

How Do Passive Funds Act as Active Owners? Evidence from Mutual Fund Voting Records

Shenje Hshieh ^{*} Jiasun Li [†] Yingcong Tang [‡]

February 1, 2018

WORK IN PROGRESS.
PLEASE DO NOT CITE OR CIRCULATE.

Abstract

The rise of passive institutional investors in the U.S. stock market raises questions about the governance implications of their portfolio firms. While the existing literature documents various governance changes in response to changes in passive ownership, it remains unclear through what mechanism such changes take place. We address this question by comparing the proxy voting records of passive and active funds. We find that compared to their active peers within the same fund family, passive funds often exert corporate governance changes on portfolio firms not via how they vote for a given proxy ballot, but rather by influencing what proxy items get included on the ballot in the first place. Our results support a “behind-the-scene” intervention argument on how passive funds approach corporate governance of their portfolio firms.

Keywords: Corporate governance, mutual funds, proxy voting.

JEL Classification Numbers: G23, G30, G34

^{*}shshieh@cityu.edu.hk. 9-200, 9/F Lau Ming Wai Academic Building, Kowloon Tong, Hong Kong.

[†]jli29@gmu.edu. 4400 University Drive, Fairfax, VA 22030, USA.

[‡]yingcong.tang.1@anderson.ucla.edu. 110 Westwood Plaza, Los Angeles, CA 90095, USA.

In recent years passive institutional investors are becoming increasingly prominent in the U.S. stock market. From 2007 through 2013, domestic index equity mutual funds and exchange-traded funds (ETFs) received \$795 billion in cumulative inflow of net new cash and reinvested dividends. By the end of 2013, index mutual funds and large cap ETFs held \$1.2 trillion and \$450 billion in assets, respectively. Actively managed domestic equity mutual funds, on the other hand, suffered outflows of \$575 billion.¹ This trend has led to significant changes in the institutional ownership composition of U.S. corporations, and raises the question of how the increasing ownership of these firms by passively manage funds can bring about changes in corporate governance.

Several studies have documented the active influence of passive funds on their portfolio firms. Using the annual reassignment of Russell 1000 and 2000 constituents as an instrument for changes in passive mutual fund ownership, Appel, Gormley, and Keim (2016) find that an increase in passive mutual fund ownership causes firms to increase board independence, remove anti-takeover defenses, and adopt equal voting rights for all shareholders. Mullins (2014) shows that an increase in passive ownership leads to higher performance sensitivity of CEO's pay, higher likelihood of CEO turnover within two years, greater resistance to management proposals at shareholder meetings, lower rate of failure of shareholder proposals, lower capital expenditures, as well as fewer cash diversifying acquisitions. Schmidt and Fahlenbrach (2017), on the other hand, find that exogenous increases in passive ownership lead to increases in CEO power and fewer new independent director appointments.² Relatedly, Crane, Michenaud, and Weston (2016) interpret the same index reassignment as an exogenous change in institutional ownership and document more dividend payments resulting from higher institutional ownership. Boone and White (2015) find that higher institutional ownership leads to greater levels of transparency from management.³

¹See Reid et al. (2014).

²They also find more value-destroying mergers and acquisitions (M&A) after passive ownership increases.

³While theses studies focus mainly on the effect of passive investors on corporate governance issues, some recent studies look into how passive investors affect firm operation decisions and product market competition. See He and Huang (2014), Azar, Schmalz, and Tecu (2015), and Azar, Raina, and Schmalz (2016).

Despite all the compelling evidence on *what* changes in corporate governance outcomes passive ownership induces, we are still left with the question of *how* such changes take place. As McCahery, Sautner, and Starks (2016) summarize in a survey of fund managers, institutional investors often engage in various strategies across multiple fronts when they approach the governance issues in their portfolio firms, such as shareholder voting and behind-the-scene intervention. Given their differences in investment objectives as well as available resources, one would expect a difference in the strategies adopted by passive and active mutual funds when approaching the corporate governance of portfolio firms. Understanding such difference would help us better gauge the consequences of the passive revolution in U.S. asset management industry on the governance of U.S. corporations.

This paper is a first step toward answering this question. We first take a granular look into the voting records of all U.S. mutual funds and compare whether and how passive institutional investors vote differently than their active counterparts. For a range of governance measures (including the election of independent directors, elimination of poison pills, strengthening of the right to call special shareholder meetings, establishment of staggered boards, and removal of unequal voting rights, i.e., dual class shares), we find significant differences between passive and active mutual funds *within* the same fund family in how they vote (support or object to the portfolio firm's management).

We then highlight possible behind-the-scenes intervention by passive mutual funds. We find that although higher passive ownership typically leads to better corporate governance outcomes (as documented by the existing literature), proxy voting records often indicate the opposite. The influence of passive ownership is often felt by affecting what agenda items get proposed at each shareholder meeting in the the first place rather than through voting itself. For example, while more passive ownership leads to more independent directors, the likelihood of passive funds casting a vote for an independent director is actually lower than their active counterparts. The actual mechanism at work is that with higher passive ownership, the firm is less likely to nominate non-independent directors in the first place.

In addition to revealing the intricate nuances in how passive investors exert active governance, our approach also addresses several limitations the index reassignment literature faces. First, as the index reassignment literature focuses on firms ranking near the Russell 1000/2000 cutoff, it raises the question of whether its findings can be generalized to firms that rank far above or below the cutoff threshold.⁴ For example, while the implication of passive ownership on governance is likely most important for large-cap firms since they typically feature higher passive ownership, such firms are excluded in the index reassignment literature. Passive mutual fund's strategies for firms with market capitalization around the Russell 1000/2000 cutoff may also not be representative of those for large cap firms. Our approach avoids this problem as we analyze the voting records of all U.S. corporations.

Second, even for firms that are affected by the index reassignment, it is unclear from the existing literature whether the effects of moving firms from Russell 2000 to Russell 1000 necessarily come from the increase in passive mutual fund ownership relative to active mutual fund ownership, or simply relative to other investor type ownership (e.g. retail investors). Indeed, while Appel, Gormley, and Keim (2016) show a discontinuity in passive mutual fund ownership around the Russell 1000/2000 cutoff, no discontinuity emerges for the active mutual fund ownership. This evidence suggests that the documented governance changes following increases in passive ownerships are likely from comparing passive institutional investors and other non-mutual-fund investors. Crane, Michenaud, and Weston (2016), for example, interpret the index changes merely as a change in institutional ownership rather than passive/active ownership. In contrast, we directly compare the voting behaviors between passive and active mutual funds.

Third, the existing literature does not identify the channel or mechanism through which passive ownership leads to governance changes. Do passive funds exert active influence through formal proxy voting at shareholder meetings or do they engage in informal behind-the-scenes interventions as suggested by McCahery, Sautner, and Starks (2016) or both?

