Proxy advisors and shareholder engagement

Evidence from Italian say-on-pay

M. Belcredi, S. Bozzi, A. Ciavarella, V. Novembre

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I *proxy advisors* e l'attivismo degli azionisti

Evidenza empirica dal *say-on-pay* in Italia

M. Belcredi*, S. Bozzi*, A. Ciavarella**, V. Novembre**

Sintesi del lavoro

Gli investitori istituzionali sono spesso criticati per lo scarso attivismo nei confronti delle società quotate. Tuttavia, la presenza di elevati costi informativi e altri costi di transazione può ridurre i loro incentivi a svolgere un ruolo attivo nella *governance* delle imprese in cui investono e a monitorare l'operato del management, poiché i costi di questa attività possono essere superiori ai benefici. I cosiddetti *proxy advisors* (PA), ossia soggetti che offrono professionalmente servizi di consulenza agli azionisti in materia di esercizio dei diritti di voto, possono contribuire a mitigare tali costi di transazione e, per tale motivo, favorire una partecipazione più attiva degli azionisti alla vita societaria. In questo lavoro si analizza, in particolare, l'attività svolta dai PA, e il suo riflesso sulle scelte degli azionisti, con specifico riferimento al tema delle modalità di voto sulle politiche di remunerazione degli amministratori (cosiddetto *say-on-pay*), utilizzando i dati sul voto espresso da ogni singolo azionista sulle politiche di remunerazione adottate dalle società quotate italiane nel 2012 e sui giudizi in materia espressi dai due principali PA attivi sul mercato italiano. I risultati del lavoro possono essere così sintetizzati: i) mentre il dissenso degli azionisti sulle politiche di remunerazione è basso, in linea con quanto accade in altri paesi, il dissenso degli investitori istituzionali (prevalentemente fondi pensione e fondi comuni con un portafoglio diversificato a livello internazionale) è particolarmente alto; ii) il voto degli investitori istituzionali sulle politiche di remunerazione è fortemente correlato con le raccomandazioni dei PA; tuttavia, i PA influenzano maggiormente gli investitori istituzionali con quote di partecipazioni inferiori alle soglie di comunicazione al mercato

(c.d. non-blockholder, ossia prevalentemente fondi pensione e fondi comuni con un portafoglio molto diversificato a livello internazionale), mentre gli investitori istituzionali blockholder (ossia detentori di partecipazioni rilevanti soggette a obblighi di comunicazione al mercato), avendo un maggiore incentivo a investire in attività di raccolta e analisi delle informazioni societarie, sembrano essere meno sensibili alle raccomandazioni dei PA; iii) stime preliminari mostrano che in Italia l'effetto delle raccomandazioni dei PA sul voto degli investitori istituzionali è altrettanto forte, se non più forte, di quello osservato negli Stati Uniti. Ciò è coerente con il rilevante peso nelle assemblee societarie di investitori esteri con un portafoglio molto diversificato, che non possono conoscere in modo approfondito le numerose società in cui investono, e con l'elevata incidenza sul nostro listino di società classificabili come medio-piccole, per le quali i costi di accesso alle informazioni sono più elevati e il rapporto costi-benefici del loro utilizzo può essere più sfavorevole; iv) gli investitori istituzionali non utilizzano passivamente le raccomandazioni dei PA e tendono a focalizzarsi su specifiche criticità evidenziate nei loro report che reputano particolarmente rilevanti nel contesto italiano, quali, in particolare, la struttura della remunerazione e il suo rapporto con la creazione di valore nel lungo periodo e l'entità dei trattamenti di fine rapporto.

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Abstract

Institutional investors are often criticized for their insufficient "engagement" with listed companies. Actually, information and other transaction costs limit their capacity to actively monitor investee firms, and to engage with their management. A partial solution is offered by Proxy Advisors (PAs), providing proxy voting services on a subscription basis. We use Say-On-Pay (SOP) in Italian listed firms to investigate PA activity and (institutional) shareholder voting behavior. Making use of a unique dataset, including information on how each shareholder voted in 2012, we analyze the behavior of different classes of shareholders and their relation with PA recommendations. Our main results can be summarized as follows: i) while shareholder dissent on SOP is low, in line with what happens in other developed countries, dissent by institutional investors is surprisingly high; ii) the voting behavior of institutional investors is strongly correlated with PA recommendations. The influence of PAs is higher on nonblockholders (mostly internationally diversified pension and mutual funds) than on blockholders; iii) preliminary estimates show that the influence of PAs in Italy is at least as strong as (and probably stronger than) that observed in the US. This is coherent with the weight of non-domestic institutions, which can be hardly expected to independently analyze thousands of firms; and it is especially so in Italy, where most listed firms may be classified as small/medium cap firms on a comparative basis; iv) institutional investors, however, do not take PA recommendations at face value, but focus on the specific reasons of concern underlined in the reports (in particular, on the structure and long-term value creation of the remuneration policy). Severance pay has, by far, the largest impact..

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Contents

1 Introduction

This paper aims at analysing (institutional) shareholders' voting decisions and the extent to which they are correlated with proxy advisors' (PAs) recommendations. Specifically, taking advantage of a unique database on say-on-pay votes in Italian firms, we investigate three main issues: a) the level of dissent expressed at AGMs by different classes of shareholders, with a particular focus on institutional investors; b) whether shareholders' voting decisions are correlated with PAs' voting recommendations and c) whether and to what extent institutional investors implement PAs' recommendations passively or look at specific elements on the basis of their own concerns and analysis.

In the last few years institutional investors have made an increasing use of PAs, not only in the US - where there is a well-established market for their services - but also in Europe. Institutional investors are subject to a growing pressure to exercise their stewardship responsibilities, and actively engage with listed firms. In recent years their opportunity to have a say on several corporate governance issues (say on pay and related party transactions being the most relevant cases) has widely increased in several member states. These trends call for a better understanding of the mechanics of PA recommendations production and their potential influence on voting decisions and – ultimately – on the governance of individual firms.

PAs may play a very influential role since institutional investors have substantial voting power but often lack the appropriate incentive to cast informed ballots. In particular, institutional investors tend to have relatively small holdings in a large number of stocks, making the cost of researching every ballot item at each annual meeting for all the firms in their portfolio unsustainable. As a consequence, the voting process is sometimes performed by institutional investors as a compliance duty (i.e. they simply make sure that the votes are cast according to a pre-specific policy), rather than as an activity directly involving asset managers who engage in equity research for the purpose of portfolio selection (i.e. buy or sell decisions to enhance the fund's value).

PAs constitute a natural way for institutional investors to reduce engagement costs through outsourced services while complying with fiduciary duties to their ultimate beneficiaries. This business model is particularly frequent when institutional investors hold internationally diversified portfolios, i.e. they hold stakes in a number of companies listed in different countries, which are therefore subject to diverse corporate governance rules. PAs can easily provide information on corporate governance specificities of each company/country at an affordable price.

The role of PAs has been, however, criticised for a number of reasons.

First of all, the market for PA services is very concentrated. Virtually everywhere, Institutional Shareholder Services (ISS) and Glass Lewis (GL) are the

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incumbents[1].

Secondly, PAs may be subject to conflicts of interests which can undermine the independence and objectivity of their analyses. For example, they may provide corporate rating or consultancy services to an issuer, and at the same time offer advice to institutional clients with regard to the same issuer[2].

Thirdly, concerns have been expressed with respect to the procedures, systems and controls adopted by PAs. A specific concern is that PAs may perform their analyses following a one-size-fits-all approach, without taking into account specific local market conditions. Moreover, several doubts have been cast with regard to the accuracy and reliability of the voting recommendations, as well as the transparency of resources and processes related to the preparation of the recommendation.

These issues have called for the attention of policy makers and regulators around the world[3]. In the US, furnishing a proxy voting advice constitutes a solicitation and is subject to the information and filing requirements set out in the proxy rules. However, the Securities and Exchange Commission (SEC) has adopted a rule to exempt them from the filing requirements when certain conditions are met (Cremers & Romano 2009, ESMA 2012). Recent guidance from the SEC has then addressed the potential conflicts of interests faced by PAs by clarifying when these exemptions apply. It has also specified a series of duties for institutional investors making use of PAs' services for engagement purposes (SEC 2014).

The European Securities and Markets Authority (ESMA) published in 2013 a report, following a previous discussion paper, encouraging the proxy advisory industry to develop its own code of conduct, based on a set of principles drafted by ESMA

1   In the US, ISS has around 61 per cent of the market, Glass Lewis around 36 per cent, while the rest is split among other PAs. European data on market shares are not publicly available, but ISS is widely considered the market leader, followed once again by Glass Lewis (ESMA 2012).

2   Other conflicts may arise when there is a commercial or personal relationship between a proxy advisor and the firm (for example, when the former is owned by an institutional investor or by a listed company to whom the proxy advisor may be providing advice).

3   Parallels between the proxy advisory and rating agency industry structures are sometimes drawn. The main common characteristic is the low number of incumbents. On the global scenario there are currently only three big rating players: Moody's , Standard & Poor's and Fitch Ratings. In the past, this number has never rose higher than 5 and Standard & Poor's and Moody's hold alone around 80% of the total global market share. The situation is similar in the proxy market, where there are two main players and a number of relatively small local firms.

Many authors have argued that the presence of significant economies of scale, scope and standardization in the rating market is the key driver for the few number of incumbents. In particular, as lenders prefer to have a few standardized ratings (and raters) to compare, reputation is vital and firms need to cover the market extensively to establish their name among investors. Thus, the rating market is not able to lodge many competitors and is naturally oligopolistic: an argument which might easily apply to the proxy market.

While market structures are both naturally oligopolistic, there are however three relevant differences which suggest caution when envisaging further analogies between rating agencies and proxy advisors. Firstly, ratings have important regulatory relevance, especially for prudential purposes, and this has a boosting effect on their market impact. Both in the banking and investment funds industries, ratings are de facto regulatory licenses. This calls or closer public monitoring, which in turns acts as a barrier to entry in the market, reinforcing the role of incumbents. Secondly, the intensity of potential conflicts of interests is very different. Rating agencies sell their services to issuers while proxy advices are bought by active shareholders, typically institutional investors. While of course proxy advisors might in some cases also provide consultancy to issuers, this is generally a minor component of their business. Thirdly, ratings are public while proxy advisors recommendations can be accessed only by the institutional investors who buy this service.

itself (ESMA 2013). Following the publication of the ESMA final report, some key industry members formed a Group (the "Best Practice Principles Group") with the aim to develop a set of best practice principles for PAs to be adopted on a comply or explain basis[4]. The Best Practice Principles were subsequently published in February 2014 and signed by a majority of European players[5].

