The mitigating effect of the market for directors on 'special interest' shareholder activism

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Abstract

The motivation and impact of labor union and public pension fund activism is widely debated. The labor and finance literature provides consistent and varied evidence that workers' interests as important stakeholders of the firm are not aligned with shareholders' interests. Thus, if workers can gain power in the firm through their dual role as a worker and a shareholder activist, this will likely result in a conflict of interest, with activist actions that do not benefit their fellow shareholders. We provide evidence that the labor market for directorships mitigates the negative effect of 'special interest' or conflicted activism on other shareholders. Directors who cater to special interests are punished with a loss in directorships and suffer damage to their reputation as corporate monitors, providing meaningful ex-ante incentives for directors to withstand the pressure of special interests. We find no evidence to support the criticism that public pension fund activism is politically motivated or 'labor-friendly'.

1. Introduction

The role of shareholder activism in mitigating the agency problem between managers and shareholders has increasingly gained the attention of corporate boards of directors, policymakers, and academics alike. In surveys of the literature, Ferri (2012) and Denes, Karpoff, and McWilliams (2015) divide this research into studies of the high-cost variety, where primarily hedge fund activists employ costly methods such as amassing large ownership stakes and conducting proxy contests for board seats, versus the low-cost variety, where activists express dissatisfaction by sponsoring non-binding shareholder proposals or withholding votes in director elections.[1]

Over the last two decades, by far the most prolific institutional investors employing "low-cost" activism strategies are labor union pension funds and public pension funds. Renneboog and Szilagyi (2010) report that these two investor types sponsored 38% of all Rule 14a-8 shareholder proposals in the 1996 to 2005 period, while Georgeson (2014) reports that they sponsored 38.2% of shareholder proposals in the 2014 proxy season. In recent years, their activism has extended to lobbying Congress and the SEC for controversial corporate reforms, most recently on the "Say-on-Pay" reform mandating shareholder votes on executive compensation and on fundamental changes to the director nomination and election process ("proxy access").

Their dominance among shareholder activists has been highly controversial and has led to much speculation as to their true motives. Critics argue that public pension fund activism is politically motivated, with pension officials more concerned with generating private benefits and publicity for themselves, perhaps for a future political campaign or consulting career, than with maximizing shareholder wealth (Romano, 1993, 2001; Woidtke, 2002; Sharfman, 2012). Similarly, union pension funds are often accused of using the shareholder activist platform as leverage toward gaining concessions from firms on behalf of their unionized employee members

[1]See Brav, Jiang, and Kim (2010) for a survey of the hedge fund activism literature.

(Bainbridge, 2006; Anabtawi and Stout, 2008; Grundfest, 2010). In fact, both activist types are commonly characterized as sharing similar 'labor-friendly' interests (e.g., Kahan and Rock, 2007; Cohn et al., 2012; proxymonitor.org). The official ruling by the United States Court of Appeals overturning the SEC's "proxy access" Rule 14a-11 in July 2011 criticized the SEC for not providing a serious evaluation of the "costs that could be imposed upon companies from use of the rule by shareholders representing special interests, particularly union and government pension funds."[2]

Labor union and public pension funds are often lumped together when it comes to concerns that their activism generates private benefits that arise at the expense of their fellow shareholders. The empirical evidence across several strands of the literature, however, suggests that a more nuanced view is appropriate. First, the labor and finance literature finds highly consistent evidence that workers' interests as important stakeholders of the firm are not aligned with shareholders' interests. Several studies find that as workers gain power either through a union, a sizable ownership stake, or board representation, firms implement less risky investment policies, increasing worker job security, but reducing shareholder wealth (e.g., John, Litov, and Young, 2008; Faleye, Mehrotra, and Morck, 2006; Lee and Mas, 2012; Lin, Schmid, and Xuan, 2015).[3] Second, because this worker-shareholder conflict arises within the firm, labor union activist activity should only represent a conflict of interest when they target firms where they simultaneously represent workers in collective bargaining negotiations. Thus, public pension funds, which do not represent any workers in the private sector, would not have a conflict of interest, nor would labor union pension funds if they are targeting non-unionized firms where they

[2] Business Roundtable and Chamber of Commerce v. Securities & Exchange Commission, No. 10-1305 (D.C. Cir. July 22, 2011) page 15.

[3] When workers also have an equity position there is a tradeoff between the effect on the value of the equity position and the value of the fixed claim of employees in the form of wages and benefits. Examining 5% or larger blocks of employee ownership, Faleye et al. (2006) show that the effect of the fixed claim component dominates and higher employee ownership is more aligned with the fixed claimants of the firm rather than with shareholders. The worker-activists in our sample have very small equity stakes, well below 5%.

have no other ulterior motive, such as a campaign for its workers to unionize. Previous findings either support a positive or neutral effect of public pension fund activism; to our knowledge no study supports a conclusion of a negative effect from corporate governance targeting by public pension funds (e.g., Del Guercio, Seery, and Woidtke, 2008; Woidtke, 2015; Wang and Mao, 2015).[4] All together, these findings lead to a prediction that only activists with a firm-specific conflict of interest ('special interest' activists) will pursue private gains from activism, and not every labor union and public pension fund.

In this paper, we ask whether the blanket criticism of these activist types is warranted, or whether instead the presence of a firm-specific conflict of interest better identifies the problem of special interest activism. In addition, we ask whether firms with strong corporate governance in place can effectively mitigate the negative effects of special interest activism on other shareholders. In particular, we hypothesize that the labor market for directorships can at least partially solve the problem of special interest activism. There is a large body of empirical evidence that directors are rewarded in the labor market for their services when taking actions consistent with shareholders' interests and punished when taking actions inconsistent with shareholders' interests. Rewards and punishments are measured by the change in the number of public company directorships a director accrues, as additional directorships provide incremental compensation, prestige, and social standing (Fama, 1980; Grundfest, 1993; Dyck and Zingales, 2002).

The previous literature consistently shows that the labor market for directorships is discriminating, such that only directors with shareholders' best interests in mind tend to be invited to serve on additional boards (Gilson, 1990; Kaplan and Rieshus, 1990; Coles and Hoi, 2003; Harford, 2003; Yermack, 2004; Srinivasan, 2005; Fich and Shivdasani, 2007; Fos and Tsoutsoura,

[4] Woidtke (2015) and Wang and Mao (2015) find that targeting by public pension funds on socially responsible topics is associated with negative valuation effects and political motives, but corporate governance targeting is not. Del Guercio et al (2008) find that activist targeting in the form of 'just vote no' campaigns is effective in compelling boards to fire underperforming CEOs and improve operating performance, and that this also holds for the sub-sample of firms targeted by public pension funds.

2013; Bereskin and Smith, 2014). If directors who give in to special interest activists suffer damage to their reputation as good stewards of shareholder value, this mechanism provides directors with ex-ante incentives to withstand special interest pressure.

To test whether the market for directors can mitigate special interest activism, we must observe a board decision where directors have the discretion to either withstand or succumb to special interest pressure. We use a sample of shareholder proposals that receive support from a majority of votes cast. These proposals typically request that the board implement a governance change, such as putting the poison pill to a shareholder vote or de-staggering the board. Because Rule 14a-8 shareholder proposals are legally non-binding, the board of directors must decide whether to implement the proposal once the vote outcome is revealed. Thus, we can observe whether the board chooses to ignore or comply with the activist's request. While boards' failure to implement shareholder proposals receiving a majority of vote support has been heavily criticized by investor groups, such as the Council of Institutional Investors, state law requires that directors alone have the fiduciary duty to use their judgment and potentially superior information to decide which governance structures are in the best interests of all shareholders.

We examine a comprehensive sample of shareholder proposals that receive a majority of vote support from 1996 to 2004. We identify the impact on a director's reputation for complying with special interest activists by comparing the effect to that of ignoring special interest activists, and also to that of complying with other non-special interest activists. We find that directors who comply with special interest sponsors lose 0.85 directorships on net within three years, the most common horizon studied in the market for directors literature. The difference in the loss of directorships, relative to directors who ignore special interest sponsors, is economically large; directors who ignore special interest sponsors lose 0.36 fewer directorships than directors who comply. In contrast to claims that public pension fund activism is self-serving or that they are 'labor-friendly,' we find no evidence that the market for directorships view complying with a

public pension fund activist negatively. If anything, we find that directors are rewarded for complying with, and punished for ignoring, a public pension fund sponsor. We conduct several robustness tests, including examining a sample of close-call proposals garnering votes cast between 45% and 55%. This close-call sample mitigates concerns that our evidence of punishment for directors complying with special interests is due to these activists choosing targets where boards might both be more likely to comply and more likely to suffer a loss in directorships (e.g., on boards of poorly performing firms). Overall, we find that punishment for directors who comply with activist shareholder requests is unique to the requests of special interest union activists.

Our finding that the market for directors mitigates the effect of special interest activism is consistent with the findings of Bertrand and Mullainathan (2003), Cronqvist et al (2009), and Atanassov and Kim (2009). These studies find that firms with strong corporate governance mechanisms in place can protect the interests of shareholders against managers' natural inclination to favor employee-stakeholders'. Common arguments in this literature suggest that managers' desire for "the quiet life" (e.g., avoiding conflict with unions or minimizing the effort required for tough negotiations) prevails under weak investor protections.

We also test and find support for quiet life incentives for boards to comply with the requests of special interest activists. Specifically, we find that the boards most vulnerable to special interest pressure are those facing especially poor union-firm relations and those with older directors where the average director is above the median age in the sample. These directors are the most likely to face unpleasant interactions with aggressive unions if they do not give in, and the most likely to choose peace and avoidance of unpleasant union strife over additional directorships. Consistent with this, we find that boards that comply with special interest unions enjoy significantly improved union relations in the year following compliance.

We contribute to the labor and finance literature by showing that employees can gain additional power over management even without a meaningful ownership stake, as SEC Rule14a-

8 allows shareholders with only minimal ownership to sponsor proposals. Indeed, we find average ownership among proposal sponsors is only 0.3%. In addition, while most studies in the literature use industry-level measures of unionization, we hand-collect firm-specific information from 10-k filings. Specifically, we collect whether a union represents employees at the firm or one of its subsidiaries in the year prior to the annual meeting with a majority vote proposal, and whether the specific union at the firm and the proposal sponsor are one and the same.

We also contribute to the literature on monitoring by the board of directors and the labor market for directorships as a corporate governance mechanism. We consider a new setting, whether favoring stakeholders over shareholders is punished with a loss in directorships. We find evidence consistent with the literature, suggesting that the director labor market provides meaningful ex-ante incentives for boards to make decisions in the interests of shareholders. Our findings also provide new insight into when this mechanism is weakest, namely when directors suffer from a horizon problem and have less concern about their reputations as monitors, such as when they reach the age when they no longer desire additional directorships.

Finally, we contribute to the shareholder activism literature by outlining the costs and benefits of activism by labor union and public pension funds. While it is problematic that the proxy rules can be exploited by special interest activists for private gain, this appears to be limited to cases where there is a firm-specific conflict of interest (activist shareholder also represents workers at the firm), and most of these conflicts are resolved via directors motivated by their reputation to use their discretion to ignore such self-serving requests. Thus, much of the activist activity by these sponsor types is aligned with the interests of their fellow shareholders.

2. Hypothesis development and empirical setting

2.1 Workers as powerful stakeholders not aligned with shareholders

The previous literature in labor and finance finds highly consistent evidence that when workers gain power as important stakeholders of the firm, their interests are not aligned with shareholders. Because workers are fixed-income claimants, holding a contractual claim on firms' cash flows in the form of wages and salaries, several studies show that they are aligned with the interests of other fixed-income claimants such as bondholders and banks, rather than with shareholders. John, Litov, and Yeung (2008) and Chen, Kacperczyk, and Ortiz-Molina (2011) both provide evidence for U.S. firms that as unions gain power firms take on lower risk investment projects. Faleye, Mehrotra, and Morck (2006) find similar results in a sample of U.S. firms where workers gain power through a 5% or greater equity stake in the firm. Interestingly, they find that even though these employees have both a fixed claim as a worker and a residual claim as a shareholder, they appear to use their power to tilt firm policies toward employee interests and away from maximizing shareholder value. Consistent with John, et al (2008) and Chen et al (2011), they find that firms with an employee blockholding have lower capital investment rates, lower R&D, lower operating risk, lower sales and employment growth, lower total factor productivity, and lower Tobin's Q. Moreover, Lee and Mas (2012) find that firms that undergo a successful union election and become unionized suffer shareholder wealth losses, and lower profitability and growth.