⁴ISS only covers firms in the S&P1500.

This distinction is important for interpreting results from aggregate voting outcomes studied by the existing literature; tacit intervention can determine the agenda items that get voted at each shareholder meeting. This intervention is endogenous and requires more careful investigations into both the proxy voting outcomes and agenda compositions, which is provided by our analysis.

Finally, the existing literature sometimes contains contradictory evidences from index reassignment changes. For example, while Appel, Gormley, and Keim (2016) document that an increase in passive ownership leads to greater board independence, Schmidt and Fahlenbrach (2017) instead find that “the fraction of independent board members does not change” and “in firms with more passive investors, independent board turnover decreases so that directors serve longer terms.” Schmidt and Fahlenbrach (2017) further argue that “the incidence of a broad basket of governance-related shareholder proposals does not change following changes in the shareholder base, which is consistent with these shareholder proposals not being initiated by the passive, index-tracking institutional shareholders that form the basis of our study”. Such inconsistencies suggest subtleties in how passive ownership affects corporate governance. We try to reconcile the literature with a more detailed analysis into the underlying mechanism.

By focusing directly on proxy voting rather than on firms’ operating outcomes, our specifications do not suffer from the same identification challenges when looking at firm outcomes as dependent variables.⁵ While index fund creation at the fund family level is admittedly endogenous, once a fund is created its being passive or active will be fixed by the fund prospectus. In another word, funds are unable to endogenously deviate from their strategy of indexation. Hence, beyond the time of fund inception no biases would contaminate our results anymore and causal inferences could be drawn.⁶ Also note that since mutual funds

⁵Appel, Gormley, and Keim (2016) states that identifying the impact of passive investors on firms’ corporate governance and performance can be challenging. Correlations between passive investors and governance choices might not reflect a causal relation since ownership by passive investors might be correlated with factors such as firms’ investment opportunities or ownership by active investors that directly affect managerial decisions”.

⁶We include fund age in our specification to control for potential effects arising from fund inception.

are required to file N-PX forms on matters in which they are “entitled to vote”, there is no concerns over omitting non-votes or uninstructed shares from mutual funds.⁷ Our methodology also allows us to pin down the mechanism through which passive funds affect corporate governance. Overall, our findings are consistent with McCahery, Sautner, and Starks (2016), who survey institutional investors and document widespread behind-the-scenes intervention as well as governance-motivated exits. In addition, we further demonstrate how passive and active funds differ in their adoptions of these various corporate governance strategies.

Related Literature

Passive Institutional Investors and Corporate Governance Our findings are most closely related to the literature on the effect of passive ownership on corporate governance. It has been argued that because indexation prevents passive funds from divesting poor performing stocks in their portfolios, some recent papers have argued that the lack of an exit option disciplines passive funds to improve the returns of their firm holdings through the “voice” channel. The fact that passive funds holds an inflexible portfolio allows them to be more aggressive in pursuing governance intervention without fear of management retaliation (e.g. in information communication). On the other hand, the low fees charged by passive mutual funds may restrict the resources available for active governance intervention.⁸ Unsurprisingly, empirical findings are mixed (see Appel, Gormley, and Keim (2016), Mullins (2014), Crane, Michenaud, and Weston (2016), Boone and White (2015), and Schmidt and Fahlenbrach (2017)). Such intricacies in the existing literature inspire us to take a more microscopic approach and analyze the exact mechanism through which passive institutional investors can generate corporate governance changes.

⁷See <https://www.sec.gov/reportspubs/investor-publications/investorpubsmfproxyvotinghtm.html>

⁸The last argument, however, may no longer apply for some large passive fund providers such as Vanguard or BlackRock – despite their low profit margin, absolute revenue could still be high due to their sheer sizes.

Influencers of Mutual Fund Proxy Voting The literature in mutual fund proxy voting finds that mutual fund votes can be subject to manipulation. Bach and Metzger (2016) show that management holds extraordinary power over the voting process to block improvements to corporate governance supported by a large and discontinuous drop in the density of voting results at the 50% threshold. Ashraf, Jayaraman, and Ryan (2012), Davis and Kim (2007), and Ng, Wang, and Zaiats (2009) show that fund votes can be influenced by existing business ties. Specifically, Ashraf, Jayaraman, and Ryan (2012) find that fund families often support management when they have pension ties to firms in which they are also stakeholders. Similarly, Davis and Kim (2007) and Ng, Wang, and Zaiats (2009) uncover a positive relationship between business ties and the propensity to vote with management. Others such as Iliev and Lowry (2015) and Matvos and Ostrovsky (2013) suggest that mutual fund votes can be determined by recommendations of proxy advisory firms (e.g., ISS) or by other mutual funds (e.g., herding or peer effects), respectively.

Interactions within Mutual Fund Families This paper lastly relates to the literature of interactions within fund families. Several papers provide evidence of coordination failure among funds in a fund family. Kempf and Ruenzi (2008), for example, show that fund managers compete with other fund managers of their own company for the best rank in the fund family. Likewise, Gaspar, Massa, and Matos (2006) find that fund management companies have incentives to cross-subsidize the performance of “high value funds” (i.e., high fees or high past performers) at the expense of low value funds. This result is also supported by Nanda, Wang, and Zheng (2004), who show that exceptional fund performance leads to greater cash inflow to other funds in its family. All evidence suggests that mutual fund families do not act as coordinated entities, consistent with our findings on proxy voting.

The rest of the paper is organized as follows. Section 1 documents the construction details of our dataset. Section 2 gives an overview on the differences in voting patterns between passive and active mutual funds. Section 3 reports our main findings. Section 4 concludes.

1 Data

Our data comes from merging four databases: (1) SEC N-PX form filings maintained by Institutional Shareholder Services (ISS), (2) Thomson Reuters CDA/Spectrum S12 mutual fund holdings, (3) CRSP Mutual Funds and CRSP-Compustat Merged, and (4) ISS directors data. The N-PX database includes mutual fund votes cast for each agenda item appearing on firm proxy statements at shareholder meetings from 2004 to 2015. The S12 database provides information on the portfolio of mutual funds collected from fund prospectuses and quarterly holding reports including SEC forms N-30D, N-30B-2, N-CSR, N-CSRS, and N-Q filings. While the S12 holdings data includes mutual funds listed on all major U.S. stock exchanges (i.e., NYSE, AMEX, and NASDAQ), CRSP Mutual Fund data only includes mutual funds listed on NASDAQ. This is a caveat to keep in mind since we merge CRSP Mutual Fund data with S12 through the Wharton Financial Institution Center Number (WFICN), which provides links between 98% of the domestic domestic equity funds in CRSP Mutual Fund and Thomson Reuters S12.

