mention of the Shareholder Empowerment Act in the press (June 12, 2009), the SEC announcement

likelihood of shareholder proxy access. The authors use the number of institutions with 1% or more ownership (*NLargeBlock*) and the number of possible coalitions that would control 1% or more of the shares outstanding (*NSmallCoalitions*) as proxies for a company's exposure to a shareholder access rule. For five out of the thirteen events, the authors find a statistically significant (at 95% confidence) negative correlation between *NLargeBlock* and events that increased the likelihood of shareholder proxy access. For a (somewhat different) five out of thirteen events, the authors find a statistically significant negative correlation between *NSmallCoalitions* and events that increased the likelihood of proxy access. As with the Akyol study, the coefficients for both *NLargeBlock* and *NSmallCoalitions* become highly significant and inversely correlated with increased likelihood of shareholder access when all thirteen events are pooled. The authors conclude that their findings are consistent with the view that >1% shareholders "will use the privileges afforded to them by proxy access regulation to manipulate the governance process to make themselves better off at the expense of other shareholders." Larcker & Tayan (2010) summarize this literature as suggesting that "regulation of corporate governance is viewed negatively by shareholders."

One problem inherent in both of these prior event studies is that at least some of the events being studied are of questionable importance. For example, both studies identify the announcement of a SEC roundtable discussion series on April 24, 2007 as an event that increased the likelihood of proxy access. With the SEC having considered proxy access off-and-on for

of a roundtable discussion on proxy access (April 24, 2007), the SEC announcement of amendments to Rule 14a-8 14a-8(i)(8) (July 27, 2007), first mention of potential amendments to Rule 14a-11 (April 6, 2009), the SEC's vote in favor of the proposed rule on proxy access (May 20, 2009), and the publication of the SEC's draft proposal for Rule 14a-11 (June 10, 2009).

¹⁸ The five events that, according to the authors, decreased the likelihood of shareholder proxy access are: the SEC's publication of a final Rule 14a-8 with no substantial changes (Nov. 28, 2007), the SEC's publication of a final Rule 14a-8(i)(8) with no substantial changes (Dec. 6, 2007), the introduction of an opt-in shareholder proxy access bill in the Delaware House of Representatives (Mar. 10, 2009), the passage of this bill in the Delaware House (Mar. 18, 2009), the passage of the bill in the Delaware Senate (April 8, 2009), and the reopening of the comment period on the SEC proposed Rule on shareholder access (Dec. 14, 2009).

most of the prior decade (and having already promised to take up proxy access after the *AFSCME* decision the prior year), it is not clear why the announcement of a roundtable discussion – with, of course, no prediction on what conclusions the discussants would reach – should convey meaningful information to the marketplace, much less increase the likelihood of proxy access.

In fact, the impact of the April 24 announcement on the likelihood of proxy access is not even directionally clear. At the time of the announcement, the *AFSCME* decision permitted proxy access on a company-by-company basis. In the press release announcing the Roundtable series, SEC Chairman Christopher Cox noted generally: “This roundtable will explore the relationship between the federal proxy rules and state corporation law, and pose questions to the participants about whether this relationship can be improved.”¹⁹ After the Roundtable, the first move from the SEC, proposed in October 2007 and finalized in December 2007, was amendments to Rule 14a-8(i)(8) that overruled the *AFSCME* decision and eliminated proxy access. To the extent that investors interpreted Cox’s general statement to mean that the *AFSCME* decision was vulnerable (which, in retrospect, would have been an accurate interpretation) the April 24 announcement should have decreased the likelihood of shareholder access, rather than increased it as the Akyrol and Larcker studies predict.

A second problem with both studies is that many of the events were predicted in advance, at least in part, by the marketplace. For example, it is well-known that the Corporate Law Section of the Delaware Bar Association, not the Delaware legislature, creates Delaware corporate law. Once the Corporate Law Section voted in favor of a shareholder access amendment on February 26, 2009, its implementation in Delaware became virtually a foregone conclusion. Both the Akyrol study and the Larcker study examine the introduction of the

¹⁹ SEC Announces Roundtable Discussions Regarding Proxy Access, Press Release (April 24, 2007).

shareholder access bill in the Delaware House of Representatives (March 10, 2009), the passage of the bill in the House (March 18), and the passage of the bill in the Delaware Senate (April 8), but fail to examine the recommendation from the Corporate Law Council that occurred on February 26. If the marketplace fully anticipates an event, then wealth effects around the event date can be meaningless.

Despite these deficiencies, the Akyol and Larcker studies have led some commentators to conclude that shareholder proxy access reduces shareholder wealth. For example, Grundfest (2010) summarizes the “consistent conclusion” from the two studies as follows:

[P]roxy access, as currently proposed by the Commission, reduces shareholder wealth, and, even if preferred by vocal institutional investors, is inimical to the best interests of the shareholder community as a whole. . . . The best currently available empirical data indicate that, given a choice between the current regime and the Commission’s proxy access rules, shareholders seeking to maximize returns would prefer the status quo because the proposed rules appear to destroy shareholder wealth.

In contrast, Coates (2009) summarizes the empirical evidence on shareholder access as being inconclusive: “[T]o my knowledge, there is no reliable large-scale empirical evidence – good or bad – on the effects of shareholder access to a company’s proxy statement . . . because there has been no significant observed variation in such a governance system within any modern developed economy.”

3. Empirical Strategy

The unexpected delay in shareholder access that occurred on October 4, 2010 provides the basis for an empirical test of the wealth effects of shareholder access. We apply the idea of Schwert (1981) that stock price changes following the announcement can be informative about the market’s evaluation of the impact of regulation on value.