Lin, et al (2015) and Petry (2015) find consistent evidence in a sample of German firms, where workers gain power via national mandates that employees have equal representation on supervisory boards of directors if the firm has more than 2000 domestic employees. Using a regression discontinuity design around the threshold of 2000 domestic employees, Lin et al find that when employees have representation on the supervisory board, firm's capital structure and investment policies tend to be aligned with the interests of their lender banks; these firms have

lower capital expenditures, more stable cash flows, and lower idiosyncratic risk. Petry (2015) exploits the surprise announcement of the original 1976 German law to test for shareholder wealth effects for firms affected by the law. He finds a negative abnormal return of 1.8%, suggesting a conflict of interest between workers and shareholders.

Empirical evidence supports the conclusion that as workers increase their influence within the firm, either through a union, a sizable ownership stake, or board representation, firms implement less risky investment policies, increasing worker job security, but reducing shareholder wealth. We are not aware of any studies that find that shareholders' interests are served as worker power increases. Together, this suggests that shareholders' interests are not served when management and the board tilt firm policy toward the interests of other stakeholders.

2.2 Governance as a check on stakeholder power

Generally speaking, the literature discusses the favoring of worker interests over shareholder interests as failures of governance or poor investor protection. For example, Bertrand and Mullainathan (2003) show that when the discipline of the takeover market is removed via the adoption of state laws protecting firms from takeovers, worker wages increase, and productivity and profitability decrease. They hypothesize that managers acquiesce to workers and offer higher wages or tolerate lower productivity in order to "enjoy the quiet life" and have a harmonious and peaceful co-existence with workers. Thus, because of these quiet life private benefits, managers and boards may prefer to reduce bargaining effort and pay workers more than a wealth-maximizing shareholder would. Cronqvist et al (2009) provide consistent evidence and find that workers are more heavily favored and receive higher wages when the CEO's equity ownership is lower. They find that when the firm is faced with aggressive unions, where the personal cost to management to negotiate a lower wage bill is especially high, the effects are strongest. Thus, only when the CEO

personally bears the cost of lower equity values do they favor shareholders over workers, suggesting that managers succumb to quiet life incentives in the absence of financial incentives.

Atanassov and Kim (2009) in their cross-country study find that in the face of poor firm performance, there are significantly fewer employee layoffs and CEO turnovers when unions are strong and investor protection is weak, indicating that strong union laws increase job security not only for employees but also for underperforming managers. The common theme across these findings is that managers will find it beneficial to align with the interests of workers over shareholders in the absence of a strong governance mechanism to offset this. In this paper, we test for the role of a director's personal reputation and the market for directorships as a governance mechanism to provide a check on managers favoring powerful stakeholders over shareholders.

2.3 The problem of special interest (stakeholder) activism

In a shareholder activism context, the commonly stated concern is that the proxy rules allow workers to achieve private benefits and gain power to influence corporate policy. According to Rule 14a-8 of the Securities and Exchange Act of 1934, any shareholder that holds $2000 or more of stock for one year is eligible to submit a proposal and have it appear on the proxy that is distributed to shareholders at company expense. Thus, the proxy rules allow union pension funds to gain this stakeholder power through a very small ownership stake and at very low cost, assuming they are able to gain the vote support of other shareholders.

While critics tend to make general statements about potential private benefits of activism by both union pension funds and 'labor-friendly' public pension funds (Bainbridge, 2006; Anabtawi and Stout, 2008; Grundfest, 2010; Cohn et al 2014), the labor and finance literature suggests that there should only be a conflict of interest when shareholder activists and workers at the firm are one and the same. In other words, when a labor union shareholder targets a firm with a proposal where they simultaneously represent workers in collective bargaining negotiations, this

represents a conflict of interest within that firm, which we label 'special interest' activism. In contrast, because public pension funds do not represent workers in the private sector, their activism should not be motivated by this type of conflict of interest. Under this same logic, even labor union pension fund activists when targeting firms where they do not also represent workers do not have a conflict of interest.

Two labor union activism studies are exceptions in recognizing that the conflict of interest arises on a firm-specific basis. Ertimur et al (2011) find that ISS is less likely to recommend supporting a shareholder proposal, and vote support is lower, when a labor union sponsor also represents workers at that firm, suggesting that ISS and at least some shareholders recognize the conflict. Agrawal (2012) exploits the break-up of the AFL-CIO into two groups of unions in 2005 to identify implications of the firm-specific conflict of interest. He finds that when labor union shareholders also represent workers they tend to withhold votes against directors in elections, which he finds to subsequently result in better union relations at the firm after the vote. After the break-up, however, the withholding of votes behavior changes toward more vote support for directors, but only at the firms where the union no longer represents workers at that firm. He interprets his findings as worker-shareholders using their voting power to pressure directors toward favoring the union to the detriment of shareholders' interests. We build on these findings by exploring the role of a corporate governance mechanism in mitigating these firm-specific conflicts. In the spirit of Bertrand and Mullainathan (2003), Cronqvist et al (2009), and Atanassov and Kim (2009), we ask whether directors are sufficiently motivated to resist the pressure of special interest activism in order to preserve their personal reputations as good stewards of shareholder value.

2.4 Does the labor market for directors have a mitigating effect on special interest activist power?

Fama (1980) and Fama and Jensen (1983) first suggested that the labor market for directors can align their incentives with shareholders. There is a substantial literature providing empirical

support for the ex post settling-up hypothesis, which predicts a link between director performance on the job and future opportunities in the form of additional public company directorships (Kaplan and Reishus, 1990; Gilson, 1990; Brickley et al., 1999; and Yermack, 2004). Specifically, poor director performance is punished via a devaluation of the director's human capital, or reputational damage.

Gerety and Lehn (1997), Harford (2003), Coles and Hoi (2003), Srinivasan (2005), Fich and Shivdasani (2007), Fos and Tsoutsoura (2013), and Bereskin and Smith (2014) find strong support for the hypothesis that the market for directors discriminately punishes directors whose actions reveal themselves to be poor monitors, or to be more aligned with managers than shareholders. For example, Fich and Shivdasani (2007) find that outside directors at firms sued for financial fraud (who presumably failed to monitor management) experience a fifty percent reduction in external directorships in the three years following the lawsuit. The interpretation is that directors observed to make poor decisions consequently either lose board appointments at other firms at which they sit or are subsequently invited as a new board member less frequently. A net loss in directorships provides a disciplinary mechanism, as it will mean a loss of director compensation and/or social standing (Grundfest, 1993; Dyck and Zingales, 2002), and thus, improved ex-ante incentives for directors.

A limitation of this approach in interpreting additional directorships as a reward is that we can only observe the number of directorships accepted and not the number of directorships offered (e.g., Kaplan and Reishus, 1990). In addition, it is also possible that CEOs control director selection and that CEOs prefer directors who are willing to rubber stamp management decisions and not diligently monitor. However, there has been no empirical support for this alternative hypothesis that 'poor' directors are rewarded with additional directorships. Instead, there is consistent empirical evidence in a variety of settings that directors lose directorships if they make decisions that are not in shareholders' interests. For example, this has been consistently shown in

varied applications such as the revelation of fraud (Gerety and Lehn, 1997; Srinivasan, 2005; Fich and Shivdasani, 2007), opting in favor of protection from takeovers (Coles and Hoi, 2003), resisting a takeover bid despite poor performance (Harford, 2003), and involvement in an option backdating scandal (Bereskin and Smith, 2014).

2.5 Empirical setting to observe director decision-making: Majority vote shareholder proposals

In the previous section, we summarize the substantial empirical support for the hypothesis that the labor market for directors is well-functioning and discriminating. We would like to know whether this governance mechanism can at least partially solve the problem of special interest activism. In order to test this, we need to identify an event where the board is faced with a decision to favor either stakeholders' or shareholders' interests. If boards comply with activist demands to the benefit of all shareholders, we expect them to be rewarded with more external directorships. But if instead they simply give in to special interest pressure to enjoy the quiet life and buy peace with the union, then we expect they will be punished in the director labor market with a net loss in directorships.

We use a sample of non-binding Rule 14a-8 shareholder proposals that receive a majority of vote support at the annual meeting as our observable board decision point for several reasons. First, shareholder proposals make a very specific request to the board, such as 'de-stagger the board,' so it is unambiguous what decision activists are asking the board to consider. Second, the timing and outcome of the decision is known to market participants. If the board had already decided that the request is beneficial to implement, then the proposal would not have appeared on the proxy statement to be voted on by shareholders. Because the proposal is either implemented or not after the shareholder vote, there is a direct link between the activist request and the board decision. Furthermore, the vote outcome and subsequent board decision is easily verifiable and is indeed tracked by the Council of Institutional Investors and Institutional Shareholder Services

(ISS), presumably because it is of interest to investors. Importantly, relative to a sample of all shareholder proposals, majority vote proposals have a meaningful probability of being implemented. Ertimur, Ferri, and Stubben (2010) report that only 3.2% of proposals with votes below 50% were implemented by the board, while 23.9% of proposals were implemented for vote outcomes between 50% and 60%.

A less obvious characteristic of majority vote shareholder proposals is important for the validity of our study design. Namely, we assume that not *all* shareholder proposals that receive a majority of vote support would increase value if implemented. Brownstein and Kirman (2004), Bainbridge (2006), and Alexander and Honaker (2008) argue that shareholder proposals are non-binding for good reason, and that the corporation should not be run by referendum. Directors alone have a fiduciary duty under state law to exercise their business judgment and decide what governance structure is value-maximizing for the firm. Shareholders, in contrast, can vote as altruistically or selfishly as they please. Thus, on any given issue up for a vote, directors have a greater incentive to make an informed decision relative to the typical diversified shareholder.

Brownstein and Kirman (2004) argue that in recent years, several forces have combined to increase the frequency of majority vote proposals and to render them noisier signals of the true intensity of shareholder preferences. Beginning in 2003, SEC regulations require mutual funds, which collectively own about one-quarter of the equity of U.S. public companies, to disclose voting policies describing their stance on issues that typically come up for a vote, as well as to disclose their individual voting records.[5] To efficiently comply with these requirements, many funds subsequently either outsourced their voting to third-party proxy consultants, such as ISS, or developed issue-based voting rules, such as 'vote in favor of all shareholder proposals to de-stagger the board'.[6] Brownstein and Kirman argue that this has led to both "rote policy voting in lieu of

[5] Interestingly, the AFL-CIO made the original request to the SEC to consider a mutual fund proxy vote disclosure rule (*The Washington Post*, April 8, 2001, p H1).

[6] The Department of Labor, which oversees pension plans under ERISA, has long made clear that voting rights are considered pension assets, and as such, pension trustees have a fiduciary duty to vote in the best interests of

case-by-case analysis (p. 45)" and substantial influence of proxy consultants over vote outcomes. The empirical literature supports both of these arguments.

Several studies find that ISS recommendations are influential and can sway 6 to 20% of the votes cast in corporate elections.[7] Because ISS recommendations are also somewhat predictable, proposal sponsors can easily game the system; majority vote support is practically guaranteed with carefully chosen proposal topics in firms with high institutional ownership, independent of its merits at that particular company. Under this view, a proposal that receives support of a majority of the votes cast is not necessarily in the best interests of all (non-activist) shareholders.

