# All Shareholder Votes Are Not Created Equal[*]

Davidson Heath[†]          Da Huang[‡]          Chong Shu[§]

November, 18, 2024

## Abstract

We find that the identity of the shareholder matters as much as, if not more than, the number of shares they hold: firms are twice as responsive to the votes of active funds as to those of passive funds. We provide suggestive evidence that this discrepancy arises not because active funds are better informed, but because they pose a greater threat of future action. Despite the significantly larger holdings of Vanguard, BlackRock, and State Street – the so-called "Big Three" funds – their votes carry no more weight than those of an average active fund. These findings suggest that concerns over the influence of ever-larger index funds may be overstated.

**Keywords:** Voting, Director Elections, Active Investing, Passive Investing, Shareholder Democracy
**JEL Classification:** G12, G14

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[†]Department of Finance, David Eccles School of Business, University of Utah. 1655 Campus Drive, Salt Lake City, UT 84112, US. E-mail: `davidson.heath@eccles.utah.edu`

[‡]Department of Finance, D'Amore-McKim School of Business, Northeastern University. 370 Huntington Ave, Boston, MA 02115, US. E-mail: `da.huang@northeastern.edu`

[§]Department of Finance, David Eccles School of Business, University of Utah. 1655 Campus Drive, Salt Lake City, UT 84112, US. E-mail: `chong.shu@eccles.utah.edu`

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### Abstract

We find that the identity of the shareholder matters as much as, if not more than, the number of shares they hold: firms are twice as responsive to the votes of active funds as to those of passive funds. We provide suggestive evidence that this discrepancy arises not because active funds are better informed, but because they pose a greater threat of future action. Despite the significantly larger holdings of Vanguard, BlackRock, and State Street – the so-called "Big Three" funds – their votes carry no more weight than those of an average active fund. These findings suggest that concerns over the influence of ever-larger index funds may be overstated.

# 1. Introduction

The hallmark of democracy is that a poor man's vote carries the same weight as a rich man's vote. Should this principle extend to shareholder democracy so all shareholder votes are treated equally, regardless of who casts them? Shareholders' votes, similar to how citizens elect politicians, have the potential to shape corporate policies through vote tallies. However, shareholder votes also serve as a signal of investor preferences, which can indirectly shape corporate policies even if the votes do not achieve a majority (Levit & Malenko, 2011; Aggarwal, Dahiya, & Prabhala, 2019). Given the different information that each vote conveys, management might respond differently to votes on the same item cast by different investors, even if all votes are counted equally in the tally. Understanding the signaling value of each vote, along with how different votes on the same item are treated, is essential when crafting regulations aimed at enfranchising shareholders' voting rights.

In this paper, we study different shareholder's influence over the long-term outcomes of the proposals they vote on. Specifically, we focus on the influence gap in director elections for several reasons. First, director elections are among the most important mechanisms through which shareholders impact corporate governance (Cai, Garner, & Walkling, 2009; Fos, Li, & Tsoutsoura, 2018). Second, the long-term outcome of a director election, namely whether the director remains on the board for a period following the election, can be systematically measured with no ambiguity, unlike most other proposals. Lastly, the presence of multiple directors within a single firm provides within-firm variations that help rule out many firm-level unobserved variables confounding the results. As a result, director elections are a natural laboratory for studying the shareholder influence gap, though there is no reason to

believe our findings are confined solely to this context. Our results are likely applicable to broader settings involving shareholder proposals and governance mechanism.

We find that firms respond differently depending on the identity of the investor casting the vote. A dissenting vote by passive funds in a director's election decreases the probability that they remain on the board three years beyond the election by 0.7 percentage points. In contrast, an active fund withholding its support decreases this probability by 1.5 percentage points – more than double the association compared to its passive counterpart. Given the unconditional probability of departure is only 20%, this influence gap is both economically and statistically significant. The influence gap is robust to a variety of fixed effects and controls. Firm and year fixed effects sweep out firm-specific time-invariant factors and market-wide trends that apply to all firms. The more stringent firm-by-year fixed effects compare directors up for election in the same annual meeting, ruling out alternative explanations related to firm characteristics or performance. Item-level controls such as the ISS and Glass Lewis recommendations control for the situation specific to each director and year. We conclude that the influence gap is a robust pattern, and all shareholder votes are not created equal.

Is the influence gap explained by differences in holding size? For example, it could be that active funds hold larger positions either on average or when they are more likely to dissent. In this case, the influence gap between active and passive funds is only capturing the effect of holding size. To test this possibility, we separately estimate the influence gap for blockholders with 1% (roughly 95th percentile) or more holdings and non-blockholders. The influence gap is present for both blockholders and non-blockholders. Surprisingly, in a horse race, the influence gap between active and passive investors is larger than the gap between blockholders and non-blockholders. That is, as a determinant of firm response to shareholder

votes, shareholder identity is not only *separate from* but also *more important than* the size of the shareholder's stake. This finding again emphasizes the role of shareholder voting as a signaling mechanism.

Next, we explore the economic channels leading to the influence gap between active and passive investors. Put differently, in the cases where shareholder votes convey a signal, what do they signal? We examine two potential channels. First, passive funds cannot threaten to exit a position and are less likely to support outside slates in proxy contests (Kakhbod, Loginova, Malenko, & Malenko, 2023; Brav, Jiang, Li, & Pinnington, 2024). As a result, their no-votes carry less of a disciplinary threat than active fund votes. We term this mechanism the threat channel. Second, passive funds may be less informed about the firm than active funds are (Bebchuk & Hirst, 2019; Heath, Macciocchi, Michaely, & Ringgenberg, 2022). Understanding the lack of information in their vote, firm management may rationally underreact to signals from passive funds. We term this mechanism the information channel.