The ISS N-PX database is merged with CRSP Mutual Fund data in two stages. In the first stage, we associate each mutual fund’s identification number created by ISS to their tickers (if it has one). This is done by parsing each raw N-PX filing from SEC to get a list of tickers and fund names associated to each N-PX filing through a unique SEC filing number. We map the mutual funds in ISS N-PX database to the tickers and names extracted from SEC N-PX filings by first matching on the SEC filing numbers and then fuzzy string matching on mutual fund names.⁹ In the second stage, we link ISS N-PX database with CRSP Mutual Fund data by year and ticker.

To merge ISS N-PX database with ISS directors data, we first use a natural language processing software to tag and extract human names from agenda item descriptions related to director elections in N-PX.¹⁰ We then link these two databases by matching on firm

⁹We thank Peter Iliev for suggesting this procedure.

¹⁰See <https://stanfordnlp.github.io/CoreNLP/>.

CUSIP and year and fuzzy string matching on director name.

We identify passive mutual funds using the same method in Appel, Gormley, and Keim (2016). We categorize funds as passive funds if their names contain at least one of the following strings: Index, Idx, Indx, Ind_ (where _ indicates a space), Russell, S & P, S and P, S&P, SandP, SP, DOW, Dow, DJ, MSCI, Bloomberg, KBW, NASDAQ, NYSE, STOXX, FTSE, Wilshire, Morningstar, 100, 400, 500, 600, 900, 1000, 1500, 2000, and 5000. In addition, we augment our classification method by incorporating the passive mutual fund identifying variable provided in CRSP.

2 Do Passive and Active Funds Vote Differently?

In this section, we first estimate panel regressions to assess voting behavior differences between passive and active mutual funds within the same fund families. The left-hand side variables are dummies for whether a fund votes for several agenda items studied in the literature: retaining a shareholder rights plan (poison pill), rights to call special shareholder meeting, removal of classified boards, removal of a stock class (Table 5), and director elections (Table 11), respectively. Our main variable of interest on the right hand side is a dummy indicating whether a fund is passive or active. We control for ownership share, Management and ISS recommendations as well as their interactions, the fund's turnover and expense ratios, fund age, fund flow relative to total net assets, and fund size. We include fund family and firm fixed effects interacted with year as well as CRSP fund style fixed effects. Standard errors are clustered at the firm and fund levels.

Our findings show that passive mutual funds are becoming more active in proxy voting in recent years. Using a sample from 2006 to 2010, Iliev and Lowry (2015) explore the influence of ISS on the voting behavior of active funds through probit models. For compensation and governance related proposals, they find a 99 percent probability of passive funds voting with management when ISS recommends so and a 5 percent probability of voting with manage-

ment when ISS recommends otherwise. On the other hand, the probability of most active funds voting with management is essentially unrelated to ISS recommendations. Morgan et al. (2011) document that this divergence in voting behavior persists even within fund family and across board, compensation, governance, environmental and social issues related proposals. They find that funds within the same family vote in the same way only 90% of the time (with a standard deviation of 16.1%). By including more recent data, we find the incidences of “active” voting increase significantly for passive mutual funds.

Table 5 and 11 renders some interesting facts. By looking at voting records alone, we find that increased passive ownership does not necessarily appear to lead to better governance (at least on the surface). For example, while the literature has established that higher passive ownership leads to proportionately more independent directors on the board, from voting records the sensitivity of ownership concentration with respect to voting for an independent director is significantly smaller for passive funds compared to active funds. This evidence suggests possible behind-the-scenes interventions from passive funds, e.g. passive funds influence which items get to be voted on before the shareholder voting takes place. We test this hypothesis in Section 3, along with detailed discussions of the voting results from Table 5 and 11.

3 Explicit voting vs. behind the scenes intervention

In this section, we conduct detailed analysis into several agenda items extensively studied in the existing literature, and reveal nuanced intricacies about how governance changes actually take place when a firm becomes more highly owned by passive institutional investors.

3.1 Approving, Amending, or Renewing the Poison Pill

While the existing literature (Appel, Gormley, and Keim (2016)) argue convincingly that an increase in passive ownership leads to “removals” of poison pills, what actual happens

during shareholder meetings is much more complex. Proxy statements rarely contain proposals that explicitly removes a shareholder rights plan (i.e., poison pill). Indeed, out of our sample of about 65 million agenda items, only 356 that are exclusively sponsored by shareholders specifically ask for the elimination or restriction of a poison pill.

A more common observation is that firms allow their poison pills to automatically expire.¹¹ Most companies follow the advice (e.g., general guidelines set by ISS) of not adopting or renewing a poison pill unless a raider or activist attempts a takeover. In our sample, there are about 60,208 cases of approving, amending, or renewing poison pills.

Table 5 shows that passive mutual funds are actually more likely to vote in favor of agenda items that call for the approval, amendment, or renewal of a shareholder rights plan, regardless of whether ISS agrees or disagrees with management. On average, passive mutual funds are 4.8 percentage points more likely than active mutual funds to vote to retain a poison pill after controlling for fund portfolio characteristics. This point estimate is statistically significant at the 1 level.

[Insert Table 7]

To see whether passive mutual funds can also influence the appearance of agenda items that approve/amend/renew a poison pill on firm proxy statements, Table 7 documents results from regressing an indicator variable for whether such agenda items are up for vote at firm annual shareholder meetings on aggregate measures of firm ownership by passive mutual funds. We find that an increase of 100 percentage points in passive ownership relative to all mutual funds leads to a significant .1 percentage points decrease in probability of observing an agenda item that retains a poison bill. The presence of passive funds seems to deter management from putting poison pill renewal into vote.

¹¹See https://www.sharkrepellent.net/pub/rs_20070920.html.

3.2 The Right to Call Special Meetings

Table 5 shows that passive mutual funds have a strong preference for the right to call special meetings at the voting stage. On average, passive mutual funds are 8.9 percentage points more likely than active mutual funds to vote for the right to call special meetings after controlling for fund characteristics. For the rights to call special meetings, passive funds appear to be more active in the voting stage.

[Insert Table 8]

Table 8 examines the relationship between passive mutual fund ownership and the probability of seeing agenda items that propose to call special meetings. When the passive mutual fund ownership share of total shares outstanding increases 100 percentage points, the likelihood of observing such an agenda item on the proxy statement decreases by around 10 percentage points.

3.3 Declassifying Boards

Staggered boards can delay not only the turnover of directors but also prevent the removal of directors in the event of hostile takeovers. Table 5 reveals there is basically no disagreement between active and passive funds within fund family on whether or not to classify boards, regardless of ISS recommendations.

On the other hand, we find some evidence that more passive mutual fund ownership leads to a higher likelihood of voting on proposals to declassify boards. As documented in Table 9, all else equal, increasing passive ownership share of total shares outstanding by 100 percentage points leads to an increase in probability of encountering a proposal to declassify boards by roughly 10 percentage points (significant at the 5 percent level). This result implies that passive mutual funds can also influence corporate governance through changing the composition of the proposals voted on at each shareholder meeting.