Iliev and Lowry (2015) find support for the argument that ISS has an incentive to minimize costs by issuing 'blanket recommendations' whereby they recommend to vote in favor of a proposal topic for all firms, rather than analyze the issue on a firm-specific basis. For example, in their sample of mutual fund votes from 2006-2010, they find that ISS recommends voting in favor of shareholder proposals to put the golden parachute severance agreement to a shareholder vote 100% of the time.[8] In contrast, they find that the mutual funds with the greatest incentive to make informed votes, such as those from large fund families, support these same proposals only 61% of the time. More importantly, they find that proposals that pass have higher abnormal returns upon passage when the incentivized mutual fund voters support them, and lower abnormal returns when

beneficiaries. (See the DOL's 1988 "Avon letter.") Thus, institutional investor demand for third-party proxy services, such as that of ISS, precedes the mutual fund vote disclosure regulation. These plans typically have written voting policies or follow proxy consultant recommendations, similar to mutual funds.

[7] For example, Cai, et al. (2009) find votes in director elections are 14 to 19% lower when ISS recommends that shareholders withhold their vote for that director. In contrast, Choi et al. (2010) find that ISS independently controls only 6 to 13% of the vote. They argue that the difference from Cai et al. is because they account for firm- and director-specific factors that ISS clients would base their vote on in the absence of an ISS recommendation. Thus, they argue that the influence of ISS is overstated when one does not account for the factors that influence both ISS' recommendation and shareholder votes.

[8] Morgan et al. (2001) provide similar evidence of blanket recommendations in their 2004-2005 sample. For example, they find that 100% of shareholder proposals on the topic of de-staggering the board and 86% of shareholder proposals on the topic of submitting the poison pill to a shareholder vote received an ISS recommendation to vote in favor and that these proposals received 90% and 78% of votes in favor on average, respectively. Examining the incentives and influence of proxy consultants is a topic of increasing regulatory and academic interest.

proposals these mutual funds support fail to garner a majority vote. They do not find similar valuation effects for ISS recommendations, which suggests that firm-specific factors, which presumably are best known and understood by the firms' board of directors, are likely important in determining the value-maximizing action in any given situation. For example, even though removing takeover defenses are generally viewed to be in the best interests of shareholders, there are well-known exceptions. For example, Cen et al. (2011) and Johnson et al. (2013) find that takeover defenses are beneficial and should not be removed for firms with important long-term relationships with suppliers or customers who would otherwise find relationship-specific investment unattractive.

In sum, we should observe punishment in the form of a loss of directorships for boards that comply with special interest activists motivated by private benefits, and rewards of additional external directorships for boards that comply with activists that are aligned with the interests of other shareholders.

2.6 Data on majority vote shareholder proposals

Our final sample of 610 majority vote shareholder proposals from 1996 to 2004 comes from two main sources, the Council of Institutional Investors (CII) and the Investor Responsibility Research Center (IRRC) (now ISS). The CII is an investor group founded in 1985 to promote best practices in corporate governance. The membership is primarily union and public pension funds but also includes corporate pension funds. One issue that has consistently remained on the CII's agenda for over a decade is corporate boards that fail to implement a shareholder proposal despite a majority of votes cast in favor of that proposal. Every year the CII sends a letter to the boards of directors at companies receiving a majority of vote support requesting that the proposal be implemented, tracks the company response, and tabulates a summary available to its member pension funds (prior to 2004 this summary was available publicly on its website).

We use the CII's annual list containing the firm, proposal topic, proposal sponsor, and whether the company implemented the proposal from 1998 to 2004 as a starting point in collecting our sample. We supplement this with company responses from ISS and data on shareholder proposals from the IRRC Corporate Governance Bulletin. When ISS documents a response and CII does not, we conduct a search to verify the correct response. From ISS and IRRC, we add data on the percentage of votes cast, 49 proposals from 1996 and 1997 (years not covered by CII), and 12 proposals from 1998 to 2004 that do not appear on the CII list. We determine board responses for these added proposals by examining press announcements, proxy statements, and 10-k filings in the subsequent year. We identify 643 proposals from 1996 to 2004 and are able to obtain the necessary data on 610 proposals.

We obtain the share ownership of the proposal sponsor directly from corporate proxy statements. In 416 proposals the proxy discloses the sponsor name and share ownership. In the remaining cases, the proxy statement states that this information is only available upon request. While the IRRC Corporate Bulletin lists proposal sponsors in these cases where the company does not disclose sponsor information in the proxy statement, they do not provide sponsor ownership information. Thus, sponsor ownership is missing whenever the company does not disclose it in the proxy statement.

2.7 Majority vote shareholder proposals: summary statistics and compliance rates

Before testing whether the market for directorships mitigates the effect of special interest activism, we present summary statistics on our sample of majority vote proposals and the subsequent board response in Table 1. The header of Table 1 contains detailed variable definitions and data sources. The first column of Panel A shows that unconditionally over our sample period, majority vote shareholder proposals have a 17.7% probability of the board responding by fully complying with the activist request before the next annual meeting. The average proposal receives

63.5% of votes cast in favor, and the average proposal sponsor owns only 0.26% of shares outstanding. Using primarily information reported in 10-k filings, we report the percentage of proposal targets where the firm has a unionized workforce. Although we check the robustness of our results to an alternate definition of a unionized workforce, we report results where we define a firm as unionized if any of its employees are subject to collective bargaining agreements.[9] We find that 69.8% of majority vote proposals are at unionized firms. Finally, for the subsample of unionized firms, we report a summary score based on variables from the KLD SOCRATES database as a measure of the state of union-management relations in the year prior to the annual meeting. This variable ranges from -1 to 1, with a -1 indicating poor relations, 0 indicating neutral, and +1 indicating excellent relations, with an overall sample mean of -0.04.[10]

2.8 Identifying 'special interest' activists with conflicts of interest at target firms

Within proposals at unionized firms sponsored by union pension funds, we also determine whether the sponsor is the same umbrella union representing some or all of the target firm's employees ("dual role" sponsor). In 1997 the AFL-CIO created an Office of Investment to coordinate corporate governance efforts on behalf of its member unions (Jacoby, 2008).

[9] We use unionization data from Ertimur, Ferri, and Muslu (2011) for firms that overlap in our samples and thank these authors for generously sharing their data. We then supplement this for missing firms using the same data sources and variable definitions described in Appendix 5 of their paper. Specifically, we primarily use 10-k filings but also consult F-7 filings from the U.S. Department of Federal Mediation and Conciliatory Service (FMCS) available from their website when information is missing from the 10-k. The National Labor Relations Act requires employers or employees' representatives to file a report 60 days prior to the termination or modification of a collective bargaining agreement. This filing provides the firm name, union name, bargaining unit size, and notice date. We also check the robustness of our results to an alternate definition of a unionized firm, such as 5% or more of employees are subject to collective bargaining agreements. Our results are qualitatively similar under these definitions.

[10] Specifically, the union relations score is computed as Union Relations Strengths minus Union Relations Concerns. KLD assigns a score of either 0 or 1 at calendar-year ends based on their analysts' review of company news, filings, or other public sources. Union Relations Strength =1 if "the company has taken exceptional steps to treat its unionized workforce fairly", and =0 otherwise. Union Relations Concerns = 1 if "the company has a history of notably poor union relations", and = 0 otherwise. Because the union relations score is defined as strengths minus concerns, a 1 indicates excellent relations, a zero is neutral, and a -1 indicates poor relations. KLD assigns scores for publicly-traded firms in many categories of interest to their institutional investor clients focused on socially responsible (Environmental Social Governance) issues. Recent papers using KLD data to study labor and finance issues include Landier et al. (2009) and Bae et al. (2011).

Consequently, we consider a proposal that is sponsored by the AFL-CIO or one of its members to be a dual role proposal if one of the firm's employee collective bargaining agreements is with an AFL-CIO member union.[11] Because of the centralized nature of the AFL-CIO's targeting activity and its broad reach in terms of its large array of member unions, we find that a "dual role" sponsor and a labor union sponsor of a proposal at a unionized firm is effectively the same thing. For example, we find that 19% of majority vote proposals are sponsored by dual role union pension funds and a slightly higher 21.1% of majority vote proposals are sponsored by union sponsors at unionized firms. Thus, for ease of exposition we will define 'special interest' sponsors with a firm-specific conflict of interest as labor union sponsors at unionized firms, but we note that our results are robust to using the narrower definitions of a 'dual role' union sponsor, such as whether the exact same member union sponsors the proposals and represents workers at the target firm.[12]

2.9 Majority vote statistics by sponsor type, topic, year of vote, and repeat proposal status

The next columns in Table 1 Panel A report statistics by sponsor type, including separate columns for special interest union funds and union funds targeting non-unionized firms. Combining these two, union funds sponsor 32.8% of all majority vote proposals, while public pension funds sponsor 7.4%. Renneboog and Szilagyi (2010) report that these sponsor types represent 33% and 4.8% of all shareholder proposals that came to a vote from 1996 to 2005, suggesting that public pension funds have disproportionately more success in garnering majority vote support. Interestingly, special interest sponsors comprise the majority of union sponsored

[11] We also consider an alternate definition where we require an exact match between a specific union sponsor and a specific collective bargaining agreement (e.g., Sheet Metal Workers must be both the sponsor name and the union name under that firm). The results are qualitatively similar under either definition.

[12] Technically we also include one proposal sponsored by CalPERS in 2004 under the special interest category. In 2004 Sean Harrigan, a long-time leader of the United Food & Commercial Workers Union, became the President of CalPERS. CalPERS was heavily criticized in the press for favoring union interests under his leadership and his presidency lasted only a short time. Only one CalPERS sponsored proposal received majority vote support while he was in office.

proposals with majority vote support, suggesting that they are often able to gain the support of other shareholders despite the vote penalty documented by Ertimur et al (2011). In addition, the board compliance rate of 29.1% is significantly higher than all other sponsors at the 1% level. The average ownership of special interest sponsors (0.02%) is smaller than the other sponsor types, but it is possible that their ownership is underestimated due to their use of external portfolio managers who report holdings separately.[13]

By construction, special interest proposals are at unionized firms but it is notable that union relations at these firms are significantly poorer relative to unionized firms of other sponsor types. The mean union relations score for special interest targets is -0.13, which is significantly different from the average score of other sponsor types at the 1% level. A magnitude of -0.13 is also large relative to the overall sample in that it represents 31% of the standard deviation from the mean score of -0.04. Finally, the last row supports our earlier statement that a dual role sponsor and a union sponsor at a unionized firm are effectively the same, as 90% of proposals in the special interest category are from dual role sponsors.

The next set of columns provide statistics by proposal topic. Seventy-three percent of all majority vote proposals request that the board either remove the poison pill or staggered board or put its removal up for a binding shareholder vote. Relative to other proposal topics, these two types have significantly lower full compliance rates of approximately 13%.[14] In contrast, proposals on the topic of executive compensation have the highest compliance rate of 31.5%, despite also having the lowest average vote support of 58.8% (both significantly different from

[13] For example, the document "Facts about the AFL-CIO's Proxy Votes" explains that they sponsor shareholder proposals using their Reserve Fund, not subject to ERISA.

[14]Full compliance excludes cases where the company agreed to let the poison pill expire but reserved the right to adopt a new plan without shareholder approval in the future if the board decides that it is in the best interest of shareholders to do so. Based on press reports and the fact that companies tend to receive additional poison pill proposals in the year following the compromise, we infer that activists do not consider this board action as a satisfactory response to their request. In our tests we pool these compromises with ignoring activists' requests, but we note that our results are not sensitive to how we treat compromise responses.

other proposal categories at the 1% level). Interestingly, nearly half of executive compensation proposals are sponsored by dual role union sponsors, a result we explore further in later analysis.

We also present summary statistics for an early (1996-2000) versus later (2001-2004) period. As noted by Ertimur et al. (2010) and Renneboog and Szilagyi (2010), shareholder proposals have enjoyed increasingly higher average vote support over time. This is evident in the increase in the number of majority vote proposals from 188 in the earlier period (representing 19.7% of all shareholder proposals, untabulated) to 422 in the later period (35.4% of all shareholder proposals). Even within majority vote proposals, we find significantly higher vote support (64.4% vs. 61.6%) in the later sample period, but the compliance rate is not significantly different.