We find strong support for the threat channel and a lack of support for the information channel. If the threat channel leads to the influence gap, we would expect the gap to be narrower in firms with entrenched management. They are not so threatened by even active investors, which equalizes the influence between the active and passive shareholders. We find that the influence gap is an order of magnitude smaller in firms with the most entrenched firms compared to the gap in firms with the least entrenched firms, supporting the threat channel. On the other hand, if information content leads to the influence gap, we would expect the gap to be narrower for firms less sensitive to information. With several proxies for firm information sensitivity, we find that the influence gap is similar for firms more or less sensitive to information. Therefore, we conclude that there is a lack of support for the

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information channel.

In recent times, both regulators and academics have expressed concerns over large passive funds wielding outsize economic power (Coates IV, 2018). We apply our empirical framework and ask the question – just how powerful the "Big-Three" managers (Vanguard, BlackRock, and State Street) are? Comparing Big Three funds to active funds outside the Big Three, the former are no more influential than the latter because Big Three funds are predominately passive. Further, we find that Big-Three *active* funds are more influential than non-Big-Three active funds, while Big-Three *passive* funds are less influential than non-Big-Three active funds. This result further demonstrates the importance of shareholder identity beyond the size of their stake. We highlight two policy implications of our findings. First, the concern over the Big Three wielding too much power may be overstated. Firms rationally underreact to passive funds' votes because they cannot threaten to exit their passive positions. Second, pass-through voting might be more effective than originally thought, because a vote by an influential shareholder can be influential on firm behavior even if they do not have a large stake.

## 1.1. Literature Review

This paper makes several contributions to the existing literature. First, our discovery of the shareholder "influence gap" challenges traditional understandings of one-vote-one-share shareholder democracy and opens new avenues for theories of shareholder voting. Existing models of shareholder voting implicitly assume that all votes are treated equally, but not without reason. If the voting is a one-shot game with anonymity, the tally function is all

that matters and all votes are created equal. However, in reality, the management observes the identity of the voter and the voting happens repeatedly, which calls for a framework that incorporates these features.

Second, we demonstrate that the advisory role in shareholder votes is more significant than the tally function. In other words, investors participate in corporate elections primarily to express their opinions. By contrast, pivotality may not be a critical factor when shareholders consider how to cast their votes. This result relates to the debate between "expressive voting" and "instrumental voting" in the political science literature. In that context, a widely accepted assumption is that people derive an "expressive," or consumption, benefit from voting (Fiorina, 1976). Another branch of theory suggests that people vote for "instrumental" reasons, meaning they expect their vote to be pivotal with some probability. Although instrumental voting poses logical problems when applied to political elections (Downs, 1957; Riker & Ordeshook, 1968), whether it holds in shareholder voting remains an open empirical question, as many investors hold significant blocks of shares. In the shareholder voting literature, some existing theoretical papers assume instrumental voting (Malenko, Malenko, & Spatt, 2024), while others assume expressive voting (Câmara, Matsusaka, & Shu, 2024).

## 2. Data

Our sample comprises all votes to confirm directors (director elections) at routine annual meetings of U.S. public firms from 2007 to 2020. ISS Voting Analytics provides mutual fund votes and details on these elections' final voting outcome, as well as ISS's own recommen-

dations. Glass Lewis recommendations are obtained through a Public Records Law request directed to a large public pension fund (Shu, 2024). We exclude contested elections, using the dataset provided by Brav et al. (2024), along with any director elections where the director received less than 70% of the final vote. These filters ensure we capture the signaling value of votes because no single fund would have a meaningful probability to be pivotal and exert influence through the tally function of votes. Our results remain consistent if we omit these filters.

Firm characteristics are sourced from CRSP/Compustat. Mutual fund data, including their ownership of firms, come from the CRSP Mutual Fund Database. Both firm and fund characteristics are measured as of the calendar year preceding the year in which the votes were recorded.

Our key measure of fund voting is whether a fund voted against a particular director's reelection. We define a no-vote as the fund voting "Against," "Abstain," or "Withhold," while a yes-vote is defined as the fund voting "For." Our key measure of directors' career outcome is an indicator variable, $DirectorRenewed$ that equals 1 if the director remains on the firm's board of directors three years after the election, and 0 otherwise. If the firm drops out of the sample less than three years after the election, we also drop the election from the sample since we cannot know whether the director will be renewed.

Insert **Figure 1** About Here

Table 1 shows summary statistics of the sample. Director turnover is nontrivial: On average, 20% of directors depart from the firm's board three years after their election. On

the other hand, no-votes are unusual: Only 3.4% of mutual fund votes in director elections constitute no-votes. This fraction aligns closely with the average vote tally across all shareholders, as the average director in our sample is confirmed with a 96.7% vote share. The size of fund holdings is on average quite small at only 0.17% of the firm's market capitalization, although the distribution of holding sizes is right-skewed.

# 3. Empirical Results

In this section, we examine how votes cast by different shareholders in director elections affect the director's future career with the firm. The literature has shown that dissenting votes in director elections have negative career consequences even if the director receives a super-majority of support and the election is uncontested. We find that this effect is stronger if the dissent comes from active funds compared to passive funds, a phenomenon that we term the "shareholder influence gap."