[Insert Table 9]

3.4 Eliminating Multi-Class Share Structure

Table 5 shows that passive mutual funds essentially vote the same way as active mutual funds within the same fund family on proposals related to eliminating multi-class shares. Any effects passive funds have compared to active peers on eliminating multi-class shares must be due to other channels. We hence investigate whether passive mutual funds are able to add proposals that eliminate multi-class share structure on proxy statements. As shown by Table 10, passive mutual fund ownership does not affect the probability that a proposal to eliminate multi-share class structure will be voted on by shareholders.

[Insert Table 10]

3.5 Director Elections

By matching ISS N-PX filings data with ISS director data, we are able to identify the votes made by mutual funds for each director candidate. In Table 11, we regress the vote cast by mutual funds for each nominated director (i.e., dependent variable is equal to 1 if the vote is cast in support of a candidate) on a passive mutual fund dummy variable and the interaction of the passive mutual fund dummy and the passive mutual fund ownership percentage of total shares outstanding. We also include fund and director characteristics as controls. We split the director elections data into two separate subsamples: proposals to elect independent and non-independent directors. This is done to account for the fact that these two groups of directors are different from each other in many dimensions.

After controlling for ISS and management recommendations, we do not find significant differences in the voting patterns between active and passive mutual funds in both independent and non-independent director elections. However, the negative coefficient on the interaction term suggests that larger holdings by passive mutual funds leads to an increased likelihood of rejecting independent directors, as documented in column 2 of Table 11. This counter-intuitive result can be made sense if passive mutual funds can influence the slate of

nominated directors to be voted on by shareholders.

[Insert Table 12]

Table 12 shows the results of regressing the slate percentage of independent directors on passive mutual fund ownership along with controls. We find that higher passive mutual fund ownership measured as the fraction of total share outstanding leads to a higher percentage of independent directors nominated. Increasing passive mutual fund ownership by 100 percentage points increases the proportion of nominated independent directors by 2.4 percentage points. This is consistent with the evidence on declassifying boards as mentioned above: passive mutual funds can exert their influence on board issues through changing the composition of director candidates to be voted on by shareholders.

3.6 Summary

Our analysis so far shows that both “on-the-stage” voting and “behind-the-scene” intervention play important roles in how passive funds exert active corporate governance. For different agenda items, however, passive and active funds seem to have different preferences for these two methods. Table 1 summarizes such preference differences.

Table 1: **Who is more pro-governance on the stage or behind the scene?
Passive versus Active Funds**

	on the stage	behind the scene
approval, amending, or renewing the poison pill	Passive	Active
right to call special meetings	Passive	Active/Institutional
declassifying boards	No Difference	Passive
eliminating multi-class structure	No Difference/Passive	No Difference
independent director elections	Active	Passive

It looks that when an agenda item involves the interest of shareholders in general (declassifying boards, independent directors), passive funds are more likely to stay behind the scene. For items involving different classes of shareholders (approval poison pill, rights to

special meeting, and eliminating multi-class), passive are more pro-governance at on the stage voting.

4 Conclusion

In this paper we first compare the voting behavior between passive and active mutual funds in the U.S. While previous studies document more independent boards and removal of takeover defenses following increases in passive ownership, we find no evidence that passive mutual funds vote in favor of independent directors or declassifying staggered boards. However, we find strong evidence that more passive ownership significantly increases the likelihood of such proposals being accepted and voted on at shareholder meetings. These findings lead to the support for the argument that passive mutual funds use a mixture of strategies, especially those behind-the-scene to influence corporate governance.

Our approach bypasses several limitations that the existing literature faces, and provides a more in-depth analysis on the nuances of how passive mutual funds affect corporate governance differently than their active peers.

In ongoing research we are attempting to understand why passive funds behave differently from their active peers? Why for board-related issues passive funds prefer behind-the-scene interventions while their active peers prefer voting? Does our finding relate to the coordination and competitions between active and passive mutual funds within the same fund family? We look forward to address these issues in upcoming revisions.

References

- Appel, Ian R, Todd A Gormley, and Donald B Keim. 2016. “Passive investors, not passive owners”. *Journal of Financial Economics* 121 (1): 111–141.
- Ashraf, Rasha, Narayanan Jayaraman, and Harley E. Ryan. 2012. “Do pension-related business ties influence mutual fund proxy voting? Evidence from shareholder proposals on executive compensation”. *Journal of Financial and Quantitative Analysis* 47 (3): 567–588.
- Azar, José, Sahil Raina, and Martin C Schmalz. 2016. “Ultimate Ownership and Bank Competition”. *Available at SSRN 2710252*.
- Azar, José, Martin C Schmalz, and Isabel Tecu. 2015. “Anti-competitive effects of common ownership”. *Ross School of Business Paper*, no. 1235.
- Bach, Laurent, and Daniel Metzger. 2016. “Are Shareholder Votes Rigged?”
- Boone, Audra L., and Joshua T. White. 2015. “The effect of institutional ownership on firm transparency and information production”. *Journal of Financial Economics* 117 (3): 508–533.
- Crane, Alan D, Sébastien Michenaud, and James P Weston. 2016. “The effect of institutional ownership on payout policy: Evidence from index thresholds”. *Review of Financial Studies*: hhw012.
- Davis, Gerald F., and E. Han Kim. 2007. “Business ties and proxy voting by mutual funds”. *Journal of Financial Economics* 85 (2): 552–570.
- Gaspar, José-Miguel, Massimo Massa, and Pedro Matos. 2006. “Favoritism in Mutual Fund Families? Evidence on Strategic Cross-Fund Subsidization”. *The Journal of Finance* 61 (1): 73–104.
- He, Jie, and Jiekun Huang. 2014. “Product market competition in a world of cross ownership: evidence from institutional blockholdings”. *Available at SSRN 2380426*.