For the event to be useful as a natural experiment, there are several requirements. First, it has to be unexpected. By all accounts, the SEC's delay was unexpected, and therefore not predicted in advance by the marketplace. The possibility of pre-announcement leaks is minimal in this context because the source would have to have been the SEC, which has a reputation for being relatively immune to leaks. Second, the value impact has to affect stock prices – that is, it must be a relatively significant event. The degree of debate and press coverage around shareholder proxy access suggests that implementation of the Rule was a significant event, and, by extension, the delay of the rule was also significant. The fact that the SEC had already implemented shareholder access means that a specific rule was on the table, and all companies reacted to the same rule. Finally, evading the proposed regulatory reform must be difficult or impossible. Rule 14a-11 is a mandatory rule, with no prospect for opt-out. For this reason, market prices before October 4 likely did not reflect any possibility that companies might evade the rule.

If shareholder access increases shareholder value, then companies that would have been most exposed to the new rule should decline in value, relative to companies that would have been more insulated from the rule. If shareholder access decreases shareholder value, then companies that would have been most exposed to the rule should increase in value, relative to those that would have been more insulated. Furthermore, we can use the event to test if the value effect of shareholder access depends on the features of a firm or its shareholders. For example, the possibility of board representation may be more valuable when shareholders are sophisticated, or if they are more willing to get involved with the governance of a firm. Board representation may be less valuable if the board already represents the views of outside investors well.

We use several proxies for determining which companies were more and less likely to be affected by the SEC's proxy access rule. First, and most importantly, we examine the institutional ownership of the companies in our sample, on the assumption that institutions, particularly institutions that held 3% or more of the company's stock, would be most likely to make use of proxy access. We also distinguish between activist institutions such as hedge funds, and traditionally passive institutions such as index funds. Our view is that activist institutions would be more likely to make use of proxy access (Pozen 2003). Many institutions are reluctant to exercise control rights and participate in activism. Examples include index funds and some pension funds (see e.g. Del Guercio and Hawkins 1999). Other institutions are much more prone to activism and direct influence on corporate governance. For example, Kahan and Rock (2006) argue that hedge funds have stronger financial incentives and fewer regulatory constraints than mutual funds, and may therefore be better able to monitor firms in their portfolios. Greenwood and Schor (2009) also suggest that hedge funds may be better able to identify underperforming companies. We use the Greenwood and Schor classification of activist institutional investors, which is based on observed activism over the 1993-2006 period.

Finally, because the SEC's proposed rule would have given proxy access to investment managers whose stakes had been held for at least 3 years, we explore empirical specifications that capture the length of time that the firms' existing investors, activist or otherwise, have held their stakes.

We also use three other governance-related measures for determining which companies were more impacted by the SEC's proxy access rule. First, we distinguish between companies incorporated in Delaware and those that are not. At least since May 2009 and likely before, shareholders in Delaware companies have had the ability to opt-in to shareholder access, while

shareholders of companies incorporated in other states do not clearly have this right. It seems possible, therefore, that Delaware companies would have benefitted less from SEC-mandated shareholder access than companies incorporated in other states.

Second, we distinguish between companies with staggered boards and those with unitary boards. Companies with staggered boards may be particularly vulnerable to Rule 14a-11 because the Rule permits shareholder access for up to one-quarter of the total seats, rather than one-quarter of the seats available in the election. For example, consider a company with an eight-member staggered board, in which two seats are up for election at the 2011 annual meeting. Under Rule 14a-11, a shareholder could nominate candidates for both of the seats – essentially running a “full slate” for the seats that are up for election. Contrast this result to a company with an eight-member unitary board. The shareholder can still nominate candidates for two seats, but this amounts to only one-quarter of the seats that are up for election. Therefore, by applying the one-quarter metric to total seats rather than available seats, Rule 14a-11 might have affected companies with staggered boards more than it affected companies with unitary boards. Finally, we differentiate companies according to their Governance Index (Gompers, Ishii and Metrick 2003), to test the theory that companies with greater entrenchment in general might be more vulnerable to the SEC’s shareholder access rule.

The impact of shareholder board representation may also depend on the scope for improvement in firm performance. A firm with strong current performance and a high stock price may offer fewer opportunities for intervention. We therefore sort firms based on lagged stock returns and valuation ratios, test whether the impact of institutional and activist institutional ownership is strongest among the firms with the worst recent performance.

Our empirical results are based on a single event, and we are careful to assess the statistical significance of results based on one day of returns. Because stock returns have patterns of cross-sectional correlation, our approach and our measures of statistical significance must be adjusted accordingly. Our baseline regressions use risk-adjusted returns, which control for market performance and the two additional risk factors identified in Fama and French (1993) (see the data section for details). Using risk-adjusted returns means that we control for the overall pattern of market movements on October 4. We report results for using raw returns as the dependent variable for the sake of completeness.

Second, we need to address cross-sectional correlation among stock returns. Incorrectly assuming independence in stock movements can yield standard error estimates that are biased downward by a factor five or more (Fama and French 2000). Therefore, we do not rely on standard regression standard error estimates to assess the significance of our coefficient estimates. Instead, we assess the significance of our results in two ways: GLS standard errors and non-parametric assessment using the empirical distribution of coefficient estimates. To calculate GLS standard errors, we use pre-event return data for our sample stocks to estimate the covariance matrix for individual stock returns. We then use the estimated covariance matrix to calculate standard error estimates that adjust for the observed correlations between different stocks.²⁰ Applied to this setting, we find GLS standard error estimates are approximately twice as large as OLS standard errors. In all tables reporting regressions, we report the GLS standard errors as well as p-values from the empirical distribution of coefficient estimates.