Insert **Figure 1** About Here

**Figure 1** shows the relation between director renewal probability and the fraction of support by active and passive funds. The dots represent the binned scatter plot and the line represents the best-fit line with the functional form reported on the top left. Panel (a) shows the relation between director renewal probability and support from active funds, defined as the fraction of the number of supporting votes by active funds to the total number of votes cast. We see a clear positive correlation between a director's renewal probability and

the support they receive from active funds. A one percentage point increase in active fund support increases the renewal probability by about 0.11 percentage points. By contrast, panel (b) shows the relation between renewal probability and passive fund support is essentially flat – a one percentage point increase in passive fund support increases the probability by 0.01 percentage points. The support from passive funds is only one-tenth as influential as that from active funds. This strong pattern in the broad cross-section of the director elections data suggests a shareholder influence gap between active and passive funds.

Next, we formally examine the shareholder influence gap in a regression framework. We estimate the following equation:

$$\text{Director Renewal}_{i,j,t} = \beta_{\text{active}} \times \text{No}_{i,j,f,t} \times \text{Active}_f$$

$$+ \beta_{\text{passive}} \times \text{No}_{i,j,f,t} \times \text{Passive}_f$$

$$+ \gamma X_{i,j,f,t} + \text{Fixed Effects} + \epsilon_{i,j,f,t} \ , \tag{1}$$

where the dependent variable is an indicator variable that equals 1 if director $j$ remains on the board of firm $i$ three years after their election in year $t$. Vote $\text{No}_{i,j,f,t}$ is a vote-level indicator that equals 1 if fund $f$ votes "Against", "Abstain", or "Withhold". Active Fund$_f$ (or Passive Fund$_f$) is a fund-level indicator variable that equals 1 if fund $f$ is an active (or passive) fund and equals 0 otherwise. $X_{i,j,f,t}$ is a vector of vote-level control variables and the main effects of the interactions. $\beta_{\text{active}}$ and $\beta_{\text{passive}}$ capture the effects on director renewal of shareholder dissent from active and passive funds, respectively. $\beta_{\text{passive}} - \beta_{\text{active}}$ captures the shareholder influence gap to director renewal.

**Table 2** reports the regression results and demonstrates the influence gap. Column

1 shows the OLS estimate without fixed effects or controls. We see that an active fund dissenting in a director's election by voting "Against", "Abstain", or "Withhold" leads to a 3.0 percentage point lower probability that the director will serve another three years. By contrast, a dissent by a passive fund leads to only a 1.6 percentage point drop in this probability. The influence gap reported at the bottom of the table is economically significant. A 1.4 percentage point influence gap is over three times the standard deviation of the renewal probability for the entire sample. The influence gap is also statistically significant with robust standard errors calculated using the delta method and clustered on the director and firm level.

Insert **Table 2** About Here

We next address several endogeneity concerns. One endogeneity concern is that funds systematically choose what firms they hold for reasons that correlate with managerial responsiveness. For example, passive funds might be more likely to hold the stock of firms whose board of directors is more entrenched, and active funds more likely to hold those with a less entrenched board. **Table 2** columns 2 and 3 add firm and year fixed effects and firm-by-year fixed effects, which sweeps out time-invariant or time-varying characteristics on the firm level. The estimates in column 2 compare directors serving in the same firm and the estimates in column 3 compare directors up for election in the same annual meeting. We see that the point estimates reported at the bottom of the table remain similar, suggesting that firm characteristics do not explain the influence gap.

Another endogeneity concern is that the perceived quality of a director can simulta-

neously affect their career outcomes and voting patterns of active and passive funds. For example, an Ivy League background may increase a director's renewal probability and make them more popular among active funds relative to passive funds. The perceived quality can also be time-varying. A director making controversial public statements may simultaneously make them less likely to be renewed and make active funds less likely to vote for them. We proxy directors' perceived quality with the recommendation by two major proxy advisors, ISS and Glass Lewis. Columns 4 to 6 control for the perceived quality of directors with indicator variables that equal 1 if ISS or Glass Lewis recommend voting against the director, respectively. We see that proxy advisors' recommendation has an economically and statistically strong association with director renewal probability in specifications with fixed effects. However, the shareholder influence gap remains largely unchanged, suggesting that directors' perceived quality does not explain the influence gap.

Finally, we address the endogeneity concern that the size of funds' holdings might drive managerial responsiveness. For example, active funds may hold more concentrated and large positions (Kacperczyk, Sialm, & Zheng, 2005), and firms might be more responsive due to the larger holding size and not the fund's active nature. We first compare the holding size of passive and active funds. The mean, median, and $95^{\text{th}}$ percentile holdings for passive funds are 0.17%, 0.18%, and 1.08% of firm value, whereas the same numbers for active funds are 0.16%, 0.14%, and 0.91%. Therefore, passive funds do hold slightly larger positions but the difference is unlikely to fully explain the influence gap results given how close these numbers are.