- Iliev, Peter, and Michelle Lowry. 2015. "Are Mutual Funds Active Voters?" *Review of Financial Studies* 28 (2): 446–485.
- Kempf, Alexander, and Stefan Ruenzi. 2008. "Tournaments in mutual-fund families". *Review of Financial Studies* 21 (2): 1013–1036.
- Matvos, Gregor, and Michael Ostrovsky. 2013. "Heterogeneity and peer effects in mutual fund proxy voting". *Journal of Financial Economics* 98 (1): 90–112.
- McCahery, Joseph A., Zacharias Sautner, and Laura T. Starks. 2016. "Heterogeneity and peer effects in mutual fund proxy voting". *The Journal of Finance* 71 (6): 2905–2932.
- Morgan, Angela, et al. 2011. "Mutual funds as monitors: Evidence from mutual fund voting". *Journal of Corporate Finance* 17 (4): 914–928.
- Mullins, W. 2014. "The governance impact of indexing: evidence from regression discontinuity". *Work. Pap., Smith Sch. Bus., Univ. Md.*
- Nanda, Vikram, Z. Jay Wang, and Lu Zheng. 2004. "Family Values and the Star Phenomenon: Strategies of Mutual Fund Families". *The Review of Financial Studies* 17 (3): 667–698.
- Ng, Lilian, Qinghai Wang, and Nataliya Zaiats. 2009. "Firm performance and mutual fund voting". *Journal of Banking and Finance* 33 (12): 2207–2217.
- Reid, Brian, et al. 2014. *2014 Investment Company Fact Book*. Tech. rep. Investment Company Institute. https://www.ici.org/pdf/2014_factbook.pdf.
- Schmidt, Cornelius, and Rudiger Fahlenbrach. 2017. "Do exogenous changes in passive institutional ownership affect corporate governance and firm value?" *Journal of Financial Economics* 22 (1): 1–22.

Table 2: Descriptive Statistics

	Shareholder Rights	Compensation	Board Issues	Social Issues
Mgmt. recommends voting FOR	78.05	91.33	97.29	9.91
ISS recommends voting FOR	85.98	86.67	92.63	45.63
ISS recommends voting with mgmt.	72.85	81.31	91.12	54.86
Fund votes with mgmt.	73.07	83.00	91.03	83.32
Fund votes with ISS	87.59	86.25	92.91	68.94
Shareholder proposal	23.18	7.52	2.51	90.34
Observations	1,028,389	8,920,525	53,662,112	1,329,096

The table describes the voting patterns of funds and the recommendations of management and ISS in percentage terms across the four different types of proposals: shareholder rights, compensation, board issues, and social issues. The full sample across all four agenda categories consists of 64,940,122 votes by 18,493 mutual funds, across 656 different fund families in the 2003–2015 period.

Table 3: Descriptive Statistics of Fund Proxy Votes in Fund Families **without** Passive (Index) Funds

	N	Mean	St. Dev.	25%-ile	50%-ile	75%-ile
Fund Votes FOR	5,734,729	0.872	0.334	1.000	1.000	1.000
% of TNA	1,769,315	0.012	0.013	0.003	0.008	0.016
% of Shares Outstanding	2,046,785	0.002	0.008	0.000	0.000	0.001
Turnover Ratio	3,369,847	0.517	5.522	0.310	0.580	1.000
Expense Ratio	3,369,847	0.012	0.217	0.011	0.013	0.016
Net Flow	3,412,008	-0.068	0.232	-0.183	-0.066	0.030
Fund Age	3,413,929	13.177	10.498	5	11	18
log(TNA)	3,384,104	5.544	1.968	4.113	5.421	6.964

This table shows statistics of votes cast by funds that are in a fund family without any passive mutual funds. Around 37 percent of our sample mutual funds are categorized as passive funds. On average, passive mutual funds make up 12 percent of the fund family (standard deviation of 0.26).

Table 4: Descriptive Statistics of Fund Proxy Votes in Fund Families **with** Passive (Index) Funds

	N	Mean	St. Dev.	25%-ile	50%-ile	75%-ile
Fund Votes FOR	58,590,504	0.879	0.326	1.000	1.000	1.000
% of TNA	16,569,128	0.006	0.011	0.000	0.002	0.007
% of Shares Outstanding	19,569,794	0.002	0.006	0.000	0.000	0.001
Turnover Ratio	31,020,875	-0.004	8.333	0.120	0.350	0.800
Expense Ratio	31,020,875	0.009	1.277	0.003	0.007	0.013
Net Flow	31,989,820	-0.085	0.269	-0.187	-0.095	0.016
Fund Age	32,021,672	12.007	9.753	5	10	16
log(TNA)	31,706,330	6.333	2.109	4.945	6.329	7.690

This table shows statistics of votes cast by funds that are in a fund family with at least one passive mutual fund. Around 37 percent of our sample mutual funds are categorized as passive funds. On average, passive mutual funds make up 12 percent of the fund family (standard deviation of 0.26).

Table 5: Passive Funds Vote Differently on Specific Governance Issues within Fund Family

	<i>Dependent variable:</i>			
	Voting FOR a Governance Policy = 1			
	FOR Poison Pill	FOR Special Meeting	FOR Classified Boards	FOR Removing a Stock Class
Passive	0.048*** (0.012)	0.089*** (0.024)	-0.003 (0.002)	0.005 (0.012)
% of TNA	-0.246 (0.877)	-0.505** (0.218)	0.487*** (0.146)	-1.491 (1.752)
% of Shares Outstanding	-2.292** (0.944)	1.317 (0.936)	-0.002 (0.205)	-0.545 (1.458)
Mgmt Votes FOR	0.346* (0.193)	0.017 (0.017)	-0.167 (0.135)	0.000 (0.000)
ISS Votes FOR	0.365** (0.151)	-0.212*** (0.044)	-0.520*** (0.050)	0.361*** (0.026)
Turnover Ratio	-0.001 (0.0004)	0.00004 (0.0002)	0.00003 (0.0001)	-0.0001 (0.0005)
Expense Ratio	-0.162 (1.048)	-0.002 (0.002)	0.0004 (0.0004)	-2.211 (2.260)
Net Flow	-0.029 (0.042)	0.030 (0.032)	-0.012 (0.011)	-0.052 (0.055)
Fund Age	0.0003 (0.0004)	-0.001* (0.0004)	-0.00005 (0.0001)	-0.0004 (0.0004)
log(TNA)	-0.001 (0.003)	-0.006* (0.003)	0.002*** (0.001)	-0.001 (0.004)
Passive × % Shares Outstanding	-1.127 (1.926)	2.731 (2.228)	-0.466 (0.362)	0.479 (2.789)
Mgmt Votes FOR × ISS Votes FOR	-0.379 (0.243)	0.457*** (0.052)	0.104 (0.141)	Absorbed
CRSP Fund Style FE	Yes	Yes	Yes	Yes
Fund Family × Year FE	Yes	Yes	Yes	Yes
Firm × Year FE	Yes	Yes	Yes	Yes
Observations	13,159	69,962	96,551	6,242
Adjusted R ²	0.514	0.596	0.415	0.704

Significance levels 10%, 5%, and 1% are denoted by *, **, ***, respectively. Standard errors in parentheses are clustered at the firm and fund levels. Mutual funds are categorized as passive funds if their names contain at least one of the following strings: Index, Idx, Indx, Ind_ (where _ indicates a space), Russell, S & P, S and P, S&P, SandP, SP, DOW, Dow, DJ, MSCI, Bloomberg, KBW, NASDAQ, NYSE, STOXX, FTSE, Wilshire, Morningstar, 100, 400, 500, 600, 900, 1000, 1500, 2000, and 5000. We also use the classification variable provided by CRSP to identify passive mutual funds. Retaining a shareholder rights plan includes adopting, amending, or renewing a poison pill. TNA is total net assets under fund management.