To the best of our knowledge, this is the first paper to analyse (institutional) investors' voting decisions in connection with the role played by PAs in a European country. To do so, we look at the context of shareholder say-on-pay vote in Italy. Italy is one of the several countries that have introduced say-on-pay legislation in recent years[6] in reaction to public outrage arising from episodes of huge payments to executives apparently unsupported by good corporate results[7].

Italy is a country which epitomizes the continental Europe model. While some observers have identified a slow-paced trend towards a more dispersed ownership structure and a higher presence and activism of institutional investors, the Italian financial market is still structurally different from that of the US and other Anglo-Saxon countries. Institutional investors account on average for around 6% of listed companies' capital and controlling shareholders still own on average nearly 50% of the ordinary shares[8].

Say-on-pay represents an ideal setting to analyse shareholder engagement in connection with the role of PAs for two main reasons. First, existing studies (see below) suggest that PAs' influence is particularly high in this area. Second, differently from other settings where PAs often adopt policy guidelines by topic, SOP recommendations are tailored to each different company, since the analysis needed to evaluate remuneration policies necessarily requires firm-specific considerations.

We analyse the voting recommendations on Italian listed companies' remuneration policies issued by the two most influential PAs: ISS and GL. Preliminarily, we examine the analyses they performed to support their voting recommendations and the main drivers behind their choices, how they differ across PAs and whether – as is often argued – they follow a mere "box-ticking" approach. We then narrow down to

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4   This topic is currently debated in Europe since the European Commission on April 2014 presented a proposal for the revision of the Shareholder Rights Directive which tackles corporate governance shortcomings related to listed companies, intermediaries and also PAs. The proposal requires PAs to adopt adequate measures to guarantee accurate and reliable voting recommendations and to disclose to the public some key information related to these recommendations as well as information on any actual or potential conflict of interest they are subject to.

5   Cf. Best Practice Principles for Shareholder Voting Research & Analysis, published on 5 March 2014 and available at http://bppgrp.info.

6   At the end of 2010, Italy introduced a regulation requiring companies to publish a detailed remuneration report and to submit its first section (i.e. their remuneration policy) to a mandatory, non-binding shareholder vote.

7   The UK was the first country to introduce a mandatory say-on-pay in 2002. The vote, initially advisory, became binding in 2013. As for the US, in January 2011 the SEC adopted, under the Dodd-Frank Act, rules requiring listed companies to hold shareholder advisory votes on executive compensation, leaving up to shareholders to determine the frequency of this vote. Several other countries have meanwhile given shareholders more voice in order to mitigate managerial self-interest (Correa & Lel, 2013).

8   For a comprehensive assessment of the evolution of listed companies' Corporate Governance in Italy see CONSOB (2014), Italian Report on the Corporate Governance of Listed Companies, available at http://www.consob.it/main/consob/pubblicazioni/report/rapporto_cg/index.html.

our main research question and investigate the determinants of shareholders' votes focusing in particular on the role of PAs' recommendations in possibly influencing the voting decisions of institutional shareholders.

Our paper is related to the literature on shareholder votes and, in particular, on the role of PAs. So far, little is known about PA recommendations' impact on (institutional) shareholders' vote. To the best of our knowledge, only Ertimur et al. (2013) provide a comprehensive picture on these issues. Ertimur et al. (2013) show in particular that PA voting recommendations highly affect say-on-pay votes; the sensitivity of shareholder votes to these recommendations varies according to the institutional investor ownership structure, the rationale behind the recommendation and some firm characteristics. Other studies, all based on the US experience, confirm a strong association between PA analyses and shareholder votes (Larcker et al., 2013; Cai et al., 2009; Cindy at al., 2008; Choi et al., 2009[9]). So far, no analysis on European data is available.

Thanks to the peculiar features of Italian regulation, requiring listed firms to publish on line their complete AGM minutes, we observe the number of votes cast by each shareholder for each item in the agenda. Consequently, we provide additional insights into a number of issues related to PA recommendations and their impact on shareholder voting. In particular, leveraging on our unique dataset, we are able both to disentangle the votes of several categories of shareholders, with a particular attention to institutional investors, and to analyse the impact of PA recommendations separately on the voting behaviour of each shareholder category, thereby contributing to a better understanding of the role and impact of proxy advisors.

We follow the official Consob (2014) classification of institutional investors, including: i) sovereign, private equity and venture capital funds as well as asset managers and pension funds (investment funds), ii) banks and insurance companies (financial companies).[10] For both categories, Italian and foreign investors are separately monitored. We also keep track of the size of institutional investors' stakes by differentiating those above 2% (blockholders)[11] from those below the same threshold (non-blockholders). Major stakes are normally held by active funds while passive funds normally own a diversified portfolio composed of small stakes held in a number of companies.

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9 Larcker et al. (2013) confirm the finding that proxy advisory firm recommendations have a substantive impact on say-on-pay voting outcomes. Cai et al. (2009) examine the factors that determine the percentage of "for" votes cast in uncontested director elections and find that ISS recommendation reduces the vote in favour of directors by 19 per cent. Cindy at al. (2008) analyse the role of ISS in proxy contests and find that its recommendations have a high explanatory power for contest outcomes. Choi et al. (2009) study the significance of the voting recommendations issued by four PAs in connection with uncontested director elections. They find a moderate impact of ISS recommendations on voting outcome (according to their analysis, an ISS recommendation shifts 6-10 per cent of shareholder votes).

10 Investors belonging to these categories are included in our definition of institutional investors if they hold a stake below 10% of equity capital. In line with previous literature (La Porta et al 2002, Laeven & Levine 2007), we assume that investors holding larger stakes are interested in controlling the listed firm (possibly through coalitions).

11 These are defined as the entities subject to Consob's major shareholding disclosure obligations. Cf. Consob (2014), Section III.

We finally contribute to the literature on say-on-pay, which investigates the determinants of shareholders' dissent. According to this stream of literature (mostly based, once again, on US and UK data), a key variable driving dissent is the level of CEO pay. Other relevant variables are pay for performance sensitivity, the potential dilution from equity grants, firm risk and awarded perquisites (Alissa, 2009; Carter & Zamora, 2009; Conyon & Sadler, 2010; Ertimur et al, 2013; Balsam & Yin, 2012; Kimbro & Xu, 2013). The first study addressing the topic in Italy shows, however, that dissent is mainly driven by the level of ownership concentration, investor activism at the company level, the nature of the vote (binding *vs* non-binding) and the level of disclosure, while the level and structure of CEO remuneration seem to play only a minor role (Belcredi et al., 2013).

Our main results may be summarized as follows. First, while SOP general shareholder dissent in Italy is low, in line with other developed countries, dissent by institutional investors (tipically, internationally diversified mutual and pension funds) is surprisingly high. Secondly, the voting behavior of institutional investors is strongly correlated with PA recommendations. PAs' influence seems at least as strong as in the US and this is consistent with the relative weight of non-domestic institutions within the set of institutional shareholders investing in Italian listed companies. Finally, institutional investors do not follow PA recommendations passively but evaluate the reasons behind such recommendations, paying particular attention to the structure of the remuneration and to the policy regarding severance pay.

The rest of the paper is articulated as follows. Section 2 provides a summary of the ISS and GL reports and, specifically, of their SOP-related contents. Section 3 describes our sample and presents descriptive statistics. Sections 4 and 5 analyse the determinants of PA voting recommendations and their impact on different categories of shareholders' votes. Section 6 concludes.

2 PA reports on say-on-pay

In this section we describe the say-on-pay related contents of the reports issued by ISS and GL in the first year of implementation of the new Italian rules. We hand-collected information from the 201 ISS and 172 GL reports issued for 206 (out of 251) companies listed on the Italian Stock Exchange at the time of the 2012 proxy season. Leveraging on the paper by Ertimur et al. (2013), we also provide some comparative analysis between the reports issued by ISS and GL in the US and in Italy (see Appendix 1).

2.1 ISS Analysis

In 2012 ISS analysed compensation plans of Italian firms along four dimensions: fixed pay, short term variable pay, long term variable pay, service contracts. This investigation was followed by a summary of the main pros and cons of the policy. On this basis, the quality of disclosure was judged alternatively as *above average* (or *good*), *average, below average* (or *poor*) and it was evaluated whether the

policy deviates from five guidelines, which took into account corporate governance variables, disclosure quality and remuneration structure[12].

Comparing these analyses with those performed by ISS in the US, some differences emerge. First of all, the dimensions along which the compensation plans were analysed are quite diverse[13], since the analysis in the US focuses on the structure of the remuneration package and, in particular, on the link between pay and performance, while items related to the disclosure quality and to the "governance" of the process leading to the report receive less or no attention. This different behaviour may depend upon the fact that – at least in 2012 – reports on remuneration in Italy contained less exhaustive information about the structure of the remuneration and the link between performance and results, and therefore they did not allow a correct assessment of these elements. Moreover, in the US ISS seems to perform a more detailed and articulate analysis, leading to the assignment of a rating (high, medium or low) to each "concern" category.

Coming back to the ISS analysis in Italy, issues related to compensation structure and long-term value creation as well as the lack of disclosure of basic features of the remuneration policy seemed to be the main drivers of concern, with 103 and 81 concerns being issued, respectively (see Table A)[14]. As for the US, "high" concerns are typically associated with a weak link between pay and performance.

When matching the concerns on disclosure with the final disclosure score, a strong positive correlation can be observed (see Table B)[15]. However, this is not always the case: 2 companies received a score for transparency "above average" although (some of) the basic features of the compensation policy were not disclosed, while 15 companies received a score "below average" for disclosure, although the basic features of the compensation policy had been disclosed.

2.2 GL Analysis

Glass Lewis analysed compensation plans of Italian listed firms along two dimensions: disclosure and compensation structure. Compensation structure was analysed with regard to pay mix, incentive plans, severance pay and director pay. As for disclosure, the analysis was based on a number of issues, including the following:

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12 ISS guidelines in 2012 were the following: 1) Was the report made available in a timely manner?; 2) Does the company disclose basic features of the proposed compensation policy such as performance criteria, caps, and severance payments?; 3) Does the compensation committee include executives?; 4) Do concerns exist with respect to the structure and long term creation of shareholders value of the bonus or other aspects of the remuneration policy?; 5) Do severance payments exceed 24 months' pay?

13 In the US they are: 1) pay for performance; 2) peer group; 3) non-performance pay; 4) severance and 5) communication.

14 On the other hand, severance payments set at an excessive level (i.e. higher than the 24 months limit) and governance issues (specifically, whether the compensation committee includes executives) were less frequent (35 and 20 cases, respectively).