²⁰ In matrix notation, we use $V = (X'X)^{-1}(X'\Omega X)(X'X)^{-1}$ to estimate standard errors, where X is a vector of return data, and Ω is the pre-event covariance matrix of returns. This differs from basic OLS standard errors which use the identity matrix in place of Ω . An underlying assumption in this approach is that the pre-event covariance matrix is an appropriate estimate for the true underlying covariance matrix on October 4.

Second, as a less parametric approach to assessing significance, we re-estimate each regression in the 67 trading days after June 30, 2010. We do not use earlier dates because our key variables of interest are based on institutional holdings as of June 30. We then use the empirical distribution of coefficient estimates to test the significance of each of our regression coefficients. In other words, we empirically estimate how many days *other* than the event day would have delivered estimated coefficients equal in magnitude to the coefficient we estimate for October 4. Because our significance estimates using this empirical approach are very similar to the GLS-based estimates, our tables report only the GLS standard errors.

4. Data

We collect stock price data from Datastream, and define each stock's return as the log of the closing stock price on Monday, October 4, minus the log of the closing stock price on Friday, October 1. We use a one-day event window because the SEC's announcement on delaying shareholder access came out during the trading day on October 4.²¹ We estimate factor-adjusted returns based on the Fama-French (1993) three-factor model, which controls for firms' exposure to overall stock market moves as well as a value/growth effect and a small firm effect. We estimate firm betas on the Fama-French factors using daily stock returns for the period between January 1, 2009 and December 31, 2009. We use the daily factor returns from Ken French's data library.²² We winsorize all three beta estimates at the 5th and 95th percentiles.

For each stock we take the Gompers, Ishii and Metrick (2003) governance measure for each S&P1500 firm in 2006, the last year for which the index has been calculated. From RiskMetrics, we identify firms with staggered board provisions and collect data on the number of

²¹ The SEC announcement was time-stamped at 12:21 pm on October 4. The announcement hit Bloomberg at 3:20 pm that day.

²² See http://mba.tuck.dartmouth.edu/pages/faculty/ken.french/data_library.html. Accessed October 12, 2010.

board members. We collect data on each firm's equity value from CRSP; this allows us to run both value-weighted and equal-weighted empirical tests.

Institutional ownership data come from ThomsonReuters, which summarizes data from 13F filings by institutional investors. We use data from the second quarter of 2010, because later data are incomplete.²³ We look exclusively at shares held by U.S. institutions. For each investment manager, we calculate total holdings, as both dollars and number of stocks. For each firm in the sample we construct the following measures of institutional ownership: the number of institutional owners; the number of institutional owners above the 3% ownership threshold (the requirement for proxy access); a dummy variable equal to one if a firm has at least one institutional owner with a 3% stake; and the total ownership by institutions. We calculate the average size of all institutional ownership of each firm's stock, where size is measured as the total value of an institutions' holdings or the number of stocks held.

Activist institutional investors are willing to intervene in corporate management and decision-making. Because these investors are particularly aggressive about influencing firm management and board composition, they are more likely to have made use of proxy access (see e.g. Brav, Jiang, Partnoy, and Thomas 2008). We use the classification of activist investors identified by Greenwood and Schor (2009). They construct a sample of activists based on 13D filings and DFAN filings with the SEC. Investment managers and other investors must file a 13D filing with the SEC within 10 days of acquiring 5% or more of any class of a company's securities. 13D filings also include a "Purpose of Transaction" section which allows Greenwood and Sosner to identify activist purposes and exclude investors whose 13D filings reflect passive strategies. DFAN filings are filed with the SEC by investors intending to engage in a proxy fight

²³ An earlier draft of the paper used holdings data from the first quarter of 2010.

with firm management. These filings allow Greenwood and Schor to construct a list of activist investors, which they identify as investors whose 13D or DFAN filings indicate activist intent.

We collect firm data from the CRSP-Compustat merged database. For each firm, we calculate its 2009 end of year book-to-market ratio (book value of common equity divided by the stock price times number of shares outstanding), minus the mean of its Fama-French (48) industry. Similarly, we calculate the industry-adjusted calendar year 2009 stock return based on the Fama-French 48-sector industry classification.²⁴

5. Results

Our main sample is the S&P 1500 because these firms are large, liquid, and heavily traded, but our results hold for the larger universe of all publicly-traded companies as well.²⁵ In the S&P 1500, we have ownership data for 1,445 firms. Panel A of Table 1 shows the mean institutional ownership as well as activist institutional ownership, both by decile. There is substantial variation in each of these measures. Institutional ownership overall amounts to about half of the typical company's shares, but in the bottom decile, institutional ownership averages about 24.6 percent. In the top decile it averages almost 70 percent. Activist institutional ownership averages 0.05% of the shares in the bottom decile, but 12.33% of shares in the top decile.

a. Institutional ownership

Panel B of Table 1 presents summary statistics for four measures of institutional ownership: the raw total institutional ownership; the number of owners with at least 3% of the

²⁴ We have rerun our tests using 12 Fama-French industries, 2-digit NAICS codes, or S&P Industry sectors. Results are very similar for all these industry measures.

²⁵ We exclude Actel, a S&P 1500 firm that experienced a 30 percent positive return on October 4, due to a takeover announcement. Our empirical results are not meaningfully affected by this exclusion.

capital; the highest single activist institutional ownership stake; and the number of activist institutional owners.

Table 2 sorts firms by institutional ownership, and examine returns on October 4 across the different levels of institutional ownership. The average equal weighted return was -125 basis points. There was a 42 basis point difference between the returns of the highest and lowest institutional ownership deciles. The firms with highest institutional ownership would have been most affected by the now-delayed changes to shareholder proxy access, and these firms had the largest price drops on October 4. The difference is statistically significant at the 1 percent confidence level.