Finally, in the last two columns, we present summary statistics for the number of times a proposal receives majority vote support. Four hundred and fifteen proposals, or 68% of the sample, receive majority vote support for only one year, indicating it is the first time the proposal receives majority vote support. In the remaining 32% of proposals, the company had a proposal on the same topic receive majority vote support in the previous year. We find significantly higher vote support but lower compliance rates for repeat targets. In our tests, we consider whether or not the firm is a repeat target.

Table 1, Panel B contains the number of majority vote proposals by sponsor type, cross-tabulated with proposal topic, time period, and repeat target status. Special interests sponsor more executive compensations proposals than other types, while 80% of public pension fund sponsored proposals are concentrated in removing or voting on a staggered board. Over half of the proposals sponsored by special interest union funds request the dismantling of anti-takeover provisions, which might seem counter-intuitive given that employee layoffs and restructurings often accompany takeovers. Results in the literature, however, suggest that firms with employees who own significant stock in the firm or that are unionized are less likely to be acquired (Rauh, 2006; Chen et al., 2012; Tian and Wang, 2015). These authors suggest that employee stock ownership

or unionization is an effective substitute for traditional takeover defenses, reducing the concern that the firm would be taken over if defenses were removed. It is also possible that special interest activists favor anti-takeover proposals simply because the topic tends to garner high vote support.

3. Empirical Analysis on Directorships

3.1 Director reputation effects of director decision making

In this section we test whether a well-functioning labor market for directorships mitigates the effect of special interest activism. In particular, our main interest is to test whether the reputational effect of a given board decision (e.g., comply with activist request) varies by whether the proposal sponsor has a conflict of interest at the target firm. An advantage of our test is that because we are measuring the effect on a target director's reputation in the form of directorships gained or lost at *other external firms*, the effects are arguably exogenous to the target firm.

3.1.1 Director-level univariate tests of reputation effects

To conduct our tests we identify all non-employee directors at the time of the annual meeting where the proposal garnered a majority vote using the IRRC (now ISS) director database from 1996 to 2007. We compute the director's net change in the number of external public company directorships for the three subsequent annual meetings after the majority vote (years +1, +2, and +3). We use proxy statements and searches in Lexis-Nexis to identify board seats in cases where this information is missing from the IRRC database. In our analysis we adopt three practices that are standard in the market for directors literature. First, we examine the effects up to three years following the event, in part because staggered board elections are a common governance structure. Second, we exclusively analyze the reputational effect on outside directors and not on insiders, as these are the directors charged with monitoring management and ensuring that decisions are made in the best interests of shareholders. Finally, we examine the change in external directorships for

the sub-sample of outside directors that have at least one external board seat, as directors serving on no other boards cannot lose an external seat. For brevity, we refer to the sub-sample of outside directors with one or more board seats as simply 'directors' in the remainder of the paper.

Table 2 Panel A contains a univariate comparison of changes in external directorships for sub-samples according to director response within sponsor type categories. Specifically, for each proposal sponsor category, we report the results of a two-sided t-test for differences in the mean change in directorships between directors who comply with the activist request versus directors who ignore the request. For completeness, we also report the average changes in directorships for the full majority vote sample, which includes 3,710 targeted outside directors who hold 2.25 external directorships on average at the time of the annual meeting when the majority vote occurred (year 0).

Overall, we find evidence consistent with the hypothesis that directors who comply with special interest sponsors representing employee stakeholders are perceived as not acting in the best interests of shareholders. Despite a very similar number of average directorships at year 0, we find a significantly greater loss of directorships over both two and three years, at the 5% and 1% level respectively, when directors comply with special interest sponsors relative to when they ignore their requests. Moreover, this result contrasts with directors who comply with union sponsors at non-unionized firms, as we find no significant difference at these horizons when directors comply versus ignore at these firms. (Although, we do find weak evidence at the one-year horizon that directors who comply with activists at non-unionized firms are also punished.)

Relative to the literature, the effects we find for complying with special interest activists are economically large. We find that directors who comply with special interest sponsors lose 0.852 directorships on net within three years, the most common horizon studied in the market for directors literature. The difference in the loss of directorships, relative to directors who ignore special interest sponsors, is economically large; directors who ignore special interest sponsors lose

0.36 fewer directorships on net than directors who comply with special interests. Whether the punishment for catering to special interests is viewed in a relative or absolute sense, the magnitude equals or exceeds that found in the literature using major events associated with lax monitoring or poor stewardship of shareholders' interests. For example, the average absolute change in external directorships ranges from -0.2 to -0.5 for studies of the revelation of fraud (Srinivasan, 2005; Fich and Shivdasani, 2007), opting in favor of protection from takeovers (Coles and Hoi, 2003), or having a board seat challenged in a proxy contest (Fos and Tsoutsoura, 2013).

In stark contrast, we find that directors who comply with requests from public pension funds experience significant net *gains* in external directorships relative to directors who ignore their requests, but the difference is only significant at the one- and two-year horizons. Similarly, directors who comply with requests from Other sponsors experience a significantly greater net change in external seats in two of the three horizons. The magnitudes here are also economically significant, as directors who comply with public pension fund or Other sponsors lose 0.23 to 0.26 fewer directorships than directors who ignore these sponsor types, indicating that directors are punished for *ignoring* non-special interest activists.

While the reputational effect between boards' decisions to comply with the activist request differs substantially across sponsor types, this is possibly due to some other reason besides punishment for complying with special interest activists. For example, special interests may systematically choose target firms that are both more likely to comply and more likely to have directors suffer a loss in directorships, such as firms with especially poor performance or governance. Cunat et al (2012) show that while firm governance, performance, and ownership characteristics significantly differ across shareholder proposals that do and do not receive a majority of vote support, there are no significant differences across firms within a narrow band of close-vote outcomes, within 5% of the 50% threshold. They argue that proposal passage within this close-vote sub-sample is locally exogenous, mitigating selection bias concerns.

Thus, to check the robustness of our results we also report statistics using a sample of special interest sponsored proposals with votes in favor between 45% and 55%, which we label the close-call proposal sample. We find that the magnitude of the loss in directorships for board compliance with special interest activists is -0.895 in proposals that barely pass (50 to 55% vote support), which is quite similar to the -0.852 in the full sample. The results are also quite similar for the proposals the board ignores, -0.49 in the full sample and -0.459 in the barely pass ignored sub-sample. Similar to the full sample, we find that the loss in directorships is significantly greater for directors who comply with special interest activists relative to directors who do not. Importantly, we find that firm and director characteristics of targets are ex ante similar whether the special interest sponsored proposal passes by a close margin or whether it fails by a close margin, validating that our tests address selection bias concerns. (See the Internet appendix for tests comparing firm and director characteristics across these close-call sub-samples.)

Table 2 Panel B contains the results of two-sided t-tests directly comparing the average change in net directorships of special interest sponsors to those of other sponsor types. For example, the first set of results in the last column of Panel B tests whether the average three year change in directorships is significantly different for directors who comply with special interest sponsors relative to directors who comply with other categories of sponsors. We find in Panel A that the direction of the result is always the same; complying with special interest activists implies a greater loss in directorships than complying with any other sponsor type. Panel B shows that all comparisons are statistically significant at the two- and three-year horizon. We also report a comparison relative to all other non-special interest sponsors pooled and find the differences are significant at the 1% level. We conclude that the effect on a director's reputation is very different when complying with a conflicted activist relative to any other type.

The next set of results in Panel B compare the average change in directorships where directors ignored special interest sponsors to those where the directors ignored other sponsor types.

Once again, the results are strongest at the three-year horizon. Generally speaking, the results suggest that directors receive greater punishment when ignoring the requests of public pension funds and other sponsors, including all non-special interest sponsors as a group; the three-year loss in directorships is significantly different from ignoring special interest sponsors in each case. Note that we would not necessarily expect the effect on directors of complying or ignoring to be symmetric. Because the vast majority of shareholder proposals are ignored, taking no action may be more of a non-event than the higher visibility, less ambiguous, and relatively rare event of complying with an activist request.

Finally, in the last set of test results in Table 2 Panel C we examine the sub-sample of directors who comply with special interests where the proposal received between 50 and 55% of the vote (barely-passed proposals). In support of our earlier results, this sub-sample is not significantly different from the larger sample of special interest proposals where the board complied, but is significantly different from both the special interest proposals that barely failed (votes between 45% and 49%) and the proposals where the board complied with all other non-special interest sponsors. Thus, our conclusion that directors who give in to special interest pressure are punished holds in tests designed to avoid the selection bias problem. We further examine the robustness of these results in a multivariate setting in the next section.

3.1.2 Director response and reputation in the market for directors: multivariate analysis

Table 3 columns (1) and (2) contain the results of an ordinary least squares regression where the dependent variable is the change in the number of other public company directorships held by the director over the one- and three-year horizons, respectively, following a majority vote proposal. In the remaining columns, we include additional specifications that are variations on the net change in external directorships measure. Specifically, we include probit regression estimates of the probability that a director experiences a net loss in external directorships in the one year and

in the three years following majority vote support in columns (3) and (4). We also include analogous probit regression estimates of the probability that a director experiences a net gain in external directorships in columns (5) and (6).

We aim to test whether our finding of director punishment for complying with special interest activists is robust to a multivariate analysis. Thus, the main variable of interest is a dummy variable equal to one if the director is on a board that complied with a proposal sponsored by a special interest activist, and equal to zero otherwise. In all specifications, the omitted category is a dummy variable equal to one if the director is on a board that did not implement the requested action in a majority vote proposal sponsored by special interest activists, so the estimated effects are relative to directors who choose to ignore special interest activists' requests. We also include separate dummy variables indicating all other proposal-sponsor-by-board-response categories. We compute robust standard errors corrected for firm-level clustering and report the corresponding p-values.

We control for the following year 0 director characteristics: age (between 65 and 69, or over 69), tenure, number of external public company directorships, gray designation, gender, committee membership, and chair of committee designation. We control for the following firm characteristics: natural log of previous calendar year-end market value of equity, prior fiscal year-end leverage, prior calendar year market-adjusted stock return, and the market-adjusted stock return from year 0 to +1 (or 0 to +3 for the three-year specifications), beginning in March of year 0. We begin in March to include the annual meeting for most firms. Consistent with the literature, directors who are older and sit on more boards experience a lower net change in external directorships. We additionally find that directors serving on audit committees experience a greater net change in external directorships. Similar to Ertimur et al. (2010), we find that the one-year change in the number of seats is negatively related to market-adjusted performance during the year after the annual meeting, although the effect on the three-year change is no longer significant.

Ertimur et al. interpret the negative relation as being potentially driven by directors of firms with positive abnormal performance choosing to focus their board service on their well-performing firm and less on external boards.

We generally find support for the hypothesis that directors are punished in the external labor market for complying with special interest activist requests. We find that the three-year net change in directorships is significantly more negative for directors complying with a request by a special interests, relative to directors ignoring these activists. Furthermore, the magnitude of the coefficient suggests a sizable incremental decrease of nearly one-third of a directorship within three years, consistent with the univariate results. Consistent with this, we find directors complying with special interests are significantly less likely to have a net gain in directorships relative to directors ignoring special interests. In contrast, we do not find punishment for complying with other sponsor types. Although, consistent with the univariate results, we again find weak evidence at the one-year horizon that directors who comply with union activists at non-unionized firms are also punished.

Relative to the effect of ignoring special interest activists, directors are both rewarded with additional directorships for complying with public pension funds and punished with a loss in directorships for ignoring their requests. We find a significant increase in net directorships and a decrease in the probability of losing a directorship in the one year after a director complies with a public pension fund sponsored proposal. Moreover, the net three-year change in directorships is significantly negative and the probability of a one-year loss in directorships is significantly higher when directors ignores public pension funds. These results consistently support the interpretation that complying with public pension funds is in the interests of shareholders. Recall that approximately 80% of the majority vote proposals sponsored by public pension funds are to de-stagger the board, a highly visible action when the board complies. Further, Bebchuk, Cohen, and Farrell (2009) find that staggered boards are associated with lower firm value, and Guo, Kruse,

and Noel (2008) find a shareholder wealth gain upon the announcement of the boards' intention to de-stagger the board. Thus, a reward for complying with public pension fund requests is consistent with the findings of these papers. Finally, we find no significant incremental effects for either complying with or ignoring Other sponsors.