15 Where basic features of remuneration policy are disclosed, disclosure is set at an "average" or at a "good" level in the 85 per cent of the cases (84 firms). On the contrary, where the basics of compensation policy are not disclosed, 54 companies have been assigned a "poor" and 22 with an "average" disclosure mark.

performance metrics, targets and hurdles, vesting periods of stock-based components, other items such as severance agreements or equity award determination process and, finally, implementation of best practices (only for blue chip companies included in the FTSE-Mib Index). Glass Lewis then assigned a rating (*good, fair, poor*) to both the compensation structure and the disclosure profile.

Differently, in the US market, compensation plans are analysed along three dimensions: not only structure and disclosure, but also pay for performance. Hence, as it is the case for ISS, the link between pay and performance seemed a crucial point in the US context but not in the Italian case, at least in 2012. Similarly to the Italian case, GL assigns a separate rating (*poor, fair, good*) to compensation structure and disclosure quality while a specific grade (A, B, C, D, F) refers to the link between pay and performance.

In Italy, the main concerns related to compensation structure (Table C) came from performance conditions being inadequate (117 cases) and long-term investment plans being absent or insufficient (87 companies)[16]. Concerns related to compensation structure gave rise to a poor rating only in 45 companies (26% of the cases), while in the other cases the rating was fair (80 firms) or good (47 firms). Regarding disclosure (Table D), the main issues raised by GL were connected with targets and performance metrics not being disclosed (53 and 51 companies, respectively)[17]. The final rating was poor in only 22 cases (almost 13% of the total) and good or fair in the remaining 150 companies. In most cases, there is a correlation between the two marks: a firm receiving a good/fair (poor) rating in a given area typically received a good/fair (poor) rating also in the other area. Only 25 per cent of the ratings (i.e. 43 firms) were not aligned (Table E).

2.3 Final Recommendations

Both PAs concluded their reports with a summary of the main shortcomings and a final recommendation. Comparing the final recommendations, ISS seemed to follow a more hard-line approach than GL in the year under analysis. GL issued an "Against" recommendation for less than a third (31%) of the firms included in the sample, while ISS came up with a negative advice in almost half of the cases (48%). The same is true for the individual ratings assigned to disclosure and structure, where ISS also seemed stricter. Having regard to disclosure quality, GL assigned a "poor" rating to 22 firms (12% of the sample: in all cases except one they received an Against recommendation). ISS considered disclosure poor in 73 firms (36% of the sample). Most of these companies (62) also received an "Against" recommendation (about 31% of the sample and 85% of the firms with a poor disclosure level).

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16 Issues related to excessive severance agreements or the company's failure to implement global best practices regarding compensation structure seemed relatively less likely (35 and 28 cases, respectively).

17 Differently, the disclosure of vesting schedules gave rise to a few remarks (12) and the number of cases where the implementation of best practices was not satisfactory was relatively low (24) and similar to the 28 cases identified for low adherence to compensation structure best practices.

As for compensation structure, the two analyses are hardly comparable, since GL assigned an explicit rating to this profile, while ISS merely described its concerns in this area. To present at least some preliminary evidence, we chose to classify as "poor" on compensation structure 121 firms (60% of the sample) for which ISS expressed a concern with reference either to excessive severance payments (first item in Table A) or to the structure of remuneration and discretionary bonuses (second item in Table A): 84 of them (69% of the total) received an "Against" recommendation (Table F). GL assigned a "Poor" rating to the compensation structure only in 45 cases (equivalent to 26% of the sample); this led almost always (in 44 cases) to a recommendation to vote against the remuneration policy. Cases where both profiles are classified as poor lead, almost invariably, to an Against recommendation by both PAs.

Table G shows that ISS and GL issued the same recommendation in 59% of the cases. They tended to agree most when they issued a positive evaluation (39% of the cases). Within the subset of controversial cases (firms where at least one PA recommended to vote against), ISS and GL agreed only in 32% of the cases.

Table H compares ISS and GL scores on disclosure. It shows that in almost 66% of the cases two similar evaluations were issued. In a significant number of companies (46 firms, 30% of the total) GL disclosure grades were higher than those issued by ISS.

It is worth comparing ISS and GL grades in the Italian and in the US market. Differently from Italy, in the US GL seemed more likely to issue an "Against" recommendation (this happens in 21.7% of the firms, versus 11.3% for ISS). Also, both PAs issued the same recommendation in a great majority of cases (77%). Similarly to the Italian case, most of the agreement cases (accounting for 72% of the total) regard the "For" grades, while both ISS and GL recommend "Against" only in 5% of the cases. Agreements on controversial cases are observed in 17.9% of the sample. For both PAs, the most frequent reason of high concern is a weak link between pay and performance.

3   Sample selection and descriptive statistics

We investigate proxy advisors' recommendations and their relation with shareholder voting at the 2012 Annual General Meetings, when SOP was first implemented in Italy. Our initial database is the same used in Belcredi et al (2014), including data on shareholder votes (hand-collected from GM minutes) and information on the remuneration policy and directors' remuneration (also hand-collected from Remuneration Reports) for all companies listed in the Italian Stock Exchange in 2012 (226 firms). Additional data on ownership structure and board characteristics are drawn from the CONSOB and the *Assonime-Emittenti Titoli* Corporate Governance database, while accounting and stock market data come from Datastream-Worldscope. To be included in our sample we required at least one PA Report (from ISS and/or from GL) to be available in 2012. This leaves us with a final sample of 202 companies. Summary statistics are reported in Table 1.

Table 1 – Panel A: Descriptive statistics

Variable	n	Mean	S.D.	I Quart.	Median	III Quart.
			Firm Characteristics			
Total Assets (.000)	202	20,000,000	87,000,000	220,000	740,000	4,700,000
Market Capitalization (.000)	202	1,600,000	5,400,000	63,105	210,000	910,000
M/B	202	0.95	2.93	0.4	0.73	1.26
ROA (%)	202	5	11	1	6	10
RET1Y (%)	199	27	9	21	27	33
SQM_RET	197	1.09	0.77	0.59	0.87	1.26
			CEO Compensation			
CEOFixedPay (€.000)	201	869	807	317	629	1200
CEOVarCash (€.000)	201	470	1912	0	28	367
CEO_%_Variable_Comp (%)	196	16	0.21	0	8	27
CEOEquity (€.000)	201	194	1038	0	0	0
CEOTotComp (€.000)	201	1533	2656	353	852	1668
			Ownership concentration			
Cash_Flow_Rights (%)	202	46.00	21.00	31.00	51.00	63.00
Voting_Rights (%)	202	50.00	19.00	37.00	53.00	64.00
Wedge (%)	202	4.00	9.00	0.00	0.00	0.00
			CEO and Board Characteristics			
CEO_Age	198	56.71	9.5	51	57	63
Board_Size	202	10.88	4.43	8	10	13
			Dissent			
Total Shareholder Dissent (%)	188	6.00	12.00	0.00	0.00	6.00
Dissent of institutional shareholders (%)	159	29.00	34.00	0.00	10.00	54.00
Dissent of institutional blockholders (%)	63	11.00	30.00	0.00	0.00	0.00
Dissent of institutional nonblockholders (%)	155	32.00	34.00	0.00	17.00	63.00

The table presents sample descriptive statistics. All variables are defined in the Appendix.

Italian listed companies are usually small-medium enterprises: the average (median) firm has total assets around EUR 20,000 (740) million and a market capitalization of EUR 1,600 (210) million. Ownership is typically concentrated: on average, the largest shareholder holds a 46% stake (in terms of cash-flow rights). Around 60% of Italian listed firms are under the control of a family, holding on average a 56% block . Around a quarter of firms make recourse to control-enhancing mechanisms (dual-class shares and pyramids). The average (median) CEO total compensation (including fixed and variable pay) was around 1.5 million (850 thousand) Euro, including also sums received by subsidiaries and affiliates.

We measure total dissent as the percentage of negative votes cast at the General Meeting (i.e. (Against + Abstain)/Total votes: abstentions are counted as negative votes according to Italian rules). [18] Average total dissent in our sample was around 6% of votes cast, i.e. somewhat smaller than that recorded in the first year of mandatory SOP in Anglo-Saxon countries (8.9% in the US in 2011 (ISS, 2011); in the UK, the average dissent in 2003 varied between 7.9% and 16%, depending on the sample used (Alissa, 2009; Carter & Zamora, 2009; Conyon & Sadler, 2010; Ferri & Maber, 2013). A lower dissent is hardly unexpected in Italy, since ownership structure is typically concentrated and dissent is usually limited to shareholders who are not part of the control group.

It is important to track different categories of investors separately, since they may have different views about the firm remuneration policy and be more or less sensitive to PA recommendations. We are particularly interested in the voting behavior of institutional investors, which have often been recognized as a likely candidate for low-cost, corporate governance activism (Renneboog and Szilagyi 2011, 2013). "Institutional investors" are a broad and diverse family, made up of subjects adopting different business models and pursuing different strategies, even with reference to activism toward targeted firms. We follow the official Consob (2014) definition, including a) asset managers and pension funds (i.e. passive funds), b) sovereign, hedge and private equity funds (i.e. active funds), c) banks, d) insurance companies. We also differentiate between blockholders and subjects holding minor stakes. Major stakes are normally held by active funds while passive funds normally own a diversified portfolio composed of small stakes held in a number of companies. We finally separately keep track of Italian and foreign institutional investors. Tracking the votes actually cast by institutional investors required hand-collecting and analyzing the minutes of Shareholder Meetings (and their annexes, including a – possibly – long list of the votes cast on each item by each shareholder attending the meeting). Institutional investors' dissent on SOP issues is – surprisingly – much higher than total dissent: average (median) dissent was around 29% (10%) of the votes cast (recall that average (median) total dissent is 10% (0%)). Average (median) dissent increases further to 32% (17%) amongst institutional nonblockholders (basically, mutual and pension funds).

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18 We define negative votes according to their legal value. It should be recognized, however, that abstentions and "true" negative votes may be used by investors to convey different signals to the management of the company.

4 Determinants of PA recommendations

As a preliminary step, we analyze the determinants of PA recommendations. To this end we estimate a logistic regression where the dependent variable, ISS (GL) Against, is a 1/0 dummy variable taking value one if ISS (GL) recommends to vote Against the (first section of the) Remuneration Report (RR), and 0 otherwise. In line with previous literature, we predict that PAs are more likely to issue a negative recommendation where disclosure about the details of the remuneration policy is lower, where corporate governance (particularly of the process leading to the remuneration proposal) is worse, where firm performance is worse and where CEO compensation is higher.