Insert **Table 3** About Here

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To formally rule out the alternative explanation related to holding size, we directly control the holding size of the fund as well as its blockholder status. **Table 3** reports the results. Column 1 replicates the result in **Table 2** column 6 for ease of comparison. The shareholder influence gap between active and passive funds is directly estimated as the coefficient of $\text{No}_{i,j,f,t} \times \text{Active}_f$ since we leave out the interaction with passive funds.[1] We control for the size of the holding in column 2 and find that the shareholder influence gap remains largely unchanged. The association between director renewal and the size of the holding against their election is statistically significant but economically trivial. Increasing the holding size of a dissenting vote from the $10^{\text{th}}$ percentile (0.0001) to the $90^{\text{th}}$ percentile (0.0041) would increase the renewal probability by 0.0012 percentage points. In other words, in a linear specification, the size of the holding of the dissenting vote has an effect that is precisely estimated to be nearly zero. In column 3, we control for the blockholder status, defined as an indicator variable that equals 1 if the fund holds 5% or more of the firm's shares. Consistent with the literature (Edmans, 2009; Edmans & Manso, 2011; Edmans, 2014), we find that blockholders exert significant influence on company outcomes. Compared to a non-blockholder, a blockholder fund dissenting in the election, is associated with a 3 percentage point decrease in the director's renewal probability. However, the influence gap between active and passive funds remains unchanged. We conclude that the size of the holding has an economically trivial effect and does not affect the shareholder influence gap, which is also robust to the control of the blockholder status.

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[1]The left-out group in **Table 2** column 6 is the standalone term $\text{No}_{i,j,f,t}$ whereas the left-out group in **Table 3** column 1 is the interaction term $\text{No}_{i,j,f,t} \times \text{Passive}_f$. As a result, the coefficient of $\text{No}_{i,j,f,t}$ corresponds to that of $\text{No}_{i,j,f,t} \times \text{Passive}_f$, and the coefficient of $\text{No}_{i,j,f,t} \times \text{Active}_f$ corresponds to the differential effect between the active and passive funds, i.e., the influence gap.

# 4. Economic Channel

In this section, we first propose two plausible channels that could lead to the shareholder influence gap. The first channel is that passive funds cannot threaten to exit given their mandate even if they disagree with the firm management, which we call the threat channel. The second channel is that passive funds are less informed than active funds, which we call the information channel. We empirically test the predictions of each channel.

## 4.1. The Threat Channel

The influence gap between active and passive shareholders can arise from a threat channel. Passive funds are required to hold a representative sample of an index. As a result, they are "captive audiences" who cannot sell the shares even if they disagree with the management (Kakhbod et al., 2023). In addition, passive funds are less likely to support outside slates in proxy contests to impose discipline (Brav et al., 2024). By contrast, active funds can threaten to exit or support outside slates if they disagree with the management, endangering their jobs. Understanding this dynamic, the management chooses to be more responsive to active funds than passive funds.

If the threat channel leads to the shareholder influence gap, we would expect a narrower gap for firms with entrenched management. This is because active funds' threat to exit or support outside slates is less effective to entrenched managers, whose jobs are never in danger. As a result, management entrenchment is effectively an equalizer for passive funds and active funds. Put differently, passive funds cannot make threats against the management, but active funds' threats are equally empty if the management is entrenched.

We empirically test whether the influence gap is narrower in firms with entrenched management. We replicate the results of **Equation 1** but estimate the influence gap for entrenched and non-entrenched firms separately with the following equation:

$$
\begin{aligned}
\text{Director Renewal}_{i,j,t} = {} & \beta_{\text{E,active}} \times \text{Vote No}_{i,j,f,t} \times \text{Active Fund}_f \times \text{Entrenched}_{i,t} \\
& + \beta_{\text{E,passive}} \times \text{Vote No}_{i,j,f,t} \times \text{Passive Fund}_f \times \text{Entrenched}_{i,t} \\
& + \beta_{\text{NE,active}} \times \text{Vote No}_{i,j,f,t} \times \text{Active Fund}_f \times \text{Not Entrenched}_{i,t} \\
& + \beta_{\text{NE,passive}} \times \text{Vote No}_{i,j,f,t} \times \text{Passive Fund}_f \times \text{Not Entrenched}_{i,t} \\
& + \gamma X_{i,j,f,t} + \xi_{i,t} + \epsilon_{i,j,f,t} \, .
\end{aligned}
\tag{2}
$$

$\text{Entrenched}_{i,t}$ (or $\text{Not Entrenched}_{i,t}$) is an indicator variable that equals to 1 if the E-Index of firm $i$ in year $t$ is above (or below) a threshold and 0 otherwise. The E-index is an index of six features of firm governance such as poison pills and staggered boards (Bebchuk, Cohen, & Ferrell, 2008). $\xi_{i,t}$ is firm-by-year fixed effects. The influence gap for entrenched (or not entrenched) firms is calculated as $\beta_{\text{E,passive}} - \beta_{\text{E,active}}$ (or $\beta_{\text{NE,passive}} - \beta_{\text{NE,active}}$).

Insert **Table 4** About Here

**Table 4** reports the results and shows that the influence gap is narrower in firms with entrenched management. In column 1, we categorize the firm to have an entrenched management if its E-Index is greater than 2. We see that for firms with entrenched management, a dissent from active funds reduces the director's renewal probability by 1.58% and that from passive funds reduces the probability by 1.41%. The non-entrenched management is

more responsive to shareholder dissent. The renewal probability decreases by 2.97% and 1.91% in reaction to dissent from active and passive funds, respectively. Importantly, the shareholder influence gap for firms with entrenched management is about one-sixth of the magnitude compared to firms with non-entrenched management and is statistically indistinguishable from 0. The narrower influence gap supports the threat channel. Non-entrenched managers are less responsive to passive funds' dissent because they cannot threaten exit or discipline. In contrast, entrenched managers are not so threatened by even active investors, which equalizes the influence between the active and passive shareholders.