Table 6: Passive Funds Vote Differently on Specific Governance Issues within Fund Family
(Contested Agenda Items Only)

	<i>Dependent variable:</i>			
	Voting FOR a Governance Policy = 1			
	FOR Poison Pill	FOR Special Meeting	FOR Classified Boards	FOR Removing a Stock Class
Passive	0.069** (0.027)	0.043*** (0.014)	-0.007** (0.004)	0.082* (0.042)
% of TNA	0.297 (1.624)	2.162 (1.909)	0.512* (0.296)	2.661 (4.547)
% of Shares Outstanding	-11.265*** (3.746)	2.696*** (0.737)	-0.180 (0.433)	6.404 (6.191)
Mgmt Votes FOR	Absorbed	Absorbed	Absorbed	Absorbed
ISS Votes FOR	Absorbed	Absorbed	-1.000*** (0.000)	Absorbed
Turnover Ratio	-0.001 (0.001)	-0.000 (0.000)	0.000 (0.000)	0.015 (0.027)
Expense Ratio	-2.340 (2.687)	3.760*** (1.404)	0.003*** (0.001)	-5.964 (18.012)
Net Flow	-0.038 (0.090)	0.037 (0.041)	-0.020 (0.018)	-0.069 (0.303)
Fund Age	0.001 (0.001)	0.000 (0.001)	-0.000 (0.000)	-0.003 (0.003)
log(TNA)	0.008 (0.008)	-0.008** (0.004)	0.002 (0.001)	-0.016 (0.017)
Passive \times % Shares Outstanding	9.596** (4.891)	-1.344 (3.792)	Absorbed	-5.940 (5.025)
Mgmt Votes FOR \times ISS Votes FOR	Absorbed	Absorbed	0.618*** (0.238)	Absorbed
CRSP Fund Style FE	Yes	Yes	Yes	Yes
Fund Family \times Year FE	Yes	Yes	Yes	Yes
Firm \times Year FE	Yes	Yes	Yes	Yes
Observations	2,364	5,558	19,628	573
Adjusted R ²	0.544	0.719	0.483	0.626

Significance levels 10%, 5%, and 1% are denoted by *, **, ***, respectively. Standard errors in parentheses are clustered at the firm and fund levels. Mutual funds are categorized as passive funds if their names contain at least one of the following strings: Index, Idx, Indx, Ind_ (where _ indicates a space), Russell, S & P, S and P, S&P, SandP, SP, DOW, Dow, DJ, MSCI, Bloomberg, KBW, NASDAQ, NYSE, STOXX, FTSE, Wilshire, Morningstar, 100, 400, 500, 600, 900, 1000, 1500, 2000, and 5000. We also use the classification variable provided by CRSP to identify passive mutual funds. Retaining a shareholder rights plan includes adopting, amending, or renewing a poison pill. TNA is total net assets under fund management. Contested agenda items are those that received (lacked) at most 5 percent above (below) the vote passing threshold.

Table 7: Impact of Passive Ownership on the Probability of Voting on a Proposal to Retain a Shareholder Rights Plan

	<i>Dependent variable:</i>			
	Poison Pill Proposal Appearing on Proxy Statement = 1			
	(1)	(2)	(3)	(4)
Passive Ownership % of Mutual Funds	-0.001*** (0.0004)			-0.001*** (0.0004)
Passive Ownership % of Total Shares Out.		0.004 (0.026)		0.021 (0.027)
Passive % of Mutual Funds			0.005 (0.004)	0.006 (0.004)
% Mgmt Votes FOR	-0.132*** (0.024)	-0.132*** (0.024)	-0.132*** (0.024)	-0.132*** (0.024)
% ISS Votes FOR	0.043** (0.022)	0.043* (0.022)	0.043* (0.022)	0.043* (0.022)
% Mgmt & ISS Agree	-0.050** (0.022)	-0.050** (0.022)	-0.050** (0.022)	-0.050** (0.022)
log(Market Cap.)	-0.001 (0.001)	-0.001 (0.001)	-0.001 (0.001)	-0.0004 (0.001)
Number of Agenda Items	0.001*** (0.0003)	0.001*** (0.0003)	0.001*** (0.0003)	0.001*** (0.0003)
Firm FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes
Observations	35,919	35,919	35,919	35,919
Adjusted R ²	0.051	0.051	0.051	0.051

Significance levels 10%, 5%, and 1% are denoted by *, **, ***, respectively. Standard errors in parentheses are clustered at the firm level. Mutual funds are categorized as passive funds if their names contain at least one of the following strings: Index, Idx, Indx, Ind_ (where _ indicates a space), Russell, S & P, S and P, S&P, SandP, SP, DOW, Dow, DJ, MSCI, Bloomberg, KBW, NASDAQ, NYSE, STOXX, FTSE, Wilshire, Morningstar, 100, 400, 500, 600, 900, 1000, 1500, 2000, and 5000. We also use the classification variable provided by CRSP to identify passive mutual funds. Retaining a shareholder rights plan includes adopting, amending, or renewing a poison pill. Average management and ISS disagreement variable, which ranges between 0 and 1, is defined as the average absolute difference between how management and ISS votes.

Table 8: Impact of Passive Ownership on the Probability of Voting on a Special Meeting Proposal

	<i>Dependent variable:</i>			
	Special Meeting Proposal Appearing on Proxy Statement = 1			
	(1)	(2)	(3)	(4)
Passive Ownership % of Mutual Funds	0.0001 (0.001)			0.001 (0.001)
Passive Ownership % of Total Shares Out.		-0.086*** (0.023)		-0.103*** (0.025)
Passive % of Mutual Funds			0.007* (0.004)	0.008** (0.004)
% Mgmt Votes FOR	-0.087*** (0.027)	-0.087*** (0.027)	-0.087*** (0.027)	-0.086*** (0.027)
% ISS Votes FOR	0.134*** (0.032)	0.135*** (0.032)	0.134*** (0.032)	0.135*** (0.032)
% Mgmt & ISS Agree	-0.135*** (0.032)	-0.135*** (0.032)	-0.135*** (0.032)	-0.135*** (0.032)
log(Market Cap.)	0.00005 (0.001)	0.001 (0.001)	0.0004 (0.001)	0.001 (0.001)
Number of Agenda Items	0.003*** (0.0005)	0.003*** (0.0005)	0.003*** (0.0005)	0.003*** (0.0005)
Firm FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes
Observations	35,919	35,919	35,919	35,919
Adjusted R ²	0.153	0.153	0.153	0.153

Significance levels 10%, 5%, and 1% are denoted by *, **, ***, respectively. Standard errors in parentheses are clustered at the firm level. Mutual funds are categorized as passive funds if their names contain at least one of the following strings: Index, Idx, Indx, Ind_ (where _ indicates a space), Russell, S & P, S and P, S&P, SandP, SP, DOW, Dow, DJ, MSCI, Bloomberg, KBW, NASDAQ, NYSE, STOXX, FTSE, Wilshire, Morningstar, 100, 400, 500, 600, 900, 1000, 1500, 2000, and 5000. We also use the classification variable provided by CRSP to identify passive mutual funds. Average management and ISS disagreement variable, which ranges between 0 and 1, is defined as the average absolute difference between how management and ISS votes.