The next column reports excess returns, which control for firms' exposure to the market, size, and value factors. Using this return measure, the difference between the returns of high and low institutional ownership stocks rises to 31 basis points. Sorting on activist owners, who would have been more likely to use expanded proxy access powers, produces a differential of 38 basis points. Note that the difference in the level of ownership across deciles is much smaller for the activist institutional ownership measure than for the comprehensive measure. Using either measure the differences between high and low ownership groups are statistically significant.

Having documented the negative relationship between institutional ownership and returns on Monday, October 4, we now turn to regression results. Table 3 presents the baseline regression results. In column (1), we regress the excess returns for the day of each stock in the S&P 1500 index on institutional ownership. The coefficient estimate in this specification is -126 basis points, significantly different from zero at the 10 percent confidence level. Here and throughout the paper, our reported standard errors account for the observed correlation of individual stock returns, as discussed in Section 3. The coefficient estimate implies that a 10

percentage point increase in institutional ownership was associated with an additional 13 basis point loss of value on October 4. . Column (2) of Table 3 presents a similar regression for activist institutions. The estimated coefficients are larger in magnitude and statistically significant at the 1 percent confidence level. Our estimates suggest that a ten percentage point increase in activist ownership is associated with a 55 basis point drop in value on October 4.

In columns (3) and (4), we repeat these tests using excess returns. Our excess return measures adjust returns based on the Fama-French three-factor model. Betas for the three-factor model are estimated using daily data from 2009. The coefficient estimate using the comprehensive institutional ownership measure is -96.3 basis points, again significant at the ten percent level. The coefficient estimate for the activist institutional ownership measure is -514.7, significant at the 1 percent confidence level. From this point on, we only report regressions with excess returns. This approach is more conservative, and controls for any differences in factor exposures across stocks. Columns (5) and (6) of Table 3 examine value-weighted excess returns. Our coefficient estimates are slightly larger, but our estimated statistical significance falls.

Table 4 examines alternative measures institutional ownership. In the first column, we measure the largest institutional stake (as a share of firm value), including both activist and non-activist institutions. The estimated coefficient is negative and not statistically significant. Column (2) regresses the October 4 excess return on the largest single activist stake, and our estimated coefficient of -644 basis points is statistically significant at the 1 percent confidence level. The fact that this coefficient is larger than the coefficient for total activist ownership highlights the role of large single activist investors. This is consistent with an important role for concentrated institutional ownership, and may reflect coordination costs or free-riding (see e.g., Grossman and Hart 1980).

The second alternative measure is motivated by the details of the SEC's rule, which would have required an owner to have a 3 percent stake to qualify for proxy access. Although the rule would have allowed investors to combine for the purpose of proxy access, having an individual owner above the 3 percent threshold means that proxy access was feasible without coordination. Having more such owners might increase the likelihood further (this number ranges from zero to four). The coefficient on the number of institutional owners with stakes above 3 percent is negative and significant at the 1 percent level. The coefficient estimate, -33.8, implies that each additional large, institutional owner in a firm is associated with a reduction of equity value by 34 basis points on October 4. The results in this section lead us to conclude that the institutional ownership mattered for performance in a way that is consistent with the market assigning a positive value to the proposed proxy access rules.

Firm heterogeneity

Having established that institutional ownership is associated with negative returns on October 4, we now test hypotheses about the relationship between firm characteristics and the value of proxy access. Table 5 presents the results of this analysis. All of these results use excess return measures, use the S&P 1500 sample, and control for activist institutional ownership. In general, the evidence of any role for governance metrics is weak.

Our first test looks at the impact of staggered boards. Companies with staggered boards might be particularly vulnerable to Rule 14a-11, since the Rule would have permitted shareholder access for up to one-quarter of the total seats, rather than one-quarter of the seats available in the election. The regression results in column (1) of Table 5 suggest that having a staggered board is not predictive of stock return on the event day. In column (2), we use the Gompers, Ishii and Metrick (2003) governance index ("G"). The hypothesis is that firms with poor

governance measures (high G values) may see larger potential benefits from shareholder proxy access. Again, the results are close to zero, and we cannot reject a zero effect at standard confidence levels.

We next turn to Delaware incorporation. Because Delaware corporate law already facilitates opt-in proxy access, the SEC rule might have had a smaller effect for Delaware companies.²⁶ We test this hypothesis by including the interaction of a dummy for Delaware incorporation and institutional ownership, as well as a dummy variable for Delaware incorporation. The coefficient estimate on the Delaware dummy itself is negative and significant. The interaction of the Delaware dummy with institutional ownership is positive and significant at the 10 percent confidence level. The different coefficients imply that non-Delaware firms saw value drop by 82 basis points for every 10 percentage points of activist ownership, while Delaware-incorporated firms dropped by only 30 basis points per 10 percentage points of activist ownership ($=0.1*(-819+522)$ basis points). Thus, the estimated effect of institutional ownership is much smaller for Delaware firms, consistent with our prediction.