**Table 4** columns 2 and 3 further demonstrate the threat channel. We repeat the analysis in column 1 but change the threshold of the E-Index for the company to be considered as having entrenched management. Firms are considered to have entrenched management if they have an E-Index greater than 2 or 3 in columns 2 and 3, respectively. Therefore, the level of entrenchment increases from column 1 to column 3. We see that as management becomes more entrenched, they are less responsive to dissent in column 2 and not responsive to dissent at all in column 3. On the other hand, the influence gap is present consistently for firms with non-entrenched management. The stark contrast demonstrates the threat channel for the shareholder influence gap. The gap arises when the management is threatened by exit or future discipline from active funds while passive funds cannot threaten to do the same.

## 4.2. The Information Channel

The influence gap between active and passive shareholders can also arise from an information channel. Passive funds do less research and monitor the firms less (Iliev, Kalodimos, & Lowry,

2021; Heath et al., 2022). As a result, the signal conveyed by their votes in the de-facto non-binding director elections is less valuable (Levit & Malenko, 2011). Understanding this effect, the management chooses to be more responsive to active funds than passive funds, creating an influence gap between active and passive funds.

Under the information channel, we would expect that firms less sensitive to information see a narrower influence gap. For example, if the firm earns a high profit or has a high stock return, the management may not pay as much attention to shareholder's inputs. Similarly, if the uncertainty of the information environment is low, proxied by past stock return volatility, the management may also be less inclined to listen.

We empirically test whether the influence gap is narrower in firms less sensitive to information. We replicate the results of **Equation 1** but estimate the influence gap for firms with high and low information sensitivity (IS) separately with the following equation:

$$
\begin{aligned}
\text{Director Renewal}_{i,j,t} = {} & \beta_{\text{High IS,active}} \times \text{Vote No}_{i,j,f,t} \times \text{Active Fund}_f \times \text{High IS}_{i,t} \\
& + \beta_{\text{High IS,passive}} \times \text{Vote No}_{i,j,f,t} \times \text{Passive Fund}_f \times \text{High IS}_{i,t} \\
& + \beta_{\text{Low IS,active}} \times \text{Vote No}_{i,j,f,t} \times \text{Active Fund}_f \times \text{Low IS}_{i,t} \\
& + \beta_{\text{Low IS,passive}} \times \text{Vote No}_{i,j,f,t} \times \text{Passive Fund}_f \times \text{Low IS}_{i,t} \\
& + \gamma X_{i,j,f,t} + \xi_{i,t} + \epsilon_{i,j,f,t} \; .
\end{aligned}
\tag{3}
$$

High $\text{IS}_{i,t}$ is an indicator variable that equals 1 if firm $i$ has an above-median return on asset, above-median stock return, or below-median stock return volatility in the past year. $\xi_{i,t}$ is firm-by-year fixed effects. The influence gap for high-IS (or low-IS) firms is calculated as

$\beta_{\text{High IS,passive}} - \beta_{\text{High IS,active}}$ (or $\beta_{\text{Low IS,passive}} - \beta_{\text{Low IS,active}}$).

Insert **Table 5** About Here

**Table 5** reports the results and shows that the influence gap is similar for firms with high and low information sensitivity. In columns 1 to 3, we see that even though the influence gap in firms more sensitive to information is slightly higher than that in firms less sensitive to information, the difference is economically small. In addition, the difference in the influence gap for high-IS and low-IS firms is statistically indistinguishable from 0. The t-stat of the difference (not reported in the table) is 0.66, 0.04, and 0.39 for columns 1 to 3, respectively, calculated based on robust standard errors double-clustered on firm and director level. These results show a lack of evidence supporting the information channel.

# 5. The Influence of the "Big Three" Funds

Passive investing has become increasingly popular in the last two decades. Vanguard, Black-Rock, and State Street – the so-called "Big Three" funds – have amassed significant assets and collectively own about 20% of the publicly traded U.S. firms (Morningstar, 2024). Their outsize ownership stake has attracted scrutiny from regulators and academics in recent times. One of the concerns is that they wield enormous economic power in corporate governance and decision-making through voting. To address this concern, congress has passed the IN-DEX Act and large asset managers have started offering pass-through voting for investors. We ask a more foundational question – just how influential the "Big Three" funds are?

We separately estimate the managerial responsiveness for Big-Three (Big3) funds and non-Big3 funds and report the results in **Table 6**. In the first two columns, we see that the association between director renewal and Big3 funds' dissent has a very close point estimate compared to the association between director renewal and dissent from non-Big3 active funds. Put differently, the votes of Big3 funds carry no more weight than those of an average active fund. In columns 3 and 4, we see that non-Big3 active funds are more influential than Big3 passive funds but less influential than Big3 active funds. Our results suggest that the companies rationally underreact to votes of Big3 funds, understanding that they are passive investors and cannot threaten exit or proxy contests. These results have important implications. If the concern over the outsize influence of the Big3 funds is based on a false premise, the concern may be overstated.

# 6. Conclusion

This paper provides new insights into the impact of shareholder voting on corporate outcomes, particularly focusing on director elections. Our empirical analysis reveals the existence of an influence gap, where the votes of active funds are nearly twice as influential as those of passive funds in determining a director's career. This finding underscores the importance of considering the advisory role of shareholder votes beyond their mere tallying, especially in the context of modern corporate governance where the actual pivotality of votes is rare.

The identification of this influence gap contributes to a deeper understanding of shareholder democracy, challenging the assumption that all votes are treated equally. Our results suggest that management not only observes the identity of voters but also reacts differently based on the threat of further action associated with those votes. This has important implications for how shareholder influence is modeled and understood, particularly in the context of repeated interactions between management and different types of shareholders.