Table 9: Impact of Passive Ownership on the Probability of Voting on an a Proposal to Declassify Boards

	<i>Dependent variable:</i>			
	Declassify Boards Proposal Appearing on Proxy Statement = 1			
	(1)	(2)	(3)	(4)
Passive Ownership % of Mutual Funds	-0.0001 (0.001)			-0.001 (0.001)
Passive Ownership % of Total Shares Out.		0.089* (0.054)		0.105* (0.058)
Passive % of Mutual Funds			-0.003 (0.008)	-0.005 (0.008)
% Mgmt Votes FOR	-0.837*** (0.053)	-0.837*** (0.053)	-0.837*** (0.053)	-0.837*** (0.053)
% ISS Votes FOR	0.684*** (0.058)	0.683*** (0.058)	0.684*** (0.058)	0.683*** (0.058)
% Mgmt & ISS Agree	-0.688*** (0.058)	-0.687*** (0.058)	-0.688*** (0.058)	-0.687*** (0.058)
log(Market Cap.)	-0.0003 (0.002)	-0.001 (0.002)	-0.0005 (0.002)	-0.001 (0.002)
Number of Agenda Items	-0.002*** (0.001)	-0.002*** (0.001)	-0.002*** (0.001)	-0.002*** (0.001)
Firm FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes
Observations	35,919	35,919	35,919	35,919
Adjusted R ²	0.057	0.057	0.057	0.057

Significance levels 10%, 5%, and 1% are denoted by *, **, ***, respectively. Standard errors in parentheses are clustered at the firm level. Mutual funds are categorized as passive funds if their names contain at least one of the following strings: Index, Idx, Indx, Ind_ (where _ indicates a space), Russell, S & P, S and P, S&P, SandP, SP, DOW, Dow, DJ, MSCI, Bloomberg, KBW, NASDAQ, NYSE, STOXX, FTSE, Wilshire, Morningstar, 100, 400, 500, 600, 900, 1000, 1500, 2000, and 5000. We also use the classification variable provided by CRSP to identify passive mutual funds. Average management and ISS disagreement variable, which ranges between 0 and 1, is defined as the average absolute difference between how management and ISS votes.

Table 10: Impact of Passive Ownership on the Probability of Voting to Eliminate a Class of Stock

	<i>Dependent variable:</i>			
	Equal Vote Proposal Appearing on Proxy Statement = 1			
	(1)	(2)	(3)	(4)
Passive Ownership % of Mutual Funds	0.0001 (0.0002)			0.0001 (0.0002)
Passive Ownership % of Total Shares Out.		0.007 (0.011)		0.008 (0.012)
Passive % of Mutual Funds			-0.003* (0.002)	-0.003* (0.002)
% Mgmt Votes FOR	0.001 (0.004)	0.001 (0.004)	0.001 (0.004)	0.001 (0.004)
% ISS Votes FOR	0.004 (0.004)	0.004 (0.004)	0.004 (0.004)	0.004 (0.004)
% Mgmt & ISS Agree	-0.005 (0.004)	-0.005 (0.004)	-0.005 (0.004)	-0.005 (0.004)
log(Market Cap.)	-0.00004 (0.0003)	-0.0001 (0.0003)	-0.0002 (0.0003)	-0.0002 (0.0003)
Number of Agenda Items	0.0002** (0.0001)	0.0002** (0.0001)	0.0002** (0.0001)	0.0002** (0.0001)
Firm FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes
Observations	35,919	35,919	35,919	35,919
Adjusted R ²	0.045	0.045	0.045	0.045

Significance levels 10%, 5%, and 1% are denoted by *, **, ***, respectively. Standard errors in parentheses are clustered at the firm level. Mutual funds are categorized as passive funds if their names contain at least one of the following strings: Index, Idx, Indx, Ind_ (where _ indicates a space), Russell, S & P, S and P, S&P, SandP, SP, DOW, Dow, DJ, MSCI, Bloomberg, KBW, NASDAQ, NYSE, STOXX, FTSE, Wilshire, Morningstar, 100, 400, 500, 600, 900, 1000, 1500, 2000, and 5000. We also use the classification variable provided by CRSP to identify passive mutual funds. Average management and ISS disagreement variable, which ranges between 0 and 1, is defined as the average absolute difference between how management and ISS votes.

Table 11: Passive Funds Vote Differently on Director Elections within Fund Family

	<i>Dependent variable:</i>			
	Fund Votes for a Director = 1			
	Independent		Non-Independent	
	Full Sample	Contested	Full Sample	Contested
	(1)	(2)	(3)	(4)
Passive	0.004 (0.003)	-0.004 (0.008)	0.004 (0.005)	-0.019 (0.015)
Female	0.001** (0.001)	-0.002 (0.004)	-0.005 (0.005)	-0.073** (0.031)
Director Age	-0.0001 (0.0001)	0.00004 (0.0002)	-0.0003*** (0.0001)	-0.001 (0.001)
CEO	0.0001 (0.002)	-0.003 (0.008)	0.015*** (0.002)	0.018** (0.009)
Director % Ownership	-0.107*** (0.032)	-0.020 (0.045)	0.036*** (0.011)	-0.003 (0.055)
% of TNA	0.051* (0.029)	0.043 (0.066)	0.032 (0.048)	0.201 (0.140)
% of Shares Outstanding	0.310*** (0.076)	0.888 (0.577)	0.569*** (0.110)	1.616** (0.737)
Mgmt Votes FOR	0.071 (0.106)	Absorbed	0.214* (0.126)	Absorbed
ISS Votes FOR	0.096 (0.106)	0.269*** (0.098)	0.154 (0.135)	Absorbed
Turnover Ratio	0.0002 (0.0002)	0.0005 (0.0004)	0.0005 (0.0004)	0.001 (0.001)
Expense Ratio	0.001 (0.001)	0.013*** (0.001)	0.002 (0.001)	0.013*** (0.001)
Net Flow	-0.002 (0.002)	-0.007 (0.020)	-0.002 (0.002)	0.027 (0.032)
Fund Age	0.0001 (0.0001)	-0.0003 (0.0003)	0.0002** (0.0001)	0.001* (0.001)
log(TNA)	-0.0004 (0.0004)	0.001 (0.001)	0.0003 (0.001)	0.001 (0.002)
Passive × % of Shares Outstanding	-0.214* (0.124)	-0.829 (0.934)	-0.101 (0.181)	-2.545** (1.188)
Mgmt Votes FOR × ISS Votes FOR	0.312*** (0.105)	Absorbed	0.303** (0.135)	0.298 (0.189)
CRSP Fund Style FE	Yes	Yes	Yes	Yes
Fund Family × Year FE	Yes	Yes	Yes	Yes
Firm × Year FE	Yes	Yes	Yes	Yes
Observations	8,268,725	117,720	1,958,257	30,516
Adjusted R ²	0.288	0.430	0.376	0.462