We proxy the quality of disclosure with a dummy variable taking value one where disclosure is "low" and the quality of corporate governance of the remuneration process with the presence of a remuneration committee; firm performance is measured, alternatively, in accounting (last year's ROA) and market terms (1-year past stock return); finally, CEO compensation is proxied by three different measures, capturing the total amount paid, the structure of CEO compensation (variable/total compensation, which may be interpreted as a proxy for pay-performance sensitivity) and the quartile in the CEO remuneration distribution. To capture other firm characteristics that may affect PA decisions, we control for the same variables used in Belcredi et al (2014), namely: firm size (log(Total assets)), risk (standard deviation of stock returns), growth opportunities (MV/BV), industry (financial/non-financial) and ownership structure (CFR owned by the ultimate shareholder and CFR-VR wedge, which may be interpreted as a proxy for the risk of extraction of private benefits).[19] Our results are reported in Table 2.

Consistent with our expectations, and also with PA Guidelines, firms providing investors with less information about their remuneration policy are more likely to receive an Against recommendation. PA recommendations are also related with CEO remuneration structure: however, clear differences emerge across proxy advisors when the parameters affecting the final recommendation are observed. Although no specific guideline was issued on the quantum of remuneration, ISS is more likely to issue an Against recommendation where CEO total compensation is higher (see model (1); this is consistent also with existing US evidence), whereas GL seems less interested in the level (and more in the structure) of CEO remuneration and is likely to recommend Against where the weight of variable remuneration is lower (see model (5)). This is consistent with PAs following partially different approaches, possibly reflecting the preferences of different client bases. Quartile dummies are not statistically significant, indicating that PAs are less interested in – possibly occasional[20] – extreme payments than in the general structure of CEO remuneration. Firm performance seems to play a minor role[21]. Generally, control variables are not statistically signifi-

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19 Detailed variable definitions are reported in Appendix 2.

20 Right-hand tail cases may often be generated by lump-sum bonuses paid according to long-term-incentive plans.

21 It may be useful to underline that – since 2013 – ISS introduced new tables regarding Financial Highlights, Financial & Operational Performance, and Executive Remuneration.

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cant, with only one exception: ISS is more likely to issue an Against recommendation where the wedge between CFR and VR is higher, indicating that the risk of incentives misalignment is taken into account by ISS when issuing SOP recommendations. Though individual coefficients are generally weaker, the explanatory power of our model (in terms of pseudo-R^2) is similar (around 14% for ISS) to Ertimur et al (2013).

Table 2 – Determinants of ISS and GL "Against" recommedations

	ISS Against	GL Against	ISS&GL Against	ISS Against	GL Against	ISS&GL Against	ISS Against	GL Against	ISS&GL Against
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Log Total Assets	0.093	0.096	0.462	0.283	0.295	0.647†	0.331	0.188	0.48
	[0.335]	[0.283]	[1.290]	[1.156]	[0.919]	[1.914]	[1.363]	[0.642]	[1.550]
M/B	-0.022	0.118	0.193	-0.019	0.168	0.218	-0.031	0.175	0.21
	[-0.179]	[0.668]	[1.235]	[-0.165]	[0.864]	[1.425]	[-0.237]	[0.935]	[1.370]
Financial/Nonfinancial	-1.282	-0.757	-0.868	-1.335†	-1.219	-1.222	-1.505*	-0.251	-0.213
	[-1.623]	[-0.776]	[-0.805]	[-1.710]	[-1.138]	[-1.061]	[-1.987]	[-0.307]	[-0.236]
ROA	0.482	-0.097	1.266	0.307	1.065	2.392	0.574	-0.407	0.838
	[0.270]	[-0.039]	[0.499]	[0.170]	[0.396]	[0.872]	[0.315]	[-0.165]	[0.318]
RET1Y	3.57	3.736	2.04	3.642	5.868†	3.009	0.61	0.717	-1.367
	[1.568]	[1.241]	[0.661]	[1.589]	[1.798]	[0.922]	[0.141]	[0.134]	[-0.251]
SQM_RET	0.076	0.348	0.263	0.091	0.286	0.228	0.121	0.33	0.274
	[0.331]	[1.275]	[1.040]	[0.400]	[1.002]	[0.892]	[0.523]	[1.188]	[1.062]
Cash_Flow_Rights	0.142	-0.015	-0.895	0.004	-0.283	-0.983	0.273	0.201	-0.459
	[0.142]	[-0.012]	[-0.666]	[0.004]	[-0.227]	[-0.716]	[0.272]	[0.173]	[-0.349]
Wedge	6.096†	-2.176	-2.733	6.223†	-2.227	-3.082	7.443*	0.173	0.644
	[1.890]	[-0.679]	[-0.744]	[1.933]	[-0.643]	[-0.793]	[2.319]	[0.064]	[0.223]
Low_Disclosure	1.433†	0.591	0.235	1.294†	0.442	0.251	1.744*	1.317†	0.981
	[1.831]	[0.753]	[0.261]	[1.672]	[0.562]	[0.282]	[2.356]	[1.862]	[1.331]
Log_CEO_Total_Compensation	0.353†	0.148	0.11						
	[1.836]	[0.729]	[0.500]						
CEO_%_Variable_Comp				1.022	-2.738*	-1.559			
				[1.055]	[-2.094]	[-1.082]			
Quartile_3_CEO_Tot_Comp							-0.043	0.24	-0.055
							[-0.080]	[0.388]	[-0.082]
Quartile_2_CEO_Tot_Comp							-0.174	0.21	-0.024
							[-0.247]	[0.252]	[-0.028]
Quartile_1_CEO_Tot_Comp (Lowest)							-0.735	-0.422	-0.635
							[-0.728]	[-0.344]	[-0.509]
Remuneration_Committee	-2.114	-0.199	-0.485	-1.192	0.426	-0.316	-0.988	0.666	0.708
	[-1.576]	[-0.155]	[-0.356]	[-0.979]	[0.333]	[-0.253]	[-0.812]	[0.508]	[0.550]
Constant	-2.219	-4.075†	-5.621*	-2.013	-4.863*	-6.148*	-1.474	-3.928	-5.426†
	[-1.102]	[-1.715]	[-2.256]	[-1.013]	[-1.960]	[-2.383]	[-0.625]	[-1.325]	[-1.805]
R-squared	0.143	0.059	0.063	0.124	0.092	0.074	0.136	0.053	0.064
Observations	153	135	157	150	133	154	156	137	160

The table reports the results of Logit regressions with a dummy for "Against" recommendation issued by ISS and/or GL as dependent variable and firms characteristics as independent variables. All variables are defined in the Appendix. The t-statistics are presented in parentheses.
***, **, *, † denote significance at the .001, .01, .05, .10 level.

In a last set of models we examine whether firms targeted by both PAs differ from those targeted by only one of them. We estimate a logistic regression where the dependent variable, ISS&GL Against, is equal to one if both PAs recommend Against, and zero otherwise. Results are substantially confirmed, although the relations are generally weaker.

5 Determinants of shareholder dissent

5.1 Total shareholder dissent

We analyze the relation between PA recommendations and shareholder voting. To this end, following prior studies on compensation-related activism (Ertimur et al 2011) and shareholder voting (Gillan and Starks 2000, Ertimur et al 2010, 2013), we estimate an OLS regression where the dependent variable is SOP Voting Dissent.

Following Ertimur et al (2013), we implement a two-step research strategy to gauge the influence of PA recommendations. First, we run a benchmark model, regressing shareholder dissent on the same variables used in the analysis of PA recommendations. Then, we add a set of dummy variables to capture the additional influence of PA recommendations on SOP shareholder voting. The results for our first step are reported in Table 3 (models (1) to (3)).

The results are coherent with Belcredi et al (2014). Total shareholder dissent is strongly, negatively correlated with disclosure (actually, it is positively correlated with the "low disclosure" dummy), while firm performance, governance quality and CEO remuneration have a limited impact. Total dissent is also influenced by firm characteristics: a) it is positively correlated with firm size (contrary to what happens in the US), possibly indicating a closer scrutiny by investors in larger firms. This is consistent with the structure of the Italian stock market, institutional investors typically buy relatively more liquid blue chips, accounting for the bulk of market capitalization; b) it is lower in financial firms, subject to a stricter regulatory regime (and where the shareholder vote is binding in nature); c) above all, shareholder dissent is strongly dependent on firm ownership structure.

First, dissent is decreasing in the CFR held by the ultimate shareholder, who can barely be expected to vote against the remuneration policy adopted by the board she has, substantially, appointed. An additional, not mutually exclusive explanation may be that an ultimate shareholder holding a higher stake (in terms of CFR) may exert a stronger control over managerial pay-related conflicts of interest, thereby reducing dissent also by minority shareholders. Finally, dissent is decreasing in the CFR-VR wedge, which gives the ultimate shareholder additional grip on GM deliberations. The explanatory power of our model (in terms of adjusted R^2) is above 30%, i.e. twice as high as the benchmark model of Ertimur et al (2013) on US data. Total dissent in Italy is substantially explained by firm size, ownership structure and (low) disclosure.