Our exploration of the economic channels driving the influence gap highlights the nuanced roles of information asymmetry and the threat of exit in shaping corporate governance outcomes. The stronger impact of active fund votes in firms with less entrenched management and higher uncertainty suggests that their voting plays a crucial role in improving corporate decision-making. Conversely, the weaker influence of passive fund votes, despite their growing prevalence, raises concerns about the potential for suboptimal governance when management under-reacts to their signals.

Overall, this paper sheds new light on the impact of shareholder voting and its implications for corporate governance. Our results emphasize that the identity of the voter matters significantly in determining long-term outcomes, even within the framework of one-share-one-vote democracy. By documenting the influence gap between active and passive investors and highlighting the underlying threat channel as its primary driver, our findings challenge common assumptions about shareholder voting. The evidence suggests that shareholder voting serves as a powerful signaling mechanism, with implications that extend beyond simple vote tallies to influence corporate decisions.

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# Figure 1. Managerial Response to Votes from Different Shareholders

## (a) Active Funds



## (b) Passive Funds
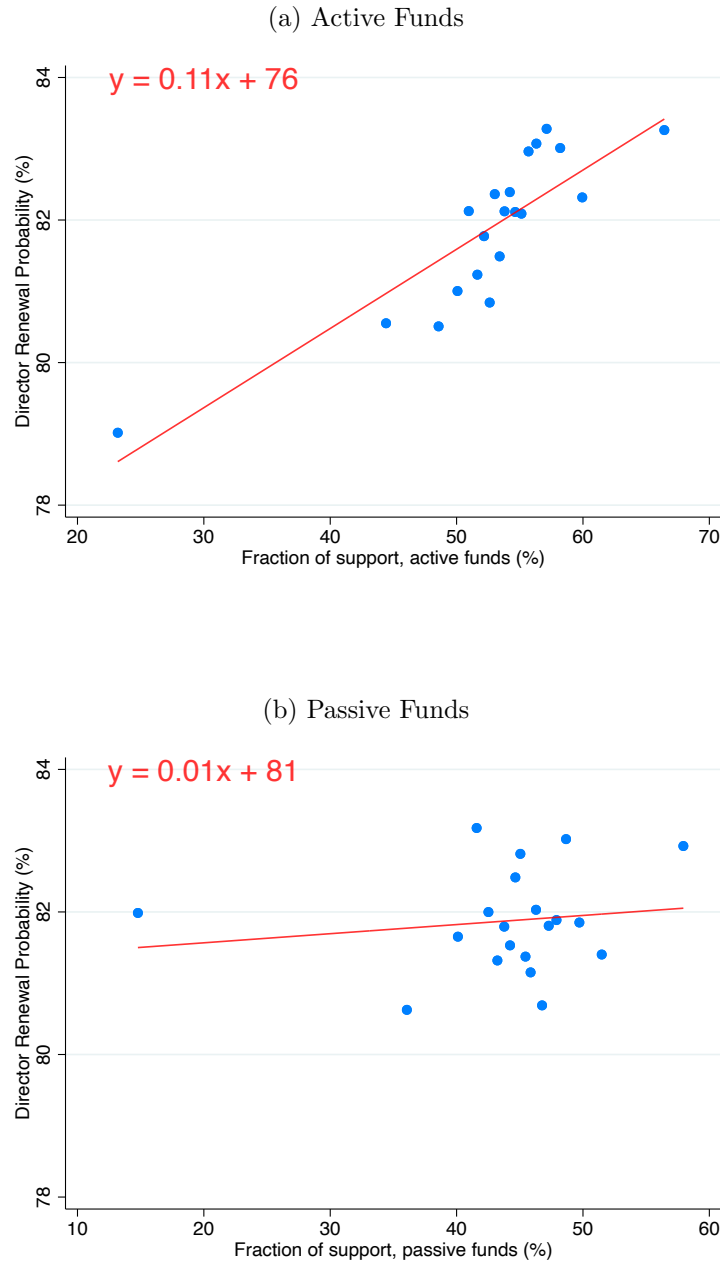


The figure plots the relation between the probability of a director remaining on the board for over three years after their election and the fraction of supporting votes by shareholder type. The function of the fitted line is reported on the top-left of the figure. Panel (a) shows the binned scatter plot of the relation between the probability and the level of active fund support while controlling for the level of passive fund support. Panel (b) shows the binned scatter plot of the relation between the probability and the level of passive fund support while controlling for the level of active fund support.

## Table 1
## Summary Statistics

The table presents summary statistics of the sample. The sample consists of votes to confirm directors (director elections) at routine annual meetings of U.S. public firms, from 2007 to 2020.

| Variable | Mean | SD | p10 | p50 | p90 | N |
|---|---|---|---|---|---|---|
| DirectorRenewed | 0.802 | 0.398 | 0.000 | 1.000 | 1.000 | 1.18e+07 |
| VotedNo | 0.034 | 0.180 | 0.000 | 0.000 | 0.000 | 1.36e+07 |
| PassiveFund | 0.481 | 0.500 | 0.000 | 0.000 | 1.000 | 1.36e+07 |
| FracFor | 0.967 | 0.046 | 0.919 | 0.984 | 0.997 | 1.36e+07 |
| log(AUM) | 6.95 | 2.26 | 3.92 | 7.01 | 9.78 | 1.36e+07 |
| Expense ratio | 0.64 | 0.57 | 0.08 | 0.48 | 1.36 | 1.36e+07 |
| FracHeld | 0.0017 | 0.0054 | 0.0001 | 0.0002 | 0.0041 | 1.36e+07 |