3.1.3 Robustness tests for director reputation effects

In this section, we repeat the analysis of Table 3 on three separate samples to confirm the robustness of our results. It is possible that the market for directors views the response to repeat majority vote proposals and first time majority vote proposals differently, or that the first response reveals new information about director quality. To investigate this, the first sample deletes repeat proposals and only includes first-time majority vote proposals. In this case, the omitted category in the regressions is the same as in Table 3, directors from boards who choose to ignore special interest activists' requests.

In the second sample, we include control directors at firms matched to majority vote target firms on the basis of both firm-size (sales) and recent market-adjusted stock performance. Thus, instead of comparing directors who all received proposals with majority vote support but were targeted by different sponsor types, we now compare targeted directors to non-targeted directors at firms with similar size and past performance. We report the details of our matching procedure in the header to Table 4. In this case, the omitted category in the regressions are all non-targeted control directors.

Finally, the third sample is the close-call sample of directors at firms with proposals sponsored by union pension funds and vote outcomes between 45% and 55%. In this case, the omitted category is directors at firms with proposals that receive between 45% and 49% and do not pass, as well as directors at non-unionized firms with proposals sponsored by union pension

funds. We note that we are missing information on director committee assignments for the sample of proposals with votes below 50%, so drop these control variables in the close-call specifications.

Table 4 contains the results of regressions using these three samples. For brevity, we only report results for the main horizon of interest, the three-year change in directorships. In general, we find that our main results are robust, and in some cases stronger in these alternative samples. Taken together, the results are consistent with the view that directors who comply with special interest activists are punished in the external market while directors who ignore them are not. In contrast, directors complying with majority vote requests by public pension fund sponsors are rewarded with a greater net gain in external seats. Under the premise that the director labor market is well-functioning, we interpret our findings as evidence that public pension fund interests are aligned with other shareholders, while special interest activists seek private benefits for their unionized employee members. Consistent with the market for directors literature, directors complying with conflicted activists are punished as a form of ex-post settling up and damage to the value of the director's reputation for not acting in the interests of shareholders. Through this mechanism, directors generally have improved ex-ante incentives to represent shareholders.

3.2 When are boards most vulnerable to special interest pressure?

In this section, we explore the circumstances under which boards are most vulnerable to pressure from special interest activists. The literature suggests there are likely to be two opposing forces at work. First, the labor and finance literature finds that managers' and boards' desire for the quiet life is especially strong when faced with aggressive, vocal, and persistent worker grievances. Second, the logic underlying the market for directors suggests that the incentive to be good stewards of shareholder value should be strongest when directors care the most about damaging their personal reputations, at points in their career when they have the greatest desire to attract additional directorships. Combining these two arguments leads to a prediction that directors

will comply with special interest activists 1) when the firm's own employee-shareholders are applying the pressure, 2) when there is strife and poor relations in the workplace, and 3) when directors are at the end of their careers and no longer actively seek directorships.

To examine these predictions, we begin by comparing rates of compliance with majority support proposals by whether the firm has a unionized workforce, both for the sample as a whole and for each sponsor type. Consistent with the "quiet life" hypothesis, Table 5 Panel A reports significantly higher compliance rates for unionized firms only in the case where the sponsor is a union pension fund (special interest activist with a conflict of interest). Specifically, of firms targeted by union pension funds, only 7.1% of boards comply at non-unionized firms, while the compliance rate is over twenty percentage points higher, 29.4%, at unionized firms. This difference in compliance is significant at the 1% level. In contrast, for the sample as a whole and for other sponsor types, there are no significant differences in compliance rates between unionized and non-unionized firms, suggesting that the unionized status of the firm only affects the board's decision when the sponsor is a union.

To further examine whether a "quiet life" interpretation is warranted, we test whether the compliance rate is significantly higher when directors face contentious union negotiations and are closer to retirement age. Specifically, we test whether boards are more likely to comply with the stakeholder-activist when management-union relations are poor and when the average age across the firm's non-employee directors is above the sample median (59.9 years). We define poor union relations as a union relations score of -1 in the year prior to the annual meeting, using the KLD database as described in Table 1. We conjecture that as directors approach retirement the benefits of the quiet life potentially outweigh the costs of the damage to their reputations as vigilant corporate monitors.

In Table 5 Panel B we report the mean compliance rates for these categories. We find that boards of firms targeted by special interest activists with poor union relations comply with the

proposal 42.1% of the time, relative to 26.9% of the time for all other special interest targets. While the economic magnitude of the difference in compliance rates is large (15 percentage points), the difference is not statistically significant (p-value of 0.18), possibly due to the small sample size. In a comparison of special interest target firms with directors above and below the sample median, we find that targets with older directors comply with the proposal 36.4% of the time, relative to 21.3% of the time for targets with younger directors, with the difference significant at the 10% level. Both of these results support a quiet life interpretation for board compliance.

We additionally find that special interest target firms comply with 46.8% of compensation related proposals but only 18.8% of non-compensation related proposals, statistically different at the 1% level. This fits the prediction of Matsusaka and Ozbas (2013) whereby union activists might strategically pick proposal topics that management cares a lot about, such as their compensation, in order to provide a credible threat that they will apply more pressure if side payments are not made to them (e.g., employee benefits).

In Panel C of Table 5 we examine whether these results extend to a multivariate analysis. We report estimates of a probit regression where the dependent variable equals one if the board complies with the request in the majority vote proposal, and zero otherwise. Although they do not examine the impact of a special interest sponsor, Ertimur et al. (2010) examine the determinants of compliance with majority vote proposals. They find that the percentage of vote support, proponent ownership, and the sponsor and proposal type are significant determinants of compliance. We include these variables and find similar signs and significance for most variables. Specifically, compliance is significantly more likely for proposals with higher vote support and higher proponent ownership. We also find results generally consistent with the univariate results in Table 1. Proposals to remove takeover defenses have lower average compliance rates, while first-time majority vote proposals have higher average rates. We include an additional control for recent firm performance as a proxy for alternative pressure on directors, but it is not significant.

In untabulated results we also include two-year changes in institutional ownership, but it is also never significant. The omitted dummy variable in the probit regression is equal to one if the proposal sponsor is in the Other category.

Consistent with the univariate results in Table 5 Panel A, whether or not the firm is unionized is generally negatively related to compliance, but in column (1) we find that when the firm is unionized *and* the sponsor is a special interest union activist, the coefficient is positive and significant at the 1% level. Columns (2) – (6) add control variables for proposal topic. The special interest sponsor dummy loses significance, suggesting that the higher probability of compliance for special interest sponsors may be driven by the sub-sample of target firms where unions can potentially exert more pressure. Consistent with this, we find a significant positive coefficient for special interest sponsor interacted with compensation related proposals, but not for the interaction with non-compensation related proposals. The marginal effects indicate compliance is 21.5 percentage points greater for compensation related proposals by special interest sponsors, but is only significantly greater than the coefficient for the non-compensation related interaction in a one-tailed test. Consistent with the univariate results, we generally find that boards are not more likely to comply with public pension fund sponsors.

In columns (4) and (5) we test whether boards are more likely to comply with a special interest sponsor when union relations in the prior year have been poor and when directors are older, as predicted by the quiet life hypothesis. We find that the coefficient on the interaction terms is only positive and significant when firms targeted by special interests have poor union relations in the prior year or when the average age of independent directors is above the median.[15] Even though the coefficient is larger when union relations are poor (and the unreported marginal effect is 20 percentage points greater), it is only statistically greater than the coefficient when union relations

[15] It can be difficult to interpret the marginal effect of interaction terms in a nonlinear model (e.g., Norton, Wang, and Ai, 2004); however, graphs of the interaction effects generally support that the effect on the probability of compliance is positive and significant across nearly all firms when we report a significant positive interaction term.

are not poor in a one-tailed test. We find similar results in testing coefficients for director average age interactions in column (5). However, when we interact special interest sponsor with *both* poor union relations and older directors in column (6), the marginal effects indicate the probability of compliance is 53.6 percentage points greater and the coefficient is significantly greater (p-value = 0.05) than the coefficient for special interest interacted with no poor union relations and older directors.

In untabulated results, we also examine the interactions with special interest sponsor and compensation related proposals, separately combined with poor union relations and director age. We find the interaction of special interest and compensation proposal topic is only significantly positive for target firms with older directors. Moreover, the positive coefficient is significantly greater (p-value = 0.03) than the coefficient when special interest compensation proposals are at firms with younger directors.

In sum, our results are consistent with the view that boards are more likely to comply with special interest sponsors who are likely to aggressively and persistently target the firm due to their interests as unionized employees, consistent with a quiet life motivation for compliance. In the next section, we test whether special interest sponsors and the employees they represent tend to benefit from applying public pressure to boards.

3.3 Do directors who comply with unions enjoy the quiet life? Changes in management-union relations following majority vote shareholder proposals

Our evidence so far is only suggestive that union employees benefit from union pension fund activism, possibly at the expense of shareholders. Ideally, we would like to directly measure whether employees benefit from union activism in the form of higher wages or better healthcare or retirement benefits in the next collective bargaining agreement. However, these data are not

generally available.[16] However, KLD updates the union relations score annually, allowing us to measure the change in union relations from before to after the proposal year. Specifically, for the sub-sample of unionized firms, we compute the change in the union relations score from one year prior to the annual meeting to one year after the annual meeting. This change in score theoretically ranges from -2 to +2, with a positive score indicating that union relations improve, a negative score indicating worsening relations, and a zero indicating no change. However, the sample minimum and maximum are -1 and +1, suggesting that we do not observe any firms changing from excellent to poor, or vice versa, within two years. The mean change over all proposal firms is -0.01, with a standard deviation of 0.24.

For each proposal sponsor category, Table 6 reports the mean union relations score in the year prior to the annual meeting and the change in score from year -1 to year +1 by whether the board ignored or complied with the activist sponsor's request. Consistent with Table 5 Panel B, we find that the boards that comply tend to be at firms with the poorest union relations in the year prior to the annual meeting. We find that the mean union relations score is -0.123 for firms with boards that comply, relative to a mean score of -0.022 for firms with boards that ignore activists' requests, with the difference significant at the 10% level. Similarly, 16.9% of firms with boards that comply have poor union relations, relative to 8.7% of firms with boards that ignore activists' requests, a difference significant at the 5% level. Also consistent with Table 5, firms with boards who comply with special interest sponsors have even poorer union relations on average, with a mean score of -0.194, and nearly 22% of these firms have poor relations before the annual meeting, in contrast to the other sponsor types. We note, however, that union relations are poor for almost all targets of special interest sponsors and not significantly different if the board either ignores or complies with the request. This suggests that special interest sponsors intentionally target boards

[16] For example, total wages are reported as a separate item by only a small number of Compustat firms. Only 17.5% of our sample firms report wages separately from aggregate expenses reported under Selling, General, and Administration (SG&A).

when union relations are contentious, which is consistent with the findings of Agrawal (2012). He finds that union pension funds that represent the firm's employees are more likely to withhold votes in a director election during times of union strife.

Of greater interest is whether union relations improve following compliance with an activist request, relative to if the board ignores the activist request. For each sponsor type, the bottom three rows of Table 6 present changes in score from -1 to +1. For the sample overall, and for the sub-sample of special interest sponsors, we find that the mean change in union relations score is significantly higher for firms with boards that comply relative to firms with boards that ignore the activist request, indicating relative improvement in union relations when boards comply. In contrast, for public pension or other sponsors the difference in the mean change in score is not significant. Interestingly, comparing the percentage of firms with worsening relations reveals that the special interest sponsor result is driven by union relations significantly worsening in firms that ignore special interest requests. About 10% of the firms whose boards ignore special interest union requests experience worsening relations, relative to none of the firms whose boards comply with them.