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Table 3 – Determinants of Total Shareholder Dissent

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
ISS_Against				0.043**		0.051**	
				[2.908]		[3.060]	
GL_Against					0.043*	0.007	
					[1.998]	[0.353]	
ISS&GL_Against							0.056*
							[2.207]
Only_ISS							0.031
							[1.544]
Only_GL							0.073*
							[2.037]
Log Total Assets	0.033**	0.033**	0.035**	0.036***	0.039**	0.048***	0.031*
	[2.728]	[3.044]	[3.192]	[3.634]	[2.799]	[4.218]	[2.550]
M/B	0.003	0.003	0.002	0.002	0.003	0.001	0.002
	[0.904]	[0.961]	[0.834]	[0.763]	[0.846]	[0.298]	[0.831]
Financial/Nonfinancial	-0.063	-0.064	-0.065†	-0.059†	-0.059	-0.060†	-0.048
	[-1.654]	[-1.652]	[-1.762]	[-1.874]	[-1.515]	[-1.943]	[-1.275]
ROA	0.064	0.084	0.065	0.045	0.116	0.131	0.056
	[0.699]	[0.880]	[0.694]	[0.595]	[0.976]	[1.379]	[0.613]
RET1Y	0.167	0.173	0.002	0.132	0.148	0.124	0.131
	[1.607]	[1.599]	[0.007]	[1.537]	[1.197]	[1.243]	[1.269]
SQM_RET	-0.004	-0.002	-0.004	-0.004	-0.002	0.004	-0.006
	[-0.441]	[-0.227]	[-0.385]	[-0.467]	[-0.148]	[0.401]	[-0.607]
Cash_Flow_Rights	-0.221***	-0.223***	-0.232***	-0.192***	-0.193***	-0.156***	-0.226***
	[-4.585]	[-4.560]	[-4.784]	[-4.849]	[-3.682]	[-3.718]	[-4.741]
Wedge	-0.323**	-0.334**	-0.340**	-0.305**	-0.276*	-0.283**	-0.347**
	[-2.694]	[-2.780]	[-2.821]	[-3.088]	[-2.208]	[-2.789]	[-2.891]
Low_Disclosure	0.151***	0.156***	0.148***	0.078**	0.171***	0.080*	0.138***
	[4.704]	[4.824]	[4.703]	[2.821]	[4.586]	[2.525]	[4.332]
Log_CEO_Total_Compensation	0.001			-0.002	-0.006	-0.008	-0.002
	[0.133]			[-0.261]	[-0.773]	[-1.227]	[-0.271]
CEO_%_Variable_Comp		-0.008					
		[-0.189]					
Quartile_3_CEO_Tot_Comp			-0.017				
			[-0.537]				
Quartile_2_CEO_Tot_Comp			-0.009				
			[-0.210]				
Quartile_1_CEO_Tot_Comp (Lowest)			-0.049				
			[-0.722]				
Remuneration_Committee	0.014	0	0.021	-0.007	-0.031	-0.055	0.021
	[0.302]	[-0.005]	[0.489]	[-0.182]	[-0.558]	[-1.242]	[0.455]
Constant	-0.106	-0.09	-0.047	-0.112	-0.08	-0.132	-0.087
	[-1.248]	[-1.029]	[-0.375]	[-1.615]	[-0.758]	[-1.559]	[-1.031]
R-squared	0.308	0.318	0.313	0.353	0.344	0.393	0.345
Observations	147	144	148	143	126	122	147

The table reports the results of OLS regressions with Total Shareholder Dissent as dependent variable and ISS and/or GL "Against" recommendation and firms characteristics as independent variables. All variables are defined in the Appendix. The t-statistics are presented in parentheses.
***, **, *, † denote significance at the .001, .01, .05, .10 level.

The second step of our analysis aims to gauge the influence of PAs on the voting outcome. To this end, in models (4) to (7) we add a set of dummies capturing PA recommendations (ISS Against, GL Against, and ISS&GL Against) to our benchmark

regression.[22] Total dissent is, indeed, correlated with proxy advisor recommendations, but PA dummies add little explanatory power. In model (4), the coefficient of ISS Against is positive at 0.043 and statistically significant (this compares with 0.268 in the US: Ertimur et al 2013) and the R^2 is 35.3% (65.7% in the US). Similarly, in model (5), the coefficient of GL Against is positive and significant at 0.043 and the R^2 is 34.4%. In model (6), we include both ISS Against and GL Against. The R^2 increases to 39.3%. Notably, relative to models (4) and (5), in model (6) the coefficient of ISS remains substantially the same, while that of GL Against is lower and not statistically significant. In model (7), after adding the ISS&GL (jointly) Against dummy, it is the coefficient of ISS Against to lose significance. We interpret this evidence as consistent with ISS having a stronger influence (ISS is the dominant player in the market for proxy advisory services) on shareholder voting in companies targeted by both PAs, with GL providing, nonetheless, additional useful information.

To sum up, the influence of PAs on total dissent looks quite limited in Italy: for example, the influence of ISS on the shareholder vote is just 16% of what is observed in the US (0.043/0.268 = 0.1604). Furthermore, the inclusion of PA recommendations adds little explanatory power to the model (the inclusion of the ISS Against dummy leads to an increase in R^2 from 30 to 35%; even the best-fitting model – including both ISS and GL against dummies – has a R^2 around 39%). For the sake of comparison, in the US the inclusion of PA recommendations enhances R^2 from 15% to 66% (for the ISS Against dummy) and to 82% (for the model including both dummies).[23]

5.2 Institutional investor dissent

Institutional investors may follow a different voting pattern on SOP issues, both to justify their role as stewards of other people's money and as a response to external pressures for engaging with investee companies. Descriptive statistics showed that they dissent more frequently than other shareholders (institutional investor dissent is 29%, vs. 6% for total dissent), implying that they tend to assume a rather active stance toward investee companies, at least on directors' remuneration policy.

Although institutional investors have often been recognized as a likely candidate for low-cost, corporate governance activism (Renneboog and Szilagyi 2011, 2013), no analysis has been performed – so far – on the votes they actually cast, mostly due to data availability constraints. Previous literature investigated the impact of PA recommendations regressing total dissent on a set of variables including explanatory proxies for institutional investors' ownership; however, data availability

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22 To keep things simple, we report the results of regressions where CEO remuneration structure is defined in terms of total pay. The adoption of different specifications (e.g. variable/total compensation or remuneration quartiles) does not change our results.

23 We also look at the possible link between PAs' advice and market prices and find no robust correlation. This result might indicate that in the first year of implementation of a mandatory vote on directors' remuneration, proxy recommendations on SOP might have come to the market as a surprise and – not being expected - they were paid only limited attention.

constraints have precluded, so far, to analyze institutional investors' actual voting behavior. Given the well-known tendency to rational apathy of several institutional investors, this aspect is key to understand the role they actually play in corporate governance.

Capitalizing on the peculiar features of Italian regulation, mandating on line disclosure of GM minutes (and their annexes), we have been able to fill in this gap: a) we identify shareholders which may be qualified as institutional investors explicitly; b) we count the votes actually cast by each of them on the first section of the Remuneration Report; c) consequently, we analyze the determinants of their dissent on SOP and its relation with PA recommendations.

It would be incorrect to analyze institutional investors' dissent (and the influence of PA recommendations) merely on the basis of the number of their negative votes, since this measure is influenced by their higher or lower participation to a firm's equity capital. It is preferable, instead, to measure their dissent as the negative votes they cast as a percentage of the votes cast by all institutional investors, i.e. (Inst.Against + Inst.Abstain)/Inst.investor votes. As already observed, institutional investors dissent more frequently on SOP issues than the average shareholder.

We expect institutional shareholder votes to be associated with PA recommendations; the association should be stronger than for the average shareholder, since institutional investors have a strong incentive to outsource research and analysis activities to PAs (Choi et al 2010, Ertimur et al 2013), particularly if they hold small equity stakes. To analyze the relation of PA recommendations with institutional investor voting, we follow the same two-step research strategy implemented for total shareholder dissent. Our results are reported in Table 4.

Consistent with our expectations, institutional investors are much more active than the average shareholder on SOP issues, and their vote is strongly correlated with PA recommendations. Panel A reports results for institutional investors as a whole. The coefficients for the dummies capturing PA recommendations are positive and much higher than those obtained for total dissent. In model (4) ISS Against is positive at 0.457 (i.e. more than 10 times the coefficient in the regression for total dissent) and R^2 is as high as 60.1% (i.e. twice the R^2 in the regression for total dissent). Similarly, in model (5), the coefficient of GL Against is positive at 0.201 and significant (it is around 5 times the coefficient in our regression for total dissent). Even in a country where ownership is concentrated (and, therefore, the voting outcome is often known in advance), institutional investors are quite active on SOP, and their voting behavior is strongly correlated with PA recommendations. This feature remains hidden from view, when looking only at total dissent, since this measure is overwhelmingly affected by the votes cast by other categories of shareholders, holding larger equity stakes.

Table 4 – (Panel A) Determinants of Institutional Investors' Dissent

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
ISS_Against				0.457***		0.442***	
				[11.021]		[10.258]	
GL_Against					0.201**	0.095*	
					[3.241]	[2.021]	
ISS&GL_Against							0.531***
							[9.591]
Only_ISS							0.420***
							[8.892]
Only_GL							0.047
							[0.590]
Log Total Assets	0.028	0.044	0.057	0.002	-0.001	-0.009	-0.005
	[0.699]	[1.221]	[1.547]	[0.080]	[-0.016]	[-0.324]	[-0.168]
M/B	0.003	0.002	0.002	0.002	0.005	0.003	0.002
	[0.329]	[0.264]	[0.248]	[0.280]	[0.583]	[0.423]	[0.359]
Financial/Nonfinancial	-0.093	-0.105	-0.14	0.026	-0.064	0.032	0.037
	[-0.817]	[-0.906]	[-1.237]	[0.327]	[-0.586]	[0.406]	[0.461]
ROA	0.02	-0.022	0.044	0.01	-0.217	0.027	-0.021
	[0.066]	[-0.072]	[0.140]	[0.049]	[-0.623]	[0.110]	[-0.098]
RET1Y	0.886**	0.890*	0.55	0.299	0.750*	0.149	0.316
	[2.626]	[2.536]	[0.570]	[1.233]	[2.117]	[0.576]	[1.312]
SQM_RET	0.017	0.025	0.021	0.015	-0.029	-0.028	0.01
	[0.513]	[0.756]	[0.646]	[0.625]	[-0.791]	[-1.045]	[0.463]
Cash_Flow_Rights	-0.271†	-0.289†	-0.292†	-0.234*	-0.287†	-0.297**	-0.244*
	[-1.753]	[-1.840]	[-1.855]	[-2.142]	[-1.884]	[-2.738]	[-2.277]
Wedge	0.462	0.478	0.46	-0.004	0.551	0.008	0.051
	[1.254]	[1.293]	[1.222]	[-0.015]	[1.557]	[0.032]	[0.193]
Low_Disclosure	-0.003	-0.002	-0.005	-0.142†	-0.042	-0.134†	-0.113
	[-0.025]	[-0.016]	[-0.046]	[-1.741]	[-0.400]	[-1.685]	[-1.479]
Log_CEO_Total_Compensation	0.034			0.011	0.035	0.013	0.012
	[1.458]			[0.637]	[1.548]	[0.783]	[0.707]
CEO_%_Variable_Comp		0.171					
		[1.263]					
Quartile_3_CEO_Tot_Comp			-0.024				
			[-0.242]				
Quartile_2_CEO_Tot_Comp			0.007				
			[0.048]				
Quartile_1_CEO_Tot_Comp (Lowest)			-0.098				
			[-0.440]				
Remuneration_Committee	0.068	0.098	0.138	0.17	0.051	0.214†	0.176†
	[0.464]	[0.677]	[0.944]	[1.627]	[0.327]	[1.908]	[1.719]
Constant	-0.362	-0.29	-0.247	-0.201	-0.106	-0.083	-0.169
	[-1.226]	[-0.974]	[-0.555]	[-0.962]	[-0.351]	[-0.383]	[-0.824]
R-squared	0.173	0.174	0.165	0.601	0.249	0.633	0.616
Observations	128	126	128	125	120	117	128