We also examine at board structure, specifically board size. Yermack (1996) argues that smaller boards are more effective than large boards. If this is true, there may be *less* scope for improvement for firms with small boards, and so the proxy rule announcement return might be larger (i.e., smaller losses for firms that were already well managed). On the other hand, shareholder nominees might have more influence on a smaller board than on a larger board (even though the fraction of directors remains the same, at one-quarter), and so the withdrawn rule might have had *more* impact on firms with small boards. We test these competing hypotheses

²⁶ The same argument would also hold for North Dakota companies, where the corporate law since 2007 has provided mandatory proxy access for any 5% shareholder that has held their shares for at least two years. See Publicly Traded Corporations Act ch. 102, 2007 N.D. Laws 497, codified at North Dakota Cent. Code § 10-35-08. However, there are no North Dakota firms in the S&P 1500 sample.

for board size in column (4) of Table 5. The coefficient on the board size variable is positive and statistically insignificant, indicating that the value loss on October 4 did not depend on board size.²⁷

c. Investor heterogeneity: holding periods

We next examine the effect of institutional holding periods. The proposed SEC Rule would have given proxy access to investors whose stakes had been held for 3 years or more. We thus construct two additional measures of institutional ownership: the first measure (used in columns (2) and (5) of Table 6) is a measure of institutional ownership that includes only the institutional stakes that have been held for more than 3 years. The second measure is based on a weighting scheme, applying a (1/12) weight for holdings held for only 3 months, up through a (12/12) weight to holdings held for 12 quarters. Therefore, the variable puts progressively more weight on holdings that are closer to qualifying under the proxy rule. Columns (1)-(3) use the baseline measure of institutional ownership, the measure of three year old stakes, and the weighted measure. Columns (4)-(6) we use only activist investors, and apply the same three methods. Coefficient estimates are higher when we use the measures of ownership that control for holding duration, and as before borderline significant for overall institutions, and highly significant for activists. This is consistent with the market reaction on October 4 reflecting holding periods as well as the amount of institutional ownership. We cannot compare the various measures to each other in a horse race, because the measures are highly correlated with each other, however. What these results show is that the overall pattern of results is not sensitive to the details of how we construct the institutional ownership measures. Making an adjustment for

²⁷ We have replicated this finding with alternative measures of board size, such as the number of directors per million dollars of equity market value (unreported).

holding periods based on the details of the proposed Rule, if anything, raises the estimated economic magnitude of the results.

d. Lagged firm performance

The event study results presented so far have highlighted a strong relationship between ownership characteristics and firm stock price performance on October 4, 2010. These results are consistent with the details of the withdrawn SEC rule – which would have required large holdings, and holding periods of three years, for proxy access. Our final analysis looks at the relationship between lagged firm performance and the results we have described above. The scope for improvement by activist investors should vary across firms, and be related to firms' previous performance. We test this hypothesis by sorting firms based on variables related to recent performance: the end of 2009 book-to-market ratio (the ratio of equity book value to market value) and the stock return over 2007-2009. For each of these variables, we demean by Fama-French industry using all firms in the same the 48 industry classification. Our assumption is that poor performance relative to a firm's industry is a good proxy for the available scope of potential improvements. Table 7 presents the results of this exercise. Columns (1) and (2) split by 2007-2009 stock return; Columns (3) and (4) split by Market-to-Book ratios.²⁸ The impact of institutional ownership is without exception larger in firms with poor recent performance. The difference between the coefficient estimates in the subsamples is large but insignificant for both splits.

Figure 2 shows the results of a similar exercise. We split the sample into quintiles based on industry-adjusted 2007-2009 return, and then calculate regression coefficients on institutional

²⁸ Because we split by whether a firm is above or below average, not median, industry performance, and because we define averages for all Compustat firms, not just the S&P1500 group, the subsamples are not exactly of equal size. The logic of the test seems to suggest that the best possible split into strong and weak performers is more important than getting equal size samples. Splitting so that samples are equal size provides qualitatively similar results.

ownership within each subsample. The figure shows estimated coefficients as well as 95 percent confidence intervals. The estimated magnitude of the ownership effect generally falls with better lagged performance. This result is consistent with the notion that firms with poor performance had the most scope for improvement by activist investors and were therefore more likely to be affected by shareholder proxy access.

6. Conclusion

This paper uses a relatively clean natural experiment to assess the shareholder wealth implications of shareholder proxy access. Contrary to the prior event studies on proxy access, we find significant negative abnormal returns for companies that were most vulnerable to shareholder access on October 4, 2010, when the SEC unexpectedly delayed proxy access for U.S. public companies. This finding is consistent with the view that shareholder access, as manifested in the SEC's final Rule 14a-11, improves overall shareholder value. The difference between our result and earlier work may reflect different methodologies, and in particular the different natures of the events used. Our view is that the October 4 announcement makes a particularly useful event for empirical work because it was both material and unexpected.

The magnitude of this effect is economically significant. We find that firms that would have been most affected by proxy access, as measured by overall institutional ownership, lost 12 basis points of value for each standard deviation of ownership. For firms which had large ownership stakes held by historically activist institutions, the value loss was almost five times as large. This result suggests that boards of public corporations can be useful tools for mediating shareholder-manager agency conflict, when shareholders influence board appointments. The result highlights the importance of the process for nominating and electing directors.

This value loss is particularly striking because the event under examination creates only some probability (less than 1) of losing shareholder proxy access. To the extent that the market anticipated that the Business Roundtable challenge will not be successful, our results only measure the value loss from delaying shareholder proxy access by one year. That is, the overall value of shareholder proxy access is likely to be larger than what is captured in our event study.

Finally, our findings have important policy implications. Section 3(f) of the Securities Exchange Act of requires the SEC to consider whether certain proposed rules “will promote efficiency, competition, and capital formation.” Section 23(a) of the Act prohibits any rulemaking that would unnecessarily or inappropriately burden competition. The Administrative Procedure Act mandates that SEC rulemaking shall not be “arbitrary and capricious.” The findings in this paper suggest that the SEC’s Rule 14a-11 satisfies the requirements of the Securities and Exchange Act and the Administrative Procedure Act. By extension, the results presented in this paper suggest that the SEC’s Rule 14a-11 should survive, as a policy matter, against the Business Roundtable’s currently pending challenge.