In the sample overall, union relations improve on average, and 5.6% experience improving relations when boards comply. The mean change in score is 0.042, which is both statistically different from the mean change at firms that ignore requests (-0.023), and economically large, representing 18% of the standard deviation of the change in score. Overall, we conclude that union relations at unionized firms clearly improve when boards comply relative to when boards ignore activist requests and refuse to implement the proposal. The labor and finance literature finds that this is not a good thing for shareholders. For example, Faleye and Trahan (2011) also use the KLD score and find that employee and firm productivity falls as the union relations score improves, consistent with unions using bargaining power to extract leisure.

4. Conclusion

Labor union and public pension funds are by far the most active among institutional shareholders adopting "low-cost" activism strategies. Recently, their activism has extended beyond shareholder proposals to lobbying Congress and the SEC for controversial corporate reforms. Their dominance among shareholder activists has been highly contentious and has led to speculation as to their true motives. While it is inherently difficult to infer an agent's motivation, based on findings of the labor and finance literature, we hypothesize that activism motivated by private benefits arises whenever there is a firm-specific conflict of interest. Namely, the activist shareholder is conflicted if they are also a stakeholder in the target firm, such as when a labor union pension fund activist also represents workers in collective bargaining negotiations in that same firm. We find that the term 'special interest' activism is most appropriately applied to instances of firm-specific conflicts.

We find that directors who comply with the requests of special interest activists experience a significantly greater net loss in external board seats than either directors who ignore such requests, or than directors who comply with the requests of other activist types. Thus, the punishment for directors who cater to special interests suggests that the labor market for directorships serves as a corporate governance mechanism that mitigates the negative effects of special interest activism on non-activist shareholders.

We find that directors are especially susceptible to union-activist-stakeholder pressure, or equivalently the incentives from the market for directorships are weakest, when directors have countervailing incentives for the "quiet life." Boards are more likely to comply with special interest union activists when management-union relations are especially poor, and when directors are closer to retirement age. We also find that union relations improve in the year after boards comply with these activists, but deteriorate further after boards ignore the activist request, suggesting that boards can achieve a quiet life by catering to conflicted union activists. Given our

finding that these directors are subsequently punished with a net loss in directorships, we conclude that the labor market for directors provides meaningful ex-ante incentives for directors to withstand the pressure from employees and other stakeholders to take actions that are not in the best interests of shareholders.

In contrast to special interest union sponsors, we find no evidence that directors who comply with requests by public pension funds are punished, and instead find that these directors are rewarded with additional directorships. We find public pension fund sponsors to be the only activist type associated with both rewards to directors for complying with their requests and punishment for ignoring them, suggesting that public pension fund officials are not deserving of the criticisms that their activism is motivated by private benefits or 'labor-friendly' sentiment.

We also contribute to the debate on regulatory changes, such as Say on Pay and proxy access, that shift power to shareholder activists and away from boards of directors. Frictions in proxy voting, such as the recent rise of rote, issue-based voting policies in lieu of firm-specific analysis, imply that not every issue that garners a majority of vote support is in the best interests of all shareholders. We find that potent, low-cost activist tools combined with proxy voting frictions can make managers and boards vulnerable to pressure from employee stakeholders, to the detriment of other shareholders in the firm. This finding supports the argument that corporations should not be run by referendum; decision power should reside with the directors, who have fiduciary duties to make decisions in shareholders' interests (Dooley, 1992; Bainbridge, 2010).

Yet, we also find that pressure for governance changes from other non-special interest activists, such as public pension funds, are consistent with shareholder interests, suggesting that the consequences of these shifts of power are multifaceted and nuanced, rather than strictly good or bad for shareholders. Anabtawi and Stout (2008) advocate that one solution to the problem that a shareholder might use her influence to promote a governance change to extract private benefits is to hold her to a fiduciary standard similar to the one applied to corporate directors. Under this

solution, additional shareholder decision-making power is coupled with additional responsibilities, and with legal liability for self-serving actions. One less extreme solution in this spirit would require the shareholder activist to disclose any material conflict of interest, such as the activist also represents the firm's employees in collective bargaining. Our results imply that such disclosure might discourage self-serving activism, without discouraging the value-enhancing variety.

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Table 1. Majority vote shareholder proposals (1996-2004)

This table reports the frequency of majority vote shareholder proposals, defined as a Rule 14a-8 proposal where the percentage of votes cast is greater than or equal to 50%. We obtain data on majority vote proposals from the Council of Institutional Investors annual list and the IRRC (now ISS) shareholder proposal database. Proposal sponsors are classified as either a "Special Interest" or a "Non-Special Interest" sponsor. The Special Interest category includes sponsors that also represent some or all of the target company's employees under collective bargaining. Specifically, Special Interest sponsors include labor union pension fund sponsors at unionized firms and the public pension fund CalPERS at unionized firms during 2004 (the latter is only one observation). Non-Special Interest sponsors include labor union pension fund, public pension fund, and other sponsors that do not also represent employees at the target firm. Within Non-Special Interest sponsors, the Other sponsor type includes individuals and private investor groups. Proposal topics include 1) remove or vote on poison pill, 2) remove or vote on the staggered board, 3) change or vote on executive compensation (includes expense stock options at time of grant and vote on golden parachutes, pension benefits, and executive compensation structure), and 4) Other (e.g., confidential voting, majority of independent directors on board, eliminate supermajority voting, restore shareholders rights to a special meeting). A majority vote proposal is categorized as full compliance if the board fully complies with the request of the proposal before the next annual meeting. % vote support is the percentage of votes cast in favor of the proposal. Sponsor ownership % is the percentage of shares outstanding of the target firm owned by the proposal sponsor(s). The number of shares owned by the proposal sponsor is disclosed along with the sponsor's statement in support of the proposal in the proxy statement. 416 out of the 610 proposals disclose share ownership information. The others state that this information is available to those requesting it from the company. Our data source contains information when the proposal sponsor name is missing from the proxy, but does not have the missing ownership information. The ownership means below are based on 416 proposals with available information. A firm is categorized as Unionized if any of its employees belong to a union as reported in the 10-K in the year prior to the annual meeting. F-7 filings are used to supplement information from the 10-k when union information is missing. We supplement unionization data we received from Ertimur et al. (2011), using the definitions and procedure outlined in their Appendix 5. We obtain data on union relations from the KLD SOCRATES database (now called MSCI ESG STATS). The union relations score is computed as Union Relations Strengths minus Union Relations Concerns. Each calendar-year end KLD assigns a score of either 0 or 1 based on their analysts' review of company news, filings, or other public sources. Union Relations Strength =1 if "the company has taken exceptional steps to treat its unionized workforce fairly", and =0 otherwise. Union Relations Concerns = 1 if "the company has a history of notably poor union relations", and = 0 otherwise. Thus, the union relations score has a minimum of -1 (poor relations) and a maximum of 1 (excellent relations), and we report summary statistics only for the unionized target firms, as non-unionized firms would all have scores of 0. We have union relations data for 396 of 424 proposals at unionized firms. "Dual role" unionized firms indicate cases where the proposal sponsor is a union pension fund that represents some or all of the employees in collective bargaining negotiations at the proposal target firm. We consider a proposal that is sponsored by the AFL-CIO or one of its member unions to be a dual role proposal if the target firm has an employee collective bargaining agreement with one of AFL-CIO's member unions. We consider the proposal sponsor Longview Fund to be affiliated with the UNITE union based on information from their website. We obtain information on the specific unions at proposal firms from either the 10-k filing on EDGAR or F-7 filings reported on the U.S. Department of Federal Mediation and Conciliatory Service (FMCS) website. ***, **, * indicate the results of a two-sided t-test for differences in means of targets in a particular column to that of targets in all other columns within the same grouping (e.g., mean full compliance rate of targets of special interest sponsors relative to that of all targets of other sponsor types).

Table 1. Majority vote shareholder proposals (1996-2004) (continued)
Panel A. Compliance rates, votes in favor, and unionization status of target firms by sponsor type, proposal topic, year of vote, and whether repeat proposal

		Sponsor Type				Proposal Type				Year of Vote		Receives majority vote proposal	
			Non-special Interest sponsor										
	All	Special Interest sponsor	Union pension fund (non-unionized firm)	Public pension fund	Other sponsor	Poison pill	Staggered board	Executive Compensation	Other	1996 -2000	2001 - 2004	Once	More than once
Number of proposals	**610**	129	71	45	365	210	233	89	78	188	422	415	195
Number full compliance	**108**	38	5	12	53	26	32	28	21	28	79	82	25
Full compliance%	**17.7**	29.1***	7.1**	26.7*	14.6**	12.5**	13.7**	31.5***	27.6**	15.1	18.8	19.8**	13.0
Vote support %	**63.5**	62.3	61.6*	65.0	64.2*	65.7***	63.5	58.8***	63.3	61.6	64.4***	62.1***	66.5
Sponsor Own %	**0.26**	0.02*	0.01	0.52	0.39*	0.65***	0.10*	0.02	0.22	0.41	0.20	0.38**	0.02
Unionized firm %	**69.8**	100.0***	NA	51.1***	75.1***	71.4	74.2*	58.4**	65.4	67.0	71.1	66.0***	77.9
Union relations score	**-0.04**	-0.13***	NA	-0.02	0.00***	-0.01	-0.05	-0.14*	0.00	-0.01	-0.05	-0.05	-0.02
Dual role unionized firm %	**19.0**	89.9	NA	NA	NA	15.7	14.2**	49.4***	7.7***	22.3	17.5	20.5	15.9

Table 1. Majority vote shareholder proposals (1996-2004) (continued)
Panel B. Number of majority vote proposals by sponsor type, proposal topic, year of vote, and repeat proposals

	Proposal Topic				Year of vote		Receives majority vote proposal	
Sponsor Type	Poison pill	Staggered board	Executive Compensation	Other	1996 -2000	2001 -2004	Once	More than once
Special Interest sponsor	37	38	47	7	46	83	97	32
Non-Special Interest sponsor								
Non-unionized firm*Union sponsor	21	13	34	3	20	51	61	10
Public pension fund sponsor	2	36	0	7	24	21	38	7
Other sponsor	150	146	8	61	98	267	219	146

Table 2. Univariate analysis of the net change in external directorships

Panel A. T-tests for differences in the net change in directorships for directors who comply versus for directors who ignore the activist, by sponsor type

Panel A reports two-sided t-test results for differences in the mean change in external directorships between compliance and board ignores for each subgroup, where ***, **, * indicate significance at the 1%, 5%.10%.

	Year 0	(Year 0 to 1)	(Year 0 to 2)	(Year 0 to 3)
All majority vote proposal firms:	2.25 (N = 3710)	-0.201 (N = 3695)	-0.409 (N = 3687)	-0.581 (N = 3676)
Special Interest sponsor (compliance):	2.24 (N = 218)	-0.281 (N = 217)	-0.567** (N = 217)	-0.852*** (N = 216)
Special Interest sponsor (board ignores):	2.26 (N = 529)	-0.192 (N = 527)	-0.395 (N = 527)	-0.490 (N = 527)
Non-unionized firm*Union sponsor (compliance):	1.92 (N=48)	-0.333* (N=48)	-0.277 (N=47)	-0.277 (N=47)
Non-unionized firm*Union sponsor (board ignores):	2.05 (N=402)	-0.138 (N=398)	-0.303 (N=396)	-0.448 (N=393)
Public pension fund sponsor (compliance):	2.43 (N = 58)	0.155*** (N = 58)	-0.069** (N = 58)	-0.534 (N = 58)
Public pension fund sponsor (board ignores):	2.40 (N = 167)	-0.271 (N = 166)	-0.479 (N = 165)	-0.824 (N = 165)
Other sponsor (compliance):	2.18 (N = 314)	-0.208 (N = 312)	-0.309** (N = 311)	-0.392*** (N = 311)
Other sponsor (board ignores):	2.29 (N = 1958)	-0.208 (N = 1953)	-0.441 (N = 1950)	-0.621 (N = 1943)
Special Interest sponsor (Barely Pass compliance):	2.08 (N=38)	-0.158 (N=38)	-0.395 (N=38)	-0.895** (N=38)
Special Interest sponsor (Barely Pass board ignores):	2.15 (N=123)	-0.123 (N=122)	-0.311 (N=122)	-0.459 (N=122)
Special Interest sponsor (Barely Fail: non-majority vote):	2.30 (N=148)	-0.166 (N=145)	-0.229 (N=140)	-0.390 (N=136)

Table 2. Univariate analysis of the net change in external directorships (continued)

Panel B. T-tests for differences in the net change in directorships for directors within the same board response category (comply or ignore) but across sponsor types

Panel B reports p-values for the results of a two-sided t-test for differences in means of target directors in a particular sub-group to other target directors within the same grouping (e.g., mean net change for target directors complying with special interest sponsors relative to that of other target directors complying with the sponsor type listed in the row).