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Table 4 – (Panel B) Determinants of Small Institutional Investors' Dissent

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
ISS_Against				0.522***		0.522***	
				[13.770]		[13.381]	
GL_Against					0.215**	0.061	
					[3.222]	[1.406]	
ISS&GL_Against							0.569***
							[10.708]
Only_ISS							0.508***
							[11.150]
Only_GL							0.143†
							[1.724]
Log Total Assets	0.006	0.022	0.035	-0.012	-0.021	-0.022	-0.021
	[0.139]	[0.577]	[0.907]	[-0.468]	[-0.494]	[-0.852]	[-0.760]
M/B	0.006	0.006	0.006	0.003	0.008	0.004	0.005
	[0.628]	[0.601]	[0.564]	[0.575]	[0.802]	[0.614]	[0.769]
Financial/Nonfinancial	-0.088	-0.103	-0.137	0.035	-0.067	0.037	0.05
	[-0.729]	[-0.842]	[-1.157]	[0.477]	[-0.575]	[0.527]	[0.648]
ROA	0.178	0.155	0.168	0.131	-0.116	0.156	0.106
	[0.550]	[0.473]	[0.507]	[0.666]	[-0.313]	[0.694]	[0.521]
RET1Y	0.866*	0.913*	0.665	0.221	0.719†	0.09	0.164
	[2.420]	[2.449]	[0.658]	[0.995]	[1.893]	[0.386]	[0.696]
SQM_RET	0.034	0.039	0.038	0.03	-0.011	-0.004	0.022
	[0.967]	[1.109]	[1.089]	[1.405]	[-0.292]	[-0.149]	[0.992]
Cash_Flow_Rights	-0.195	-0.214	-0.216	-0.128	-0.22	-0.197*	-0.183†
	[-1.201]	[-1.294]	[-1.311]	[-1.294]	[-1.370]	[-2.015]	[-1.781]
Wedge	0.616	0.644	0.592	0.127	0.671†	0.086	0.085
	[1.591]	[1.654]	[1.505]	[0.534]	[1.799]	[0.373]	[0.338]
Low_Disclosure	0.04	0.038	0.039	-0.169*	-0.005	-0.166*	-0.091
	[0.354]	[0.328]	[0.338]	[-2.286]	[-0.045]	[-2.335]	[-1.257]
Log_CEO_Total_Compensation	0.032			0.005	0.034	0.007	0.003
	[1.310]			[0.325]	[1.400]	[0.456]	[0.180]
CEO_%_Variable_Comp		0.102					
		[0.713]					
Quartile_3_CEO_Tot_Comp			0.003				
			[0.028]				
Quartile_2_CEO_Tot_Comp			0.053				
			[0.341]				
Quartile_1_CEO_Tot_Comp (Lowest)			-0.074				
			[-0.319]				
Remuneration_Committee	0.141	0.18	0.21	0.232*	0.124	0.287**	0.257**
	[0.917]	[1.184]	[1.374]	[2.457]	[0.757]	[2.862]	[2.636]
Constant	-0.314	-0.26	-0.273	-0.19	-0.056	-0.097	-0.109
	[-1.008]	[-0.827]	[-0.587]	[-1.000]	[-0.175]	[-0.499]	[-0.549]
R-squared	0.16	0.157	0.16	0.695	0.23	0.724	0.676
Observations	125	123	125	122	118	115	125

Table 4 – (Panel C) Determinants of Institutional Blockholders' Dissent

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
ISS_Against				0.186†		0.123	
				[1.949]		[1.207]	
GL_Against					0.215†	0.212†	
					[1.883]	[1.751]	
ISS&GL_Against							0.360*
							[2.696]
Only_ISS							0.099
							[0.918]
Only_GL							-0.01
							[-0.056]
Log Total Assets	0.013	-0.013	0.06	0.012	0.052	0.03	0.01
	[0.150]	[-0.161]	[0.848]	[0.148]	[0.558]	[0.314]	[0.122]
M/B	-0.002	-0.012	-0.001	-0.024	0.046	0.017	-0.006
	[-0.039]	[-0.190]	[-0.019]	[-0.400]	[0.721]	[0.267]	[-0.110]
Financial/Nonfinancial	-0.011	0.034	-0.117	0.011	-0.021	0.023	0.033
	[-0.042]	[0.128]	[-0.530]	[0.047]	[-0.085]	[0.091]	[0.140]
ROA	-0.602	-0.933	-0.614	-0.285	-0.717	-0.459	-0.431
	[-0.919]	[-1.375]	[-0.975]	[-0.437]	[-1.117]	[-0.699]	[-0.674]
RET1Y	0.543	0.286	-0.169	0.303	0.147	0.081	0.194
	[0.879]	[0.436]	[-0.110]	[0.491]	[0.229]	[0.126]	[0.323]
SQM_RET	-0.008	0.02	-0.017	-0.008	-0.052	-0.051	-0.035
	[-0.143]	[0.333]	[-0.301]	[-0.141]	[-0.881]	[-0.859]	[-0.615]
Cash_Flow_Rights	-0.237	-0.324	-0.25	-0.364	-0.088	-0.258	-0.328
	[-0.901]	[-1.142]	[-0.962]	[-1.375]	[-0.316]	[-0.883]	[-1.293]
Wedge	-0.982	-1.02	-1.328†	-1.329†	-0.699	-0.991	-0.896
	[-1.427]	[-1.446]	[-1.907]	[-1.935]	[-1.021]	[-1.401]	[-1.273]
Low_Disclosure	0.118	0.124	0.177	0.137	0.104	0.152	0.083
	[0.772]	[0.825]	[1.139]	[0.837]	[0.678]	[0.929]	[0.565]
Log_CEO_Total_Compensation	0.026			0.008	0.017	0.006	0.01
	[0.791]			[0.233]	[0.516]	[0.164]	[0.318]
CEO_%_Variable_Comp		0.475					
		[1.672]					
Quartile_3_CEO_Tot_Comp			0.06				
			[0.353]				
Quartile_2_CEO_Tot_Comp			0.075				
			[0.295]				
Quartile_1_CEO_Tot_Comp (Lowest)			-0.194				
			[-0.527]				
Remuneration_Committee	0.091	0.123	0.073	0.004	0	0	-0.002
	[0.271]	[0.365]	[0.211]	[0.011]	[.]	[.]	[-0.007]
Constant	-0.199	0.148	-0.072	0.058	-0.305	-0.032	0.092
	[-0.367]	[0.255]	[-0.102]	[0.107]	[-0.558]	[-0.056]	[0.174]
R-squared	0.138	0.189	0.193	0.225	0.201	0.26	0.284
Observations	54	52	54	53	51	50	54

Tables report the results of OLS regressions with dissent as dependent variable and ISS and/or GL "Against" recommendation and firms characteristics as independent variables. Dissent is defined as Institutional Investors' Dissent (Panel A), Small Institutional Investors' Dissent (Panel B) and Institutional Blockholders' Dissent (Panel C). All variables are defined in the Appendix. The t–statistics are presented in parentheses.

***, **, *, † denote significance at the .001, .01, .05, .10 level.

Results are substantially confirmed in models (6) and (7), where both ISS Against and GL Against and/or a ISS&GL Against dummy are included. The vote of institutional investors is strongly correlated with PA recommendations. ISS seemingly has a stronger influence, as demonstrated by the relative size of the regression coefficients, and is apparently followed by most institutional investors when PAs provide divergent recommendations. However, GL is far from irrelevant, even after taking into account the effects of ISS recommendations. This may be connected to two, not mutually exclusive factors: on one hand, some firms are targeted only by ISS or GL, creating an obvious channel of exclusive influence. On the other hand, dissent is much stronger where both PAs recommend to vote Against, implying that even investors normally relying on ISS consider the issue of a negative report by GL an additional relevant piece of information. The inclusion of PA recommendations adds great explanatory power to our model (the inclusion of the ISS Against dummy leads to an increase in R^2 from 16.5 to 60.1%, an effect almost identical to that found by Ertimur et al (2013) for total shareholder dissent in the US).

As already observed in previous literature (Choi et al 2010), it is difficult to say whether the association between PA recommendations and shareholder votes is due to a causal relationship or simply to investors and PAs considering the same factors when taking their decisions (i.e. voting and recommending for or against, respectively). Actually, these explanations are not mutually exclusive, since different categories of shareholders may follow different voting strategies. Arguably, the sensitivity to PA recommendations depends on the incentives of institutional investors to gather and process information independently, which in turn have been proved to depend on the size of their holdings (Cronqvist and Fahlenbrach 2009, Agrawal and Nasser 2012).

5.3 Institutional blockholders' vs. nonblockholders' dissent

We distinguish between institutional blockholders and investors holding smaller stakes (i.e. above or below 2% of equity). We expect the relation to be stronger for the latter, since the incentive to outsource research and analysis activities to PAs should be decreasing in the stake held. Furthermore, nonblockholders are often internationally diversified mutual or pension funds, which have little incentive to bear the costs implied by independent analysis of thousands of companies in their portfolios; this is especially true in the case of Italian firms, only a tiny minority of which may be considered sufficiently large to justify the investment. Finally, blockholders may dissent less frequently because they may often negotiate directly with the board (or with the ultimate shareholder) and therefore agree more frequently with management proposals.

Consistent with our expectations, the influence of PA recommendations is almost always higher on nonblockholders (Table 4, Panel B). In model (4) ISS Against is positive at 0.522 and R^2 is 69.5%. In model (5) GL is also significant; GL shows also a significant additional effect in model (7). Actually, the results for institutional investors as a whole seem to be driven by nonblockholders (mostly pension and

mutual funds), while institutional blockholders, having a stronger incentive to perform their own research, appear to be less sensitive to PA recommendations (see Table 4, Panel C, models (4) to (7)).

While it is difficult to estimate whether PA recommendations have actually an impact in Italy, it is reasonable to assume that at least part of the association is causal. Following Ertimur et al (2013), it is possible to estimate the effect of the causal relationship, assuming that (1) blockholders vote independently of ISS recommendations, while only some of the institutions holding smaller stakes do so; and (2) institutions performing their own research reach on average the same conclusions. Our results suggest that about 18.6% of investors doing their own research will vote *Against* when ISS also recommends *Against*. Consequently, at least about 33.6% of the institutional nonblockholders (52.2%–18.6%) simply follow ISS recommendations, providing a lower-bound estimate of the causal effect of ISS. If, instead, institutions holding smaller stakes simply follow ISS, 52.2% may be considered an upper-bound estimate of ISS's causal influence. Both the lower and upper bound estimates of the causal impact are higher than those found by Ertimur et al (2013) on US data (33.6% and 52.2% versus 10% and 34.4% in the US). Therefore, the effect of PAs on institutional investors' voting in Italy appears to be at least as strong as (and probably stronger than) that observed in the US.