7. References

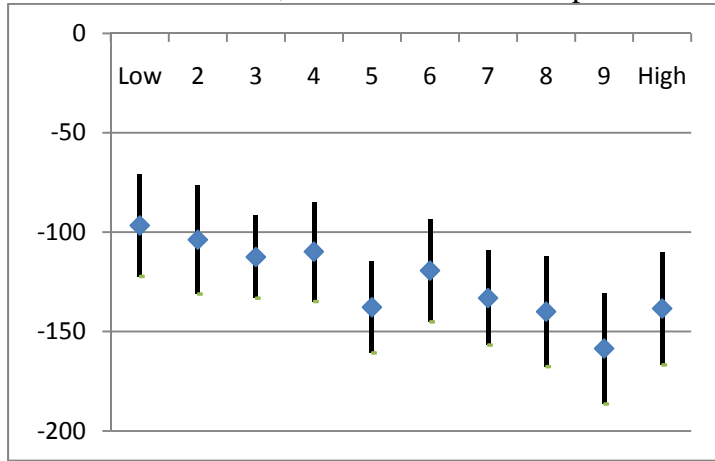
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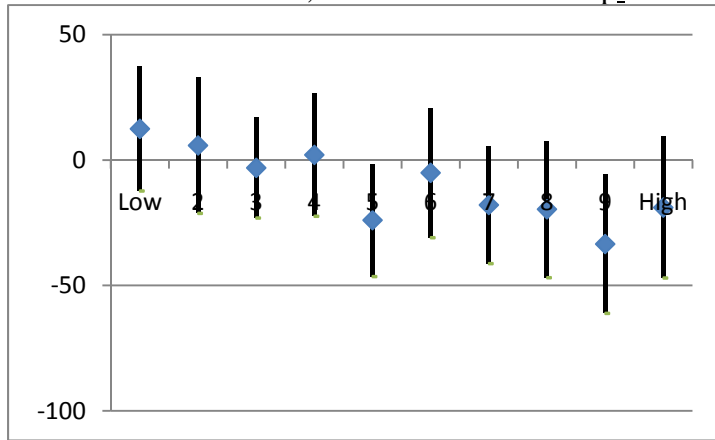
Figure 1. October, 4, returns by institutional ownership decile

The graphs show returns in basis points for firms in decile of institutional ownership or activist institutional ownership. 95% confidence intervals are plotted around each mean return, assuming independence.

Panel A. Raw returns, institutional ownership deciles



Panel B. Excess returns, institutional ownership deciles



Panel C. Excess returns, activist institutional ownership deciles

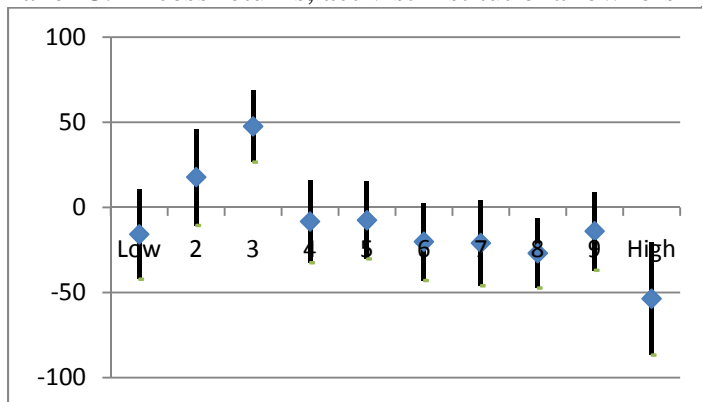


Figure 2. Regression coefficient of excess return on institutional ownership by quintile of industry-adjusted stock performance 2007-2009

The graphs regression coefficients from regressions of excess return on institutional ownership, estimated separately for each quintile of industry-adjusted 2007-2009 cumulative stock return. 95% confidence intervals are plotted around each mean return, based on robust standard errors. The confidence interval for the first quintile is [-1603,192] and for the last quintile [-784,199].