	Year 0	**(Year 0 to 1)**	**(Year 0 to 2)**	**(Year 0 to 3)**
Special interest sponsor (compliance):	p-value	p-value	p-value	p-value
vs. Non-unionized firm* Union sponsor (compliance)	0.111	0.650	**0.054**	**0.004**
vs. Public pension fund sponsor (compliance)	0.380	**0.000**	**0.001**	**0.094**
vs. Other sponsors (compliance)	0.595	0.300	**0.002**	**0.000**
vs. all non-special interest sponsors (compliance)	0.624	0.102	**0.000**	**0.000**

	Year 0	**(Year 0 to 1)**	**(Year 0 to 2)**	**(Year 0 to 3)**
Special interest sponsor (board ignores):	p-value	p-value	p-value	p-value
vs. Non-unionized firm* Union sponsor (board ignores)	**0.023**	0.308	0.194	0.626
vs. Public pension fund sponsor (board ignores)	0.297	0.285	0.388	**0.003**
vs. Other sponsor (board ignores)	0.671	0.677	0.396	**0.038**
vs. all non-special interest sponsors (board ignores)	0.985	0.800	0.608	**0.058**

Table 2. Univariate analysis of the net change in external directorships (continued)

Panel C. T-tests for differences in the net change in directorships for directors who comply with special interest activists at firms with close-call proposals (vote outcomes between 45% and 55%)

Panel C reports two-sided t-test results using the directors targeted by special interest sponsors where the vote outcome of the proposal was between 45% and 55%, which we label the Close-call sample. The Barely Pass sub-sample contains directors targeted by special interests where the vote outcome was between 50 and 55%. The Barely Fail sample contains directors targeted by special interests where the vote outcome ranged from 45% to 49%. P-values for the results of a two-sided t-test for differences in means of target directors in the Barely Pass compliance sample compared to the other sub-samples listed in each row are reported.

	Year 0	**(Year 0 to 1)**	**(Year 0 to 2)**	**(Year 0 to 3)**
Special interest sponsor (Barely Pass compliance):	p-value	p-value	p-value	p-value
vs. Special interest full sample (compliance)	0.378	0.259	0.218	0.814
vs. Special interest sponsor (Barely Fail: non-majority vote)	0.351	0.959	0.351	**0.013**
vs. all non-special interest sponsors (compliance)	0.635	0.917	0.4554	**0.013**

Table 3. Analysis of the net change in other public company directorships, and lost or gained directorships of outside directors following a majority vote proposal

Columns (1) and (2) contains estimates from an OLS regression of the change in external public company directorships from year 0 to year +1 or year 0 to year +3 for a sample of outside directors for target firms with a majority vote proposal. The omitted category is special interest target firms where the board ignored the activist request. Director characteristics are measured in year 0 and are from the IRRC director database, or if missing, from proxy statements. Directors of target firms that are acquired or bankrupt are included. Directors who die before the next annual meeting are set to missing. Columns (3) and (4) contains probit regression estimates of the probability that an outside director experiences a net loss in external directorships within one year and three years of the annual meeting of the majority vote proposal and columns (5) and (6) contains the analogous estimates for directorship gain within three years of the annual meeting. P-values, reflecting robust standard errors corrected for firm-level clustering, are in parentheses. ***, **, * indicate significance at the 1%, 5%, and 10% levels.

	Net Change in number directorships		**Directorship loss**		**Directorship gain**	
	(0 to +1)	**(0 to +3)**	**(0 to +1)**	**(0 to +3)**	**(0 to +1)**	**(0 to +3)**
	(1)	(2)	(3)	(4)	(5)	(6)
Special interest * compliance	-0.05	-0.32**	0.07	0.24	-0.20	-0.35**
	(0.501)	(0.021)	(0.536)	(0.117)	(0.202)	(0.047)
Non-unionized * Union sponsor * compliance	-0.15	0.01	0.23*	-0.09	-0.51	0.12
	(0.162)	(0.968)	(0.081)	(0.591)	(0.208)	(0.478)
Public pension sponsor * compliance	0.31**	0.02	-0.44*	0.10	0.26	0.20*
	(0.048)	(0.888)	(0.087)	(0.674)	(0.404)	(0.080)
Other sponsor * compliance	-0.02	0.08	0.12	-0.11	0.08	0.17
	(0.739)	(0.377)	(0.199)	(0.333)	(0.534)	(0.196)
Non-unionized * Union sponsor * ignore	0.05	-0.08	-0.05	0.13	0.11	0.11
	(0.388)	(0.473)	(0.653)	(0.259)	(0.362)	(0.376)
Public pension sponsor * ignore	-0.08	-0.27*	-0.03	0.21	-0.39**	-0.21
	(0.355)	(0.078)	(0.854)	(0.210)	(0.040)	(0.269)
Other sponsor * ignore	0.00	-0.12	-0.05	0.01	-0.04	-0.08
	(0.937)	(0.112)	(0.474)	(0.910)	(0.688)	(0.411)
Director age 65 to 69	-0.13***	-0.51***	0.14**	0.41***	-0.21***	-0.45***
	(0.000)	(0.000)	(0.029)	(0.000)	(0.010)	(0.000)
Director age >= 70	-0.48***	-0.76***	0.60***	0.74***	-0.57***	-0.80***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.002)	(0.001)

Director tenure	-0.00	-0.00	0.00	-0.00	-0.01*	-0.02*
	(0.217)	(0.776)	(0.307)	(0.813)	(0.065)	(0.072)
Number of external directorships	-0.13***	-0.36***	0.21***	0.31***	-0.01	-0.14***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.656)	(0.000)
Director is gray	-0.02	-0.14*	0.06	0.18**	-0.01	-0.16
	(0.756)	(0.086)	(0.505)	(0.036)	(0.927)	(0.181)
Director is female	0.06	0.00	-0.17*	-0.15*	0.01	-0.06
	(0.125)	(0.938)	(0.053)	(0.081)	(0.939)	(0.523)
Director is on compensation committee	0.04	0.04	-0.01	-0.05	0.08	0.04
	(0.193)	(0.409)	(0.875)	(0.342)	(0.306)	(0.583)
Director is on audit committee	0.04	0.12**	-0.04	-0.06	0.04	0.05
	(0.214)	(0.040)	(0.463)	(0.413)	(0.604)	(0.490)
Director is on nominating committee	0.04	0.05	-0.09*	-0.11*	-0.03	0.11*
	(0.188)	(0.337)	(0.082)	(0.090)	(0.640)	(0.090)
Director chairs a committee	-0.01	-0.08	-0.02	0.08	-0.04	-0.07
	(0.830)	(0.223)	(0.733)	(0.238)	(0.578)	(0.428)
Market capitalization, year -1	-0.02	-0.01	0.02	-0.00	-0.06**	-0.05*
	(0.115)	(0.763)	(0.426)	(0.865)	(0.019)	(0.097)
Leverage, year -1	0.05	-0.32	-0.24	0.25	-0.06	-0.37
	(0.712)	(0.152)	(0.246)	(0.271)	(0.831)	(0.191)
Market-adjusted stock return, year -1 to 0	-0.05	0.08	-0.04	-0.13	-0.23*	0.05
	(0.401)	(0.335)	(0.651)	(0.143)	(0.069)	(0.633)
Market-adjusted stock return, year 0 to +1	-0.08**	-0.03	0.06	-0.02	-0.24***	-0.04
(or 0 to +3 for 3-year change)	(0.034)	(0.398)	(0.347)	(0.534)	(0.009)	(0.412)
Constant	0.29*	0.57**	-1.22***	-0.72**	-0.48*	-0.09
	(0.054)	(0.044)	(0.000)	(0.018)	(0.087)	(0.787)
Observations	3513	3494	3513	3494	3513	3494
Pseudo R^2			0.065	0.103	0.034	0.064
Adjusted R^2	0.09	0.24				

Table 4. Analysis of the net change in other public company directorships, and lost or gained directorships of outside directors for first time majority vote proposals, targets relative to a size- and performance-matched control sample, and for the close-call vote proposals

In this table we repeat the analysis of Table 3 for three different samples. The first time proposal sample begins with the full sample and then deletes the observations from any repeat majority vote proposals that a firm receives in subsequent years. Here, the omitted category is the same as in Table 3, directors who ignore requests from special interest sponsors. For the second sample, we identify a size- and performance-matched control firm and include non-employee directors from these control firms in the tests. Directors from these control firms are the omitted category in the tests. Specifically, for each firm with a majority vote proposal we identify a sample of non-targeted firms with sales in the previous fiscal year within 25% of a target firm's. We then retain the control firm with the smallest deviation score from the targeted firm in terms of size and prior stock return performance. We compute the deviation score as Deviation = $[(Sales_T - Sales_C)/(Sales_T + Sales_C)]^2 + [(Assets_T - Assets_C)/(Assets_T + Assets_C)]^2 + [(Market\text{-}Adjusted\ Stock\ Return_T - Market\text{-}Adjusted\ Stock\ Return_C)/(Market\text{-}Adjusted\ Stock\ Return_T + Market\text{-}Adjusted\ Stock\ Return_C)]^2$, where subscripts *T* and *C* represent targeted and potential control firms and Market-Adjusted return is the firm's one-year buy and hold return ending in December prior to the annual meeting minus the CRSP value-weighted market return over the same period. We calculated the deviation score using different measures of size, and the inclusion of both Sales and Assets yielded the closest set of control firms. Other papers that calculate deviation score in a similar manner include Ertimur, Ferri, and Muslu (2011), Butler and Wan (2010), and Huang and Stoll (1996). Finally, the third Close-Call sample includes directors from firms targeted by union pension fund sponsors with vote outcomes between 45% and 55%. The omitted category here is directors from firms with proposals with vote outcomes from 45% to 49% and directors from firms targeted by union sponsors in non-unionized firms with vote outcomes from 45% to 55%. P-values, reflecting robust standard errors corrected for firm-level clustering, are in parentheses. ***, **, * indicate significance at the 1%, 5%, and 10% levels.