5.4 The influence of individual concerns

We finally analyze the influence of the details of PA reports. Specifically, we investigate whether the sensitivity of institutional investors' votes to PA recommendations varies with the rationale for the recommendation. To this end, we substitute the coefficients of *ISS* and *GL Against* with variables capturing the number and type of concerns identified in the PA reports. Since the structure of ISS and GL reports is not the same, we adopt partially different regression specifications, so as to capture the concerns explicitly identified by each proxy advisor. In untabulated tests we obtain that institutional blockholders are substantially insensitive to the contents of PA reports. Therefore, in Table 5 we report only the results for nonblockholders.[24]

Institutional investors appear to look through PA final recommendations and to vote against the remuneration policy where specific reasons of concern exist about executive remuneration structure and severance pay. In model (1) institutional nonblockholders' votes are regressed against the number of concerns expressed by ISS; model (2) repeats the analysis comparing situations where ISS formulates one single concern (or, respectively, multiple concerns)[25], and 0 otherwise. Contrary to what happens in the US, institutional investors are not particularly sensitive to the number of concerns in PA reports. In model (3) we introduce variables capturing the quality of ISS concerns; to this end, we use a set of dummy variables, taking value

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24 The results for institutional shareholders as a whole (not reported) are quite similar.

25 Model (2) considers both a "single concern" and a "multiple concern" dummy, i.e. compares such situations with cases where no concern is expressed.

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one if a reason of concern is formulated in the "Analysis" subsection of the ISS report (covering 5 different aspects of the firm's remuneration policy). Table 8 shows that institutional investors do not follow PA recommendations blindly; on the opposite, they appear to look through the final recommendation at the specific reasons of concern underlined in the reports.

Interestingly, investors' decisions are not influenced by the timeliness of the firm's Remuneration Report or even by the PA judgment on the quality of such disclosure (on apparently important features such as performance criteria, caps, and severance payments).[26] Neither do they seem particularly worried by governance issues, such as a "suboptimal" composition of the remuneration committee (i.e. including company executives). Instead, the reasons of concern they seem to care most for are the structure and long-term value creation of the proposed remuneration policy: the coefficient is here positive (0.22) and significant. The inclusion of provisions allowing the board to attribute "excessive" severance pay (conventionally defined as higher than 24 months' pay) to leaving managers is also relevant: the coefficient is here 0.365 and significant. Severance pay is a highly sensitive issue for institutional investors: actually, the impact of severance pay concerns on institutional investor voting decisions is 2/3 higher than that of problems with the general structure of the remuneration policy (0.365 / 0.22 = 1.66). Model (6) repeats the analysis for the quality of GL concerns, distinguishing between issues related to disclosure and to the structure of the firm's remuneration policy (drawn from the "overall disclosure" and "overall structure" subsections in GL reports). Here, no specific impact is apparent.

To sum up, institutional investors seem not to follow blindly PA final recommendations to vote "for" or "against" a firm's remuneration policy. Instead, they seem to look through the recommendations, at the specific reasons for concern identified in PA reports. This is true at least for ISS, whereas the evidence for GL is less clear. Institutional investors are apparently more interested in the structure (and pay-for-performance) of the remuneration policy, while disclosure and governance issues are less relevant. Severance pay provisions possibly generating payments deemed "excessive" according to the standard conventionally adopted by PAs (24 months' pay) are – by far – the most relevant reason of concern for institutional investors (in particular, for nonblockholders such as mutual and pension funds).

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26 To capture the effects of the specific concerns in this matter expressed by Pas, while – at the same time –avoiding collinearity problems, the regressions reported in Table 5 do not include the "low disclosure" dummy. The inclusion of the dummy, however, does not alter our results significantly (results not reported). The same is true for different specifications excluding the "multiple concerns" dummy or considering individual concerns separately.

Table 5 – Determinants of Institutional Blockholders' Dissent

	ISS Concerns			GL Concerns		
	(1)	(2)	(3)	(4)	(5)	(6)
Number of concerns	-0.013			0.053†		
	[-0.451]			[1.876]		
Single concern		-0.036			-0.012	
		[-0.527]			[-0.184]	
Multiple concerns		-0.024	0.026		-0.273*	-0.286
		[-0.333]	[0.464]		[-2.115]	[-1.476]
ISS: Basic features of compensation policy NOT disclosed			0.046			
			[0.758]			
ISS: Compensation Committee includes executives			0.027			
			[0.305]			
ISS: Concerns exist on compensation structure and LT value creation			0.220***			
			[3.860]			
ISS: Severance payments exceed 24 months' pay			0.365***			
			[5.879]			
GL concern structure						-0.026
						[-0.354]
GL concern disclosure						0.041
						[0.306]
Log Total Assets	0.01	0.008	-0.023	-0.051	0.036	0.036
	[0.238]	[0.180]	[-0.559]	[-1.095]	[0.821]	[0.817]
M/B	0.004	0.004	0.004	0.008	0.009	0.009
	[0.380]	[0.424]	[0.548]	[0.856]	[0.972]	[0.970]
Financial/Nonfinancial	-0.117	-0.117	0.023	-0.06	-0.12	-0.121
	[-1.029]	[-1.023]	[0.219]	[-0.525]	[-1.065]	[-1.071]
ROA	0.163	0.153	0.11	-0.314	-0.003	-0.017
	[0.500]	[0.465]	[0.389]	[-0.823]	[-0.009]	[-0.044]
RET1Y	0.816*	0.821*	0.491	0.728*	0.702†	0.672†
	[2.373]	[2.375]	[1.461]	[2.016]	[1.876]	[1.763]
SQM_RET	0.02	0.02	0.032	-0.01	0.061†	0.06
	[0.569]	[0.579]	[1.044]	[-0.258]	[1.680]	[1.648]
Cash_Flow_Rights	-0.102	-0.101	0.013	-0.072	-0.071	-0.072
	[-0.655]	[-0.645]	[0.087]	[-0.456]	[-0.441]	[-0.446]
Wedge	0.552	0.568	0.372	0.637†	0.931*	0.939*
	[1.368]	[1.400]	[0.951]	[1.749]	[2.411]	[2.420]
Log_CEO_Total_Compensation	0.047*	0.047†	0.022	0.053*	0.043†	0.043†
	[1.984]	[1.957]	[0.664]	[2.259]	[1.831]	[1.809]
Remuneration_Committee	-0.237*	-0.230*	-0.134	-0.209†	-0.328**	-0.332**
	[-2.174]	[-2.084]	[-0.728]	[-1.876]	[-2.927]	[-2.945]
Constant	-0.063	-0.046	-0.011	0.266	-0.132	-0.115
	[-0.225]	[-0.164]	[-0.034]	[0.926]	[-0.452]	[-0.388]
R-squared	0.159	0.159	0.481	0.184	0.246	0.248
Observations	147	147	108	144	125	125

The table reports the results of OLS regressions with Institutional Blockholders' Dissent as dependent variable and ISS and/or GL concerns and firms characteristics as independent variables. All variables are defined in the Appendix. The t-statistics are presented in parentheses.
***, **, *, † denote significance at the .001, .01, .05, .10 level.

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6 Conclusions

Institutional investors are often criticized for their insufficient "engagement" with listed companies. Actually, information and other transaction costs limit their capacity to actively monitor investee firms, and to engage with their management. A partial solution is offered by Proxy Advisors (PAs), providing proxy voting services on a subscription basis. We use Say-On-Pay (SOP) in Italian listed firms to investigate PA activity and (institutional) shareholder voting behavior. Making use of a unique dataset, including information on how each shareholder voted in 2012, we analyze the behavior of different classes of shareholders and their relation with PA recommendations. Our main results may be summarized as follows.

1) While total shareholder dissent is rather low, in line with what happens in other developed countries, dissent by institutional investors (mostly, internationally diversified mutual and pension funds) is surprisingly high: average (median) dissent among institutional investors was around 29% (10%) (versus average (median) values of total dissent equal to 6% (0%)). Average (median) dissent increases further to 32% (17%) amongst institutional investors holding small equity stakes (typically, mutual and pension funds).

2) Capitalizing on the peculiar features of Italian regulation, we track the actual voting decisions of institutional investors, thereby filling a gap in the existing literature on activism and SOP voting. We are also therefore to separately trace the influence of PAs on institutional investors' voting, a relevant issue in the current policy debate at the EU level.

3) The vote of institutional investors is strongly correlated with PA recommendations. The influence of PA recommendations is almost always higher on nonblockholders (mostly internationally diversified pension and mutual funds), while institutional blockholders, having a stronger incentive to perform their own research, appear to be less sensitive to PA recommendations.

4) While it is difficult to estimate the exact causal impact of PAs, preliminary estimates show that the effect of PAs on institutional investors' voting in Italy is at least as strong as (and probably stronger than) that observed in the US. This is coherent with the weight of non-domestic institutions, which can be hardly expected to independently analyze thousands of firms in their portfolios; and it is especially so in Italy, where most listed firms may be classified as small/medium cap firms on a comparative basis.

5) Institutional investors, however, do not follow PA recommendations blindly; on the opposite, they seem to take into account the specific reasons of concern underlined in the PA reports (in particular, the structure and long-term value creation of the proposed remuneration policy). Severance pay has, by far, the largest impact on the voting decisions of institutional investors (in particular, of nonblockholders such as mutual and pension funds).

6) As an aside to our main research results, we obtain evidence about the determinants of PA recommendations in Italy, i.e. a country where ownership is concen-

trated and the level of disclosure is lower than in Anglo-Saxon countries. Proxy advisors are more likely to recommend against a remuneration policy where firm disclosure is lower. PA recommendations are also related with CEO remuneration structure: our data show that, although no specific guideline was issued on the quantum of remuneration, ISS is more likely to issue an Against recommendation where CEO total compensation is higher, whereas GL is more likely to recommend Against where the % variable remuneration is lower. Different PAs seem to follow diverse approaches, possibly reflecting the preferences of a diverse client base. On the opposite, at least in 2012, firm performance does not seem to have influenced PA recommendations on remuneration policy.