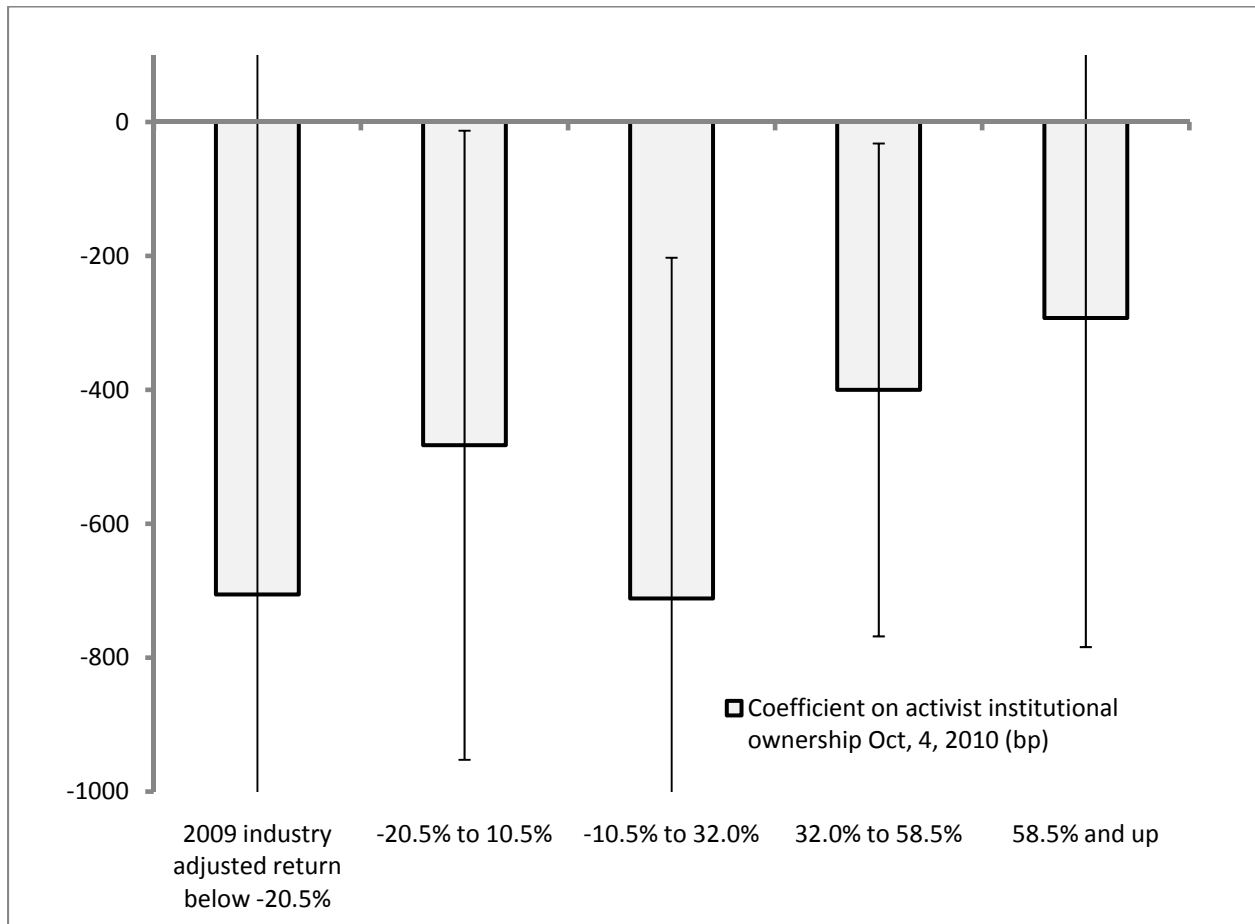


Table 1. Institutional ownership

This table summarizes the institutional ownership data for all firms in the S&P 1500 index. Actel, which experienced a merger announcement, is excluded. Ownership data is based on June, 2010 13(f) filings. Panel A reports average ownership by decile. Panel B reports summary statistics for various measures of institutional ownership

Panel A

Decile	Institutional ownership (June 2010), mean	Activist institutional ownership (June 2010), mean	Firms
1	24.6%	0.05%	145
2	37.9%	0.33%	144
3	42.2%	0.78%	145
4	45.4%	1.33%	144
5	48.4%	1.91%	145
6	51.0%	2.66%	144
7	53.8%	3.63%	145
8	56.9%	4.97%	144
9	61.3%	7.48%	145
10	69.5%	12.33%	144
All	49.1%	3.62%	1,445

Panel B

Variable	Mean	Std dev	10th percentile	Median	90th percentile	Observati ons
Institutional ownership, all	49.1%	12.6%	35.0%	49.8%	64.4%	1,445
Institutional ownership, activists	3.6%	4.0%	0.1%	2.3%	9.1%	1,445
Number of activist owners with at least 3%	0.32	0.57	0	0	1	1,445
Highest activist stake	2.52%	3.10%	0.12%	1.40%	6.69%	1,445

Table 2. Stock returns Monday, October 4, by institutional ownership

This table reports stock returns for S&P1500 firms by institutional ownership or activist institutional ownership decile for Monday, October 4, 2010. Actel, which experienced a merger announcement, is excluded. Only U.S. institutions are included. Return data is from Datastream, and measured in basis points. Excess return is the residual after regressing returns on betas from the Fama-French three factor model, with betas estimated over the first six months of 2010. Weighted average return is weighted by Market capitalization using outstanding shares of the first quarter 2010, from CRSP.

Decile	Equal weighted return, all institutions	Equal weighted excess return, all institutions	Equal weighted excess return, activist owners	Observations
Low	-96.6	12.5	-15.8	144
2	-103.8	5.8	17.8	144
3	-112.5	-3.1	47.6	145
4	-109.8	2.1	-8.3	144
5	-137.8	-24.0	-7.6	145
6	-119.3	-5.1	-20.2	144
7	-133.1	-17.9	-21.0	145
8	-140.0	-19.6	-27.0	144
9	-158.5	-33.5	-14.0	145
High	-138.4	-18.9	-53.7	144
Average	-125.0	-10.2	-10.2	1,445
Difference: 10 - 1	-41.8	-31.4	-37.8	
Difference: 10/9 - 1/2	-48.3	-35.4	-34.8	

Table 3. Regressions for stock returns Monday, October 4

The table reports regression of stock returns for October 4, on various controls. Return data is from Datastream, and measured in basis points. Actel, which experienced a merger announcement, is excluded. Any returns outside of [-0.3,0.3] are excluded. Excess return is the residual after estimating a Fama - French three factor model. Columns (5) and (6) use weighted returns based on Market capitalization, defined using outstanding shares of the first quarter 2010, from CRSP. Institutional ownership is measured in June 2010. Standard errors allow for cross-sectional correlation. * = statistically significant at 90% confidence; ** = 95% confidence; *** = 99% confidence.