## Table 2
## Differential Managerial Response to Voting, Active and Passive Funds

The table presents estimates of managerial responsiveness to active and passive funds with the following equation:

$$\text{Director Renewal}_{i,j,t} = \beta_{\text{active}}\text{No}_{i,j,f,t} \cdot \text{Active}_f + \beta_{\text{passive}}\text{No}_{i,j,f,t} \cdot \text{Passive}_f$$
$$+ \gamma X_{i,j,f,t} + \text{Fixed Effects} + \epsilon_{i,j,f,t},$$

where the dependent variable is an indicator variable that equals 1 if director $j$ remains on the board of firm $i$ three years after their election in year $t$. $\text{No}_{i,j,f,t}$ is a vote-level indicator that equals 1 if the fund votes "Against", "Abstain", or "Withhold." $\text{Passive}_f$ and $\text{Active}_f$ are indicator variables that equal 1 if fund $f$ is a passive or active fund, respectively, and 0 otherwise. $X_{i,j,f,t}$ is a vector of control variables and the main effects of the interactions. Robust standard errors double-clustered by firm and director are reported in parentheses. The influence gap is calculated as $\beta_{\text{active}} - \beta_{\text{passive}}$ with standard errors calculated using the delta method. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively.

| | (1) | (2) | (3) | (4) | (5) | (6) |
|---|---|---|---|---|---|---|
| $\text{No}_{i,j,f,t} \times \text{Active}_f$ | -3.01*** | -3.71*** | -2.50*** | -2.36*** | -2.36*** | -1.47*** |
| | (0.59) | (0.48) | (0.34) | (0.31) | (0.26) | (0.18) |
| $\text{No}_{i,j,f,t} \times \text{Passive}_f$ | -1.64*** | -2.45*** | -1.56*** | -1.11*** | -1.33*** | -0.66*** |
| | (0.48) | (0.38) | (0.31) | (0.36) | (0.30) | (0.24) |
| | | | | | | |
| ISS $\text{No}_{i,f,t}$ | | | | -1.40 | -3.21*** | -3.43*** |
| | | | | (1.09) | (1.11) | (1.29) |
| GL $\text{No}_{i,f,t}$ | | | | -0.81 | -3.08*** | -3.32*** |
| | | | | (0.96) | (0.94) | (1.01) |
| | | | | | | |
| Firm FE | No | Yes | No | No | Yes | No |
| Year FE | No | Yes | No | No | Yes | No |
| Firm × Year FE | No | No | Yes | No | No | Yes |
| Main Effects | Yes | Yes | Yes | Yes | Yes | Yes |
| Adj. R-squared | 0.000 | 0.054 | 0.199 | 0.000 | 0.054 | 0.200 |
| Observations | 12,399,447 | 12,399,447 | 12,399,446 | 12,399,447 | 12,399,447 | 12,399,446 |
| | | | | | | |
| Influence Gap | 1.36*** | 1.26*** | 0.94*** | 1.24*** | 1.04*** | 0.81*** |
| | (0.42) | (0.36) | (0.24) | (0.38) | (0.32) | (0.23) |

# Table 3
## Differential Managerial Response to Voting, Fund Identity and Blockholder Status

The table presents the estimates of managerial responsiveness to funds with different management objectives (passive or active) and blockholder status. $\text{No}_{i,j,f,t}$ is a vote-level indicator that equals 1 if the fund votes "Against", "Abstain", or "Withhold". Active $\text{Fund}_f$ is an indicator variable that equal 1 if fund $f$ is an active fund and 0 otherwise. $\text{Blockholder}_{i,f,t}$ is an indicator variable that equals 1 if fund $f$ holds more than 5% of firm $i$'s shares outstanding at time $t$. Robust standard errors double-clustered by firm and director are reported in parentheses. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively.

|  | (1) | (2) | (3) |
|---|---|---|---|
| $\text{No}_{i,j,f,t}$ | -0.66*** | -0.69*** | -0.71*** |
|  | (0.24) | (0.24) | (0.24) |
| $\text{No}_{i,j,f,t} \times \text{Active}_f$ | -0.81*** | -0.83*** | -0.83*** |
|  | (0.23) | (0.23) | (0.23) |
| $\text{No}_{i,j,f,t} \times \text{Blockholder}_{i,f,t}$ |  |  | -2.91** |
|  |  |  | (1.48) |
| $\text{No}_{i,j,f,t} \times \text{Shares Voted}_{i,f,t}$ |  | 0.31** | 0.45** |
|  |  | (0.15) | (0.20) |
|  |  |  |  |
| Controls | Yes | Yes | Yes |
| Firm × Year FE | Yes | Yes | Yes |
| Main Effects | Yes | Yes | Yes |
| Adj. R-squared | 0.200 | 0.200 | 0.200 |
| Observations | 12,399,446 | 12,399,446 | 12,399,446 |

## Table 4
## Economic Channel: Entrenchment and Threat to Exit

The table presents the estimates of managerial responsiveness to active and passive funds for firms with and without entrenched management. A firm is considered to have entrenched management if it has an E-Index greater than 2, 3, and 4 in columns 1, 2, and 3, respectively. Robust standard errors double-clustered by firm and director are reported in parentheses. The influence gap is calculated as $\beta_{\text{active}} - \beta_{\text{passive}}$ for firms with and without entrenched management with standard errors calculated using the delta method. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively.