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Description of ISS and GL concerns

Table A – Frequency of individual reasons of concern in ISS reports

concerns	frequency of concerns
severance pay >24 months' pay	35
compensation structure and long term value creation	103
the compensation committee includes executives	20
basic features of remuneration policy not disclosed	81
the report was not made available in a timely manner	1
total	*240*

Table A reports the frequency of individual reasons of concern underlined by ISS in the "Analysis" section of the Report issued for the 2012 AGMs. Multiple reasons of concern may be expressed for a single company.

Table B – Frequency distribution of the "Disclosure level" of individual companies, according to ISS

disclosure level	basic features of remuneration policy		
	disclosed	not disclosed	*total*
above average/good	35	2	*37*
average	49	22	*71*
below average/poor	15	54	*69*
total	*99*	*78*	*177*

Table B reports the number of companies classified by ISS as having a level of disclosure above/below average in Italy, as a function of concerns being expressed by ISS about "basic features of remuneration policy (being) not disclosed".

Table C – Description of GL concerns and ratings on compensation structure

compensation struc-ture rating	frequency of individual concerns				
	excessive severance agreements	long-term	performance	implementation of best practices (only for Ftse Mib companies)	other structure concerns
good (47 firms)	7	4	38	3	4
fair (80 firms)	19	44	48	16	9
poor (45 firms)	9	39	31	9	10
total	*35*	*87*	*117*	*28*	*23*

In Table C the rating assigned to compensation structure by GL is associated to the frequency of individual reasons of concern. Save for the *Implementation of best practices* category, coming directly from GL reports, the classification of concerns is the result of our own analysis. *Long-term* includes concerns related to the existence and structure of long-term incentive plans. *Performance* includes concerns related to the performance measurement adopted by the company. *Other structure concerns* includes concerns related to "Authority to award discretionary bonus", plans "Managed by interested parties" and "Director remuneration".

Table D – Description of GL concerns and ratings on compensation disclosure

disclosure rating	frequency of individual concerns				
	description of hurdles/targets not disclosed	implementation of best practices (only for Ftse Mib companies)	vesting schedules of awards not disclosed	performance metrics (or relative weights) not disclosed	other concerns
good (76 firms)	11	4			3
fair (74 firms)	31	14	7	34	8
poor (22 firms)	12	6	5	18	4
total	*54*	*24*	*12*	*52*	*15*

In Table D the rating assigned to compensation disclosure by GL is associated to the frequency of individual reasons of concern. Save for the *Implementation of best practices* category, coming directly from GL reports, the classification of concerns is the result of our own analysis. The definition of insufficient disclosure for *Description of hurdles/targets*, *Vesting schedules* and *Performance metrics* is straightforward. In *Other concerns* we grouped concerns related to "Severance agreements not disclosed", "Comparator group not disclosed", "Equity award determination process not disclosed", "No Proposed Long-Term Incentive Plan" and "Disclosure on variable compensation".

Table E – Joint distribution of GL ratings (on compensation structure and disclosure)

compensation structure	compensation disclosure			
	good	fair	poor	*total*
good	28	19		*47*
fair	28	42	10	*80*
poor	20	13	12	*45*
total	*76*	*74*	*22*	*172*

Table E reports the joint distribution of individual firm ratings (*Good/Fair/Poor*) on compensation disclosure and structure by GL.

Table F – Distribution of ISS and GL recommendations and ratings or concerns on SOP

	GL *For*	GL *Against*	ISS *For*	ISS *Against*
All firms	119 (69%)	53 (31%)	104 (52%)	97 (48%)
Poor compensation structure	1[a]	44 (98%)	37 (31%)	84 (69%)
Poor disclosure	1[b]	21 (95%)	11 (15%)	62 (85%)
Both compensation structure and disclosure are poor	0	12 (100%)	6 (10%)	53 (90%)

Table F reports, for each proxy advisor, the distribution of the recommendations according to the ratings expressed on compensation structure and disclosure. Since ISS does not assign an explicit rating to remuneration structure, we classify as "poor" compensation structure all firms where ISS expresses a concern with reference either to excessive severance payments (first item in Table A) or to the structure of remuneration and discretionary bonuses (second item in Table A).

[a] In this case GL expresses a concern with reference to some features of the company's compensation structure (namely, the absence of a long-term incentive plan and the absence of performance-based short-term incentives). However, GL explicitly states that "*While we do not believe these concerns are sufficiently grave to warrant voting against this proposal at this time, we urge the Company to take corrective measures to address each of these issues in due course. Specifically, we believe that the Company should include some form of variable compensation based on performance metrics. In the aggregate, however, considering that the executive chairman is a controlling shareholder, we do not consider any of the Company's compensation practices to be particularly contentious and find the interests of executives and shareholders to be appropriately aligned.*"
[b] In this case, GL states that :"*While we do not believe these concerns are sufficiently grave to warrant voting against this proposal at this time , we urge the company to take corrective measures to address each of these issues in due course. In the aggregate, however, we do not consider any of the Company's remuneration practices to be particularly contentious and find the interests of executives to be appropriately aligned.*" Consequently, despite the CEO's past fiscal year fixed salary was not disclosed and no performance long-term incentives are awarded, ISS issues an overall "For" proposal.

Table G – Joint distribution of ISS and GL recommendations on SOP

	GL FOR	GL AGAINST
ISS FOR	65 (39%)	18 (11%)
ISS AGAINST	51 (31%)	33 (20%)
agreement	*59%*	
agreement on controversial cases	*32%*	

Table G reports the joint distribution of ISS and GL recommendations on SOP.

Table H – Joint distribution of ISS comments and GL ratings on compensation disclosure

DISCLOSURE

ISS	GL		
	good	fair	poor
above average/good	24 (15%)	10 (6%)	1 (1%)
average	29 (18%)	29 (18%)	7 (4%)
below average/poor	18 (12%)	28 (18%)	12 (8%)
agreement	*66%*		
agreement on controversial cases	*18%*		

Table H reports the joint distribution of the number of companies classified by ISS as having a level of disclosure above/below average in Italy and GL disclosure ratings (good/fair/poor).

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Variable definitions

Firm characteristics

Log Total Assets: Natural log of Total Assets

Market Capitalization: market price of a share times the number of shares outstanding

M/B (Market to Book ratio): market value of equity divided by book value of equity

ROA: Accounting returns (Last year's EBITDA/Total Assets)

RET1Y: average dividend-adjusted stock returns over the last year prior to the shareholders' meeting year.

SQM_RET: standard deviation of stock returns over the last year prior to the shareholders' meeting year.

Fin/Nonfin: a dummy variable taking value 1 for financial companies and 0 otherwise.

CEO compensation

CEOFixedPay: natural log of salary and benefits paid to the CEO

CEOVarCash: natural log of variable cash compensation paid to the CEO

CEO_%_Variable_Comp: variable cash compensation paid to the CEO as a percentage of total compensation

CEOEquity: natural log of the annualized fair value of stock-grants and -options awarded to the CEO

CEOTotComp: natural log of cash (Fixed + Variable) + equity-based CEO compensation

Quartile_CEO_Tot_Comp1, 2, 3, 4: dummy variables for quartiles of CEOTotComp (*Quartile_4_CEO_Tot_Comp1* is the top compensation quartile)

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Ownership

Cash_Flow_Rights: cash-flow rights held by the ultimate shareholder (US) after taking into account the whole chain of control (if US owns 50% of direct cash-flows of A and A owns 40% of direct cash-flows of B, then US owns ultimately 50%*40% = 20% of cash-flows of B)

Voting_Rights: voting rights held by the ultimate shareholder in the weakest link along the control chain. 10% is the cutoff point for the existence of a control chain: a company having no shareholder above 10% is considered widely-held

Wedge: difference between Voting and Cash-flow rights

Disclosure

Disclosure index: an index (ranging from 1 to 6) of the quality of RR disclosure. It is the sum of six dummy variables, based on the disclosure of items potentially relevant for investors' decisions: 1) *Disclosure of pay composition (Fixed/Variable)*; 2) *Disclosure of cap on variable compensation*; 3) *Disclosure of performance objectives*; 4) A dummy based on the disclosure of multiple objectives for directors' variable compensation; 5) A dummy based on the disclosure of variable compensation deferral and, finally 6) A dummy based on the disclosure of a cap on directors' severance pay.

Low_Disclosure: a dummy variable taking value 1 if disclosure is low (Disclosure Index<4) and 0 otherwise

Board Characteristics

Board_Size: Number of directors in a Board

Remuneration Committee: a dummy variable taking value 1 if a Remuneration Committee has been established, and 0 otherwise

CEO_Age: age of CEO at the GM date

Voting

Total Shareholder Dissent (%): percentage of ordinary shares voting against (or abstaining on) Section 1 of the Remuneration Report at the 2012 GM

Dissent of institutional shareholders (%): percentage of ordinary shares held by institutional shareholders voting against (or abstaining on) Section 1 of the Remuneration Report at the 2012 GM. Institutional shareholders are defined according to Consob (2014): a) asset managers and pension funds (i.e. passive funds), b) sovereign, hedge and private equity funds (i.e. active funds), c) banks, d) insurance companies.

Dissent of institutional blockholders (%): percentage of ordinary shares held by institutional blockholders (holding more than 2% of the firm's equity capital) voting against (or abstaining on) Section 1 of the Remuneration Report at the 2012 GM.

Dissent of institutional nonblockholders (%): percentage of ordinary shares held by institutional blockholders (holding less than 2% of the firm's equity capital) voting against (or abstaining on) Section 1 of the Remuneration Report at the 2012 GM.

Proxy Advisors' recommendations

ISS_Against: a dummy variable taking value 1 if ISS recommended to vote "Against" Section 1 of the Remuneration Report and 0 otherwise

GL_Against: a dummy variable taking value 1 if GL recommended to vote "Against" Section 1 of the Remuneration Report and 0 otherwise

ISS&GL_Against: a dummy variable taking value 1 if both ISS and GL recommended to vote "Against" Section 1 of the Remuneration Report and 0 otherwise

Only_ISS: a dummy variable taking value 1 if ISS recommended to vote "Against" Section 1 of the Remuneration Report while GL recommended to vote "For" or issued no recommendation, and 0 otherwise

Only_GL: a dummy variable taking value 1 if GL recommended to vote "Against" Section 1 of the Remuneration Report while ISS recommended to vote "For" or issued no recommendation, and 0 otherwise

Number of concerns: number of reasons of concern expressed either by ISS (or, respectively, GL)

Single concern: a dummy variable taking value 1 if ISS (or, respectively, GL) expresses only one reason of concern, and 0 otherwise

Multiple concerns: a dummy variable taking value 1 if ISS (or, respectively, GL) expresses multiple reasons of concern, and 0 otherwise.

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