Sample Returns	S&P 1500 Raw, EW (1)	S&P 1500 Raw, EW (2)	S&P 1500 Excess, EW (3)	S&P 1500 Excess, EW (4)	S&P 1500 Excess, VW (5)	S&P 1500 Excess, VW (6)
Institutional ownership	-127* (68.4)		-96.3* (57.4)		-157.4 (128.2)	
Activist institutional ownership		-552.5*** (186.3)		-514.7*** (159.7)		-589.0* (319.2)
Constant	-62.6 (168.5)	-105.0 (172.6)	37.1 (35.5)	8.4 (26.3)	-6.9 (7.5)	15.4 (37.0)
R-squared	0.010	0.020	0.006	0.018	0.006	0.004
N	1,445	1,445	1,445	1,445	1,423	1,423

Table 4. Regressions for stock returns Monday, October 4

The table reports regression of stock returns for October 4, on various controls. Return data is from Datastream, and measured in basis points. Actel, which experienced a merger announcement, is excluded. In column (6), any returns outside of [-0.15,0.15] are excluded. Excess return is the residual after estimating a Fama - French three factor model. In columns (1) to (5), only S&P 1500 firms are included. In column (6), all NYSE, AMEX and Nasdaq stocks with a Market capitalization above \$75 million are included. Column (3) uses weighted returns based on Market capitalization, defined using outstanding shares of the first quarter 2010, from CRSP. Institutional ownership is measured in June 2010. Standard errors allow for cross-sectional correlation. * = statistically significant at 90% confidence; ** = 95% confidence; *** = 99% confidence.

Sample	S&P 1500 (1)	S&P 1500 (2)	S&P 1500 (3)
Largest institutional stake	-95.5 (160.4)		
Largest institutional stake, activist		-644.1*** (218.3)	
Number of activist institutional owners above 3%			-33.8*** (10.2)
R-squared	0.001	0.017	0.018
N	1,445	1,445	1,445

Table 5. Regressions of excess stock returns Monday, October 4 on firm characteristics

The table reports regression of stock returns for October 4, on various controls. Return data is from Datastream, and measured in basis points. Excess return is the residual after estimating a Fama - French three factor model. The firm Actel, which experienced a merger announcement, is excluded. Only S&P 1500 firms are included. Institutional ownership is measured in June 2010. Staggered board is a dummy equal to one if the board is classified. G-index is the governance index of Gompers, Ishii and Metrick (2003), based on 2006 (the last date for which the components are reported). Delaware incorporation is a dummy equal to one if the firm is incorporated in Delaware. Board size is the log of the number of board members Standard errors allow for cross-sectional correlation. * = statistically significant at 90% confidence; ** = 95% confidence; *** = 99% confidence.

Sample	S&P 1500 (1)	S&P 1500 (2)	S&P 1500 (3)	S&P 1500 (4)
Activist institutional ownership	-514.0*** (159.5)	-461.2** (184.3)	-819.0*** (238.2)	-495.2*** (157.2)
Staggered board dummy	-3.3 (12.4)			
G-index		-0.0 (0.3)		
Delaware incorporation			-57.2*** (21.2)	
Delaware * Act. inst'l ownership			522.0* (283.8)	
Board size				43.2 (40.7)
R-squared	0.018	0.014	0.037	0.023
N	1,445	1,123	1,423	1,423

Table 6. Regressions of excess stock returns Monday, October 4: length of holdings

The table reports regression of stock returns for October, 4, on various controls. Return data is from Datastream, and measured in basis points. Actel, which experienced a merger announcement, is excluded. Excess return is the residual after estimating a Fama - French three factor model. Only S&P 1500 firms are included. Institutional ownership is measured for each of the twelve quarters ending in June 2010. Standard errors allow for cross-sectional correlation. * = statistically significant at 90% confidence; ** = 95% confidence; *** = 99% confidence.

Sample	S&P 1500 (1)	S&P 1500 (2)	S&P 1500 (3)	S&P 1500 (4)	S&P 1500 (5)	S&P 1500 (6)
Institutional ownership	-96.3* (57.4)					
Institutional ownership, three year old positions only ^a		-145.6 (118.8)				
Institutional ownership, holding period weighted ^b			-172.2* (95.8)			
Institutional ownership				-514.7*** (159.7)		
Institutional ownership, three year old positions only ^a					-736.2*** (233.7)	
Institutional ownership, holding period weighted ^b						-772.6*** (278.7)
R-squared	0.006	0.005	0.007	0.018	0.013	0.018
N	1,445	1,432	1,432	1,445	1,411	1,411

^a Measure of institutional ownership includes only positions held continuously for three years.

^b Measure of institutional ownership weights holdings according to duration continuously held: (1/12) weight for positions held for 1 quarter, (2/12) weight for positions held for 2 quarters, up to (12/12) weight for positions continuously held for three years.

Table 7. Regressions of excess stock returns Monday, October 4: by subsamples of industry-adjusted performance

The table reports regression of stock returns for October, 4, on various controls. Return data is from Datastream, and measured in basis points. Actel, which experienced a merger announcement, is excluded. Excess return is the residual after estimating a Fama - French three factor model. Only S&P 1500 firms are included. Institutional ownership is measured in June 2010. All performance is measured relative to the mean for the Fama-French (48) industry to which the firm belongs. The cut-off between “HIGH” and “LOW” is zero. Standard errors allow for cross-sectional correlation. * = statistically significant at 90% confidence; ** = 95% confidence; *** = 99% confidence.

Sample	S&P 1500 2007-2009 stock return is LOW	S&P 1500 2007-2009 stock return is HIGH	S&P 1500 Book-to- market is HIGH	S&P 1500 Book-to- market is LOW
	(1)	(2)	(3)	(4)
Activist institutional ownership	-668.7** (277.1)	-428.6** (176.0)	-696.5** (284.0)	-438.8*** (167.2)
R-squared	0.024	0.014	0.033	0.013
N	453	992	311	1,134