	Net Change in number directorships (0 to +3)			**Directorship loss (0 to +3)**			**Directorship gain (0 to +3)**		
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	First time proposals	vs controls	Close-call	First time proposals	vs controls	Close-call	First time proposals	vs controls	Close-call
Special interest * compliance	-0.33**	-0.26**	-0.55**	0.30**	0.29**	0.51**	-0.39*	-0.32**	-0.47
	(0.026)	(0.031)	(0.045)	(0.049)	(0.020)	(0.016)	(0.052)	(0.041)	(0.239)
Special interest * ignore		0.05	-0.14		0.05	0.26		0.02	-0.08
		(0.410)	(0.245)		(0.560)	(0.126)		(0.842)	(0.644)
Non-unionized * Union sponsor * compliance	-0.01	0.09		-0.02	-0.07		0.10	0.13	
	(0.963)	(0.401)		(0.896)	(0.611)		(0.574)	(0.368)	
Public pension sponsor * compliance	0.08	0.07		0.05	0.16		0.21*	0.22**	
	(0.665)	(0.658)		(0.828)	(0.479)		(0.090)	(0.015)	
Other sponsor * compliance	0.09	0.15**		-0.06	-0.09		0.14	0.19*	
	(0.352)	(0.029)		(0.630)	(0.381)		(0.355)	(0.081)	
Non-unionized * Union sponsor * ignore	-0.06	0.01		0.14	0.15*		0.12	0.13	
	(0.590)	(0.949)		(0.226)	(0.072)		(0.369)	(0.158)	
Public pension sponsor * ignore	-0.25*	-0.21		0.26	0.28*		-0.13	-0.15	
	(0.062)	(0.123)		(0.113)	(0.054)		(0.526)	(0.382)	

Other sponsor * ignore	-0.11	-0.05		0.06	0.05		-0.06	-0.05	
	(0.214)	(0.287)		(0.588)	(0.430)		(0.608)	(0.384)	
Director age 65 to 69	-0.48***	-0.51***		0.40***	0.47***		-0.47***	-0.39***	
	(0.000)	(0.000)		(0.000)	(0.000)		(0.000)	(0.000)	
Director age >= 70	-0.86***	-0.74***		0.80***	0.70***		-0.98***	-0.65***	
	(0.000)	(0.000)		(0.000)	(0.000)		(0.000)	(0.000)	
Director age >= 65	-0.86***	-0.74***	-0.39***	0.80***	0.70***	0.34**	-0.98***	-0.65***	-0.36*
	(0.000)	(0.000)	(0.002)	(0.000)	(0.000)	(0.029)	(0.000)	(0.000)	(0.056)
Director tenure	-0.01	-0.00	-0.00	0.00	0.00	0.00	-0.02*	-0.01*	-0.01
	(0.339)	(0.489)	(0.671)	(0.868)	(0.823)	(0.765)	(0.050)	(0.088)	(0.375)
Number of external directorships	-0.36***	-0.36***	-0.30***	0.29***	0.29***	0.25***	-0.13***	-0.14***	-0.10
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.227)
Director is gray	-0.15*	-0.09*	0.04	0.12	0.10*	-0.05	-0.19	-0.15*	-0.12
	(0.081)	(0.093)	(0.827)	(0.210)	(0.098)	(0.774)	(0.147)	(0.055)	(0.578)
Director is female	-0.08	-0.01		-0.06	-0.05		-0.16	-0.08	
	(0.249)	(0.842)		(0.490)	(0.424)		(0.146)	(0.235)	
Director is on compensation committee	0.06	0.04		-0.05	-0.06		0.03	0.05	
	(0.274)	(0.243)		(0.369)	(0.173)		(0.710)	(0.331)	
Director is on audit committee	0.10*	0.12***		-0.05	-0.10**		-0.00	0.05	
	(0.089)	(0.001)		(0.516)	(0.028)		(0.992)	(0.311)	
Director is on nominating committee	0.08	0.02		-0.14**	-0.08*		0.11	0.04	
	(0.175)	(0.596)		(0.041)	(0.061)		(0.181)	(0.396)	
Director chairs a committee	-0.08	-0.04		0.04	0.05		-0.08	-0.02	
	(0.238)	(0.330)		(0.566)	(0.289)		(0.371)	(0.678)	
Market capitalization, year -1	0.00	-0.00	-0.02	-0.02	0.00	0.00	-0.03	-0.03	-0.08
	(0.900)	(0.781)	(0.742)	(0.515)	(0.836)	(0.923)	(0.403)	(0.186)	(0.208)
Leverage, year -1	-0.24	-0.17	-0.27	0.16	0.15	-0.30	-0.25	-0.30	-1.00**
	(0.303)	(0.240)	(0.575)	(0.518)	(0.393)	(0.560)	(0.387)	(0.125)	(0.048)
Market-adjusted stock return, year -1 to 0	0.11	0.02	-0.18	-0.19*	-0.10*	-0.15	-0.02	0.01	-0.37*
	(0.284)	(0.664)	(0.385)	(0.057)	(0.092)	(0.456)	(0.887)	(0.840)	(0.095)
Market-adjusted stock return, year 0 to +3	-0.02	-0.01	0.11	-0.04	-0.02	-0.10	-0.03	0.01	0.14

	(0.643)	(0.685)	(0.370)	(0.285)	(0.456)	(0.327)	(0.456)	(0.799)	(0.250)
Constant	0.47	0.43***	0.63	-0.59**	-0.79***	-0.82	-0.26	-0.37*	0.39
	(0.112)	(0.007)	(0.261)	(0.041)	(0.000)	(0.108)	(0.431)	(0.063)	(0.544)
Observations	2324	6946	497	2324	6946	497	2324	6946	497
Pseudo R^2				0.098	0.098	0.069	0.069	0.048	0.058
Adjusted R^2	0.23	0.24	0.15						

p-values in parentheses
* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

Table 5. Predicting board compliance with majority vote shareholder proposals

This table primarily uses the same variables defined in Table 1. In Panel A, the compliance rate is the percentage of boards at target firms in various sub-categories that fully comply with the activists' requests as outlined in the majority vote shareholder proposals. The first column divides the full sample into two categories, depending on whether the proposal firm is unionized or non-unionized. The next three columns further divide the two-subsamples by sponsor type. For each of the four columns, we report the results of a two-sided t-test of the difference in means between the unionized target firms and the non-unionized target firms. ***, **, * indicate significance at the 1%, 5%, and 10% levels. In Panel B, special interest target firms with poor union relations have a union relations score, as defined in Table 1, of -1 in the year prior to the annual meeting. We classify a special interest target firm as having outside directors above median age if the average age of its non-employee directors is above the sample median (59.9 years). The proposal topics included under executive compensation are listed in the header of Table 1. In the probit regressions of Panel C, all variables are indicator variables except the continuous variables percentage vote support (votes in favor of the proposal as a percentage of votes cast), prior 1-year market-adjusted return, and sponsor ownership. The prior 1-year market adjusted returns are the compounded monthly returns for the firm for the 12 months ending the December before the annual meeting year less the compounded monthly returns for CRSP's value-weighted market index for the corresponding period. P-values, reflecting robust standard errors corrected for firm-level clustering, are in parentheses.

Panel A. Univariate analysis of proposal compliance rates by sponsor type and unionized status of the firm

	Mean [N]	Mean [N]	Mean [N]	Mean [N]
	All proposals	**Union pension-sponsor**	**Public pension-sponsor**	**Other sponsor**
Unionized firms	18.2% [423]	29.4%*** [126]	16.7% [24]	13.2% [273]
Non-unionized firms	16.4% [183]	7.1% [70]	36.4% [22]	18.7% [91]

Panel B. Univariate analysis of the quiet life hypothesis

	Mean [N]
Special interest target firms with poor union relations	42.1% [19]
Special interest target firms with normal or good union relations	26.9% [108]
Special interest target firms with outside directors above median age	36.4%* [66]
Special interest target firms with outside directors NOT above median age	21.3% [61]
Special interest target firms with executive compensation proposal topics	46.8%*** [47]
Special interest target firms with other Non-compensation proposal topics	18.8% [80]

Table 5. Predicting board compliance with majority vote shareholder proposals (continued)
Panel C. Probit analysis of board compliance with majority vote shareholder proposals

	(1) Compliance =1	(2) Compliance =1	(3) Compliance =1	(4) Compliance =1	(5) Compliance =1	(6) Compliance =1
Unionized firm	-0.43**	-0.35*	-0.36*	-0.35*	-0.35*	-0.35*
	(0.035)	(0.093)	(0.090)	(0.093)	(0.094)	(0.092)
Special interest sponsor	0.65***	0.28				
	(0.001)	(0.187)				
Non-unionized firm*Union sponsor	-0.86***	-1.30***	-1.01***	-1.28***	-1.28***	-1.27***
	(0.006)	(0.000)	(0.002)	(0.000)	(0.000)	(0.000)
Public pension fund sponsor	0.37	0.39	0.37	0.39	0.39	0.39
	(0.174)	(0.173)	(0.196)	(0.177)	(0.174)	(0.166)
Special interest sponsor*Compensation related proposals			0.70**			
			(0.020)			
Special interest sponsor*Non-compensation related proposals			0.24			
			(0.316)			
Special interest sponsor*Poor union relations				0.66*		
				(0.074)		
Special interest sponsor*No poor relations				0.19		
				(0.393)		
Special interest sponsor*Above Median Age					0.49**	
					(0.044)	
Special interest sponsor*Below Median Age					0.05	0.05
					(0.843)	(0.843)
Special interest sponsor* Above Median Age*Poor union relations						1.52***
						(0.007)
Special interest sponsor* Above Median Age*No poor union relations						0.39
						(0.139)

% Vote support	0.01*	0.02**	0.02**	0.02**	0.02**	0.02**
	(0.082)	(0.014)	(0.017)	(0.011)	(0.017)	(0.015)
Sponsor ownership %	0.08*	0.09**	0.09**	0.09*	0.09**	0.09*
	(0.077)	(0.048)	(0.048)	(0.051)	(0.049)	(0.051)
Prior 1-year market-adjusted return	0.04	-0.01	0.01	-0.01	-0.02	-0.04
	(0.848)	(0.970)	(0.981)	(0.967)	(0.936)	(0.865)
Post-2000 proposal	0.40**	0.14	0.14	0.12	0.12	0.12
	(0.017)	(0.464)	(0.435)	(0.509)	(0.519)	(0.501)
First time MV proposal	0.41**	0.22	0.23	0.22	0.20	0.19
	(0.018)	(0.232)	(0.209)	(0.222)	(0.268)	(0.296)
Poison Pill proposal topic		-0.67**	-0.75***	-0.66**	-0.67**	-0.64**
		(0.010)	(0.001)	(0.012)	(0.010)	(0.015)
Staggered Board proposal topic		-0.65***	-0.71***	-0.65***	-0.65***	-0.63***
		(0.007)	(0.001)	(0.007)	(0.006)	(0.008)
Executive Compensation proposal topic		0.47		0.47	0.46	0.48
		(0.125)		(0.128)	(0.131)	(0.115)
Constant	-2.11***	-1.81***	-1.69***	-1.85***	-1.76***	-1.80***
	(0.000)	(0.003)	(0.004)	(0.002)	(0.004)	(0.003)
Observations	415	415	415	415	415	415
Pseudo R^2	0.099	0.159	0.158	0.163	0.165	0.171

Table 6. Change in union relations score surrounding majority vote proposals of unionized target firms

For each proposal sponsor and board response category (ignore the proposal or compliance with the activist request), the table reports mean values of the union relations score in the year prior to the annual meeting of the majority vote proposal, and the number of observations in brackets. We also report the percentage of negative scores and percentage of positive scores, but omit the percentage of zero scores. The table also reports corresponding statistics for the change in the union relations score from one-year prior to the annual meeting to the year after the annual meeting. Statistics are only computed for unionized firms, as non-unionized firms have zero scores for all observations. The union relations score is defined in Table 1. Across all unionized observations, the mean union relations score in year -1 is -0.04 and the standard deviation is 0.42. The mean change in union relations score from -1 to +1 is -0.01 and the standard deviation is 0.24. ***, **, * indicate the results of a two-sided t-test for differences in means (or percentage positive or negative) of target firms that ignore the proposal versus those that comply with the proposal. The test is conducted separately within each proposal sponsor category.

	All sponsors		**Special Interest-sponsor**		**Public pension-sponsor**		**Other sponsor**	
	Ignore	Compliance	Ignore	Compliance	Ignore	Compliance	Ignore	Compliance
Year -1	-0.022 [320]	-0.123* [73]	-0.103 [87]	-0.194 [36]	-0.067 [15]	0.000 [4]	0.014 [218]	-0.061 [33]
Year -1 (% negative)	8.67%	16.88%**	12.22%	21.62%	5.26%	0.00%	7.59%	13.89%
Year -1 (% positive)	7.19%	5.48%	2.30%	2.78%	0.00%	0.00%	9.63%	9.09%
	Ignore	Compliance	Ignore	Compliance	Ignore	Compliance	Ignore	Compliance
Change -1 to +1	-0.023 [302]	0.042** [71]	-0.086 [81]	0.029* [34]	0.071 [14]	0.000 [4]	-0.005 [207]	0.061 [33]
Change -1 to +1 (% worsening)	3.97%	1.41%	9.88%	0.00%*	0.00%	0.00%	1.93%	3.03%
Change -1 to +1 (% improving)	1.66%	5.63%**	1.23%	2.94%	7.14%	0.00%	1.45%	9.09%***