|  | (1) | (2) | (3) |
|---|---|---|---|
| Entrenched: |  |  |  |
| $\text{No}_{i,j,f,t} \times \text{Active}_f$ | -1.58*** | -0.97* | 0.56 |
|  | (0.47) | (0.59) | (0.85) |
| $\text{No}_{i,j,f,t} \times \text{Passive}_f$ | -1.41** | -0.75 | 1.60 |
|  | (0.55) | (0.65) | (1.30) |
|  |  |  |  |
| Influence Gap | 0.17 | 0.22 | 1.04 |
|  | (0.36) | (0.49) | (0.81) |
|  |  |  |  |
| Not Entrenched: |  |  |  |
| $\text{No}_{i,j,f,t} \times \text{Active}_f$ | -2.97*** | -2.73*** | -2.65*** |
|  | (0.51) | (0.43) | (0.41) |
| $\text{No}_{i,j,f,t} \times \text{Passive}_f$ | -1.91*** | -1.86*** | -1.83*** |
|  | (0.47) | (0.39) | (0.36) |
|  |  |  |  |
| Influence Gap | 1.06*** | 0.88*** | 0.82*** |
|  | (0.32) | (0.28) | (0.26) |
|  |  |  |  |
| Entrenched: | E-Index > 2 | E-Index > 3 | E-Index > 4 |
|  |  |  |  |
| Controls | Yes | Yes | Yes |
| Firm FE | Yes | Yes | Yes |
| Year FE | Yes | Yes | Yes |
| Main Effects | Yes | Yes | Yes |
| Adj. R-squared | 0.188 | 0.188 | 0.188 |
| Observations | 10,532,841 | 10,532,841 | 10,532,841 |

## Table 5
## Economic Channel: Information Sensitivity and Signaling

The table presents the estimates of managerial responsiveness to active and passive funds for firms with high and low information sensitivity. A firm is considered to have high information sensitivity if it has a low return-on-asset, a low past stock return, and a high past stock return volatility in columns 1, 2, and 3, respectively. Robust standard errors double-clustered by firm and director are reported in parentheses. The influence gap is calculated as $\beta_{\text{active}} - \beta_{\text{passive}}$ for firms with high and low information sensitivity with standard errors calculated using the delta method. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively.

|  | (1) | (2) | (3) |
|---|---|---|---|
| **High Information Sensitivity:** | | | |
| $\text{No}_{i,j,f,t} \times \text{Active}_f$ | -3.58*** | -3.54*** | -2.93*** |
|  | (0.76) | (0.49) | (0.52) |
| $\text{No}_{i,j,f,t} \times \text{Passive}_f$ | -2.86*** | -2.69*** | -2.25*** |
|  | (0.60) | (0.45) | (0.49) |
| Influence Gap | 0.99*** | 0.98*** | 1.07*** |
|  | (0.26) | (0.28) | (0.33) |
| **Low Information Sensitivity:** | | | |
| $\text{No}_{i,j,f,t} \times \text{Active}_f$ | -2.89*** | -2.81*** | -3.21*** |
|  | (0.43) | (0.47) | (0.53) |
| $\text{No}_{i,j,f,t} \times \text{Passive}_f$ | -1.90*** | -1.83*** | -2.14*** |
|  | (0.39) | (0.39) | (0.42) |
| Influence Gap | 0.73 | 0.85*** | 0.68** |
|  | (0.47) | (0.31) | (0.30) |
| High Information Sensitivity: | Low Return-on-Asset | Low Stock Return | High Stock Volatility |
| Controls | Yes | Yes | Yes |
| Firm FE | Yes | Yes | Yes |
| Year FE | Yes | Yes | Yes |
| Main Effects | Yes | Yes | Yes |
| Adj. R-squared | 0.077 | 0.077 | 0.077 |
| Observations | 11,801,530 | 11,831,011 | 11,816,461 |

## Table 6
## How Influential Are the "Big Three" Funds?

The table presents the estimates of managerial responsiveness to funds managed by Vanguard, BlackRock, and State Street (the "Big Three") and non-Big-Three active funds. Robust standard errors double-clustered by firm and director are reported in parentheses. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively.

|  | (1) | (2) | (3) | (4) |
|---|---|---|---|---|
| $\text{No}_{i,j,f,t} \times \text{Non-Big3 Active}_f$ | -3.69*** | -2.47*** | -3.69*** | -2.47*** |
|  | (0.50) | (0.35) | (0.50) | (0.35) |
| $\text{No}_{i,j,f,t} \times \text{Big3}_f$ | -3.65*** | -2.46*** |  |  |
|  | (0.59) | (0.51) |  |  |
| $\text{No}_{i,j,f,t} \times \text{Big3 Active}_f$ |  |  | -4.72*** | -3.47*** |
|  |  |  | (0.77) | (0.61) |
| $\text{No}_{i,j,f,t} \times \text{Big3 Passive}_f$ |  |  | -3.45*** | -2.26*** |
|  |  |  | (0.60) | (0.52) |
| $\text{No}_{i,j,f,t} \times \text{Non-Big3 Passive}_f$ | -1.99*** | -1.24*** | -1.99*** | -1.24*** |
|  | (0.37) | (0.29) | (0.38) | (0.30) |
|  |  |  |  |  |
| Firm FE | Yes | No | Yes | No |
| Year FE | Yes | No | Yes | No |
| Firm × Year FE | No | Yes | No | Yes |
| Main Effects | Yes | Yes | Yes | Yes |
| Adjusted R-squared | 0.053 | 0.198 | 0.053 | 0.198 |
| Observations | 9,500,505 | 9,500,503 | 9,500,505 | 9,500,503 |