Significance levels 10%, 5%, and 1% are denoted by *, **, ***, respectively. Standard errors in parentheses are clustered at the firm and fund levels. Mutual funds are categorized as passive funds if their names contain at least one of the following strings: Index, Idx, Indx, Ind_ (where _ indicates a space), Russell, S & P, S and P, S&P, SandP, SP, DOW, Dow, DJ, MSCI, Bloomberg, KBW, NASDAQ, NYSE, STOXX, FTSE, Wilshire, Morningstar, 100, 400, 500, 600, 900, 1000, 1500, 2000, and 5000. We also use the classification variable provided by CRSP to identify passive mutual funds. TNA is total net assets under fund management. Contested agenda items are those that received (lacked) at most 5 percent above (below) the vote passing threshold.

Table 12: Impact of Passive Ownership on the Slate of Nominated Independent Directors

	<i>Dependent variable:</i>			
	Slate % of Independent Directors			
	(1)	(2)	(3)	(4)
Passive Ownership % of Mutual Funds	0.000*			-0.000
	(0.000)			(0.000)
Passive Ownership % of Total Shares Out.		0.028***		0.024***
		(0.008)		(0.008)
Passive % of Mutual Funds			0.075**	0.066*
			(0.035)	(0.036)
% Mgmt Votes FOR	0.186**	0.198**	0.187**	0.201**
	(0.089)	(0.086)	(0.089)	(0.085)
% ISS Votes FOR	0.178**	0.170**	0.172**	0.168**
	(0.077)	(0.072)	(0.078)	(0.071)
% Mgmt & ISS Agree	-0.082	-0.075	-0.076	-0.072
	(0.076)	(0.071)	(0.077)	(0.070)
log(Market Cap.)	0.010*	0.012**	0.014**	0.015**
	(0.005)	(0.006)	(0.006)	(0.006)
Number of Nominations	0.000	-0.000	0.000	-0.000
	(0.000)	(0.000)	(0.000)	(0.000)
Firm FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes
Observations	14,651	14,651	14,651	14,651
Adjusted R ²	0.231	0.231	0.231	0.232

Significance levels 10%, 5%, and 1% are denoted by *, **, ***, respectively. Standard errors in parentheses are clustered at the firm level. Mutual funds are categorized as passive funds if their names contain at least one of the following strings: Index, Idx, Indx, Ind_ (where _ indicates a space), Russell, S & P, S and P, S&P, SandP, SP, DOW, Dow, DJ, MSCI, Bloomberg, KBW, NASDAQ, NYSE, STOXX, FTSE, Wilshire, Morningstar, 100, 400, 500, 600, 900, 1000, 1500, 2000, and 5000. We also use the classification variable provided by CRSP to identify passive mutual funds. Average management and ISS disagreement variable, which ranges between 0 and 1, is defined as the average absolute difference between how management and ISS votes.

Appendix

A Passive Funds Vote Differently: Broad Categories

Table 13: Passive Funds Vote Differently within Fund Family

Proxy Agenda Categories	<i>Dependent variable:</i>			
	Shareholder Rights	Fund Votes with Management = 1		Board Issues
	Executive Compensation	Social Issues		
Passive	-0.047*** (0.014)	-0.025*** (0.006)	0.001 (0.008)	-0.003 (0.003)
% of TNA	0.221** (0.105)	0.512*** (0.073)	0.126 (0.091)	0.074** (0.037)
% of Shares Outstanding	1.158*** (0.397)	0.674*** (0.174)	1.355*** (0.373)	0.433*** (0.067)
ISS & Mgmt Agree	0.551*** (0.058)	0.442*** (0.014)	0.287*** (0.015)	0.427*** (0.013)
Turnover Ratio	-0.000* (0.000)	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)
Expense Ratio	-0.001 (0.001)	0.000 (0.000)	-0.000 (0.001)	0.001 (0.001)
Net Flow	0.005 (0.017)	0.012 (0.009)	-0.007 (0.014)	-0.00005 (0.002)
Fund Age	0.001** (0.000)	0.0003* (0.000)	-0.000* (0.000)	0.000 (0.000)
log(TNA)	-0.001 (0.002)	0.000 (0.001)	0.007*** (0.001)	-0.001 (0.001)
Passive × % of Shares Outstanding	-0.761 (0.909)	-0.483 (0.380)	-0.833 (0.758)	-0.443** (0.180)
CRSP Fund Style FE	Yes	Yes	Yes	Yes
Fund Family × Year FE	Yes	Yes	Yes	Yes
Firm × Year FE	Yes	Yes	Yes	Yes
ISS Agenda Type × Year FE	Yes	Yes	Yes	Yes
Observations	245,626	2,065,518	389,956	14,049,441
Adjusted R ²	0.588	0.393	0.466	0.373

Significance levels 10%, 5%, and 1% are denoted by *, **, ***, respectively. Standard errors in parentheses are clustered at the firm and fund levels. Mutual funds are categorized as passive funds if their names contain at least one of the following strings: Index, Idx, Indx, Ind_ (where _ indicates a space), Russell, S & P, S and P, S&P, SandP, SP, DOW, Dow, DJ, MSCI, Bloomberg, KBW, NASDAQ, NYSE, STOXX, FTSE, Wilshire, Morningstar, 100, 400, 500, 600, 900, 1000, 1500, 2000, and 5000. We also use the classification variable provided by CRSP to identify passive mutual funds. TNA is total net assets under fund management.

Table 14: Passive Funds Vote Differently within Fund Family for Contested Agenda Items

Proxy Agenda Categories	<i>Dependent variable:</i>			
	Shareholder Rights	Fund Votes with Management = 1		Board Issues
		Executive Compensation	Social Issues	
Passive	0.005 (0.008)	-0.042*** (0.009)	0.065 (0.066)	-0.017** (0.007)
% of TNA	0.184 (0.263)	0.298* (0.157)	4.392 (7.309)	0.003 (0.073)
% of Shares Outstanding	1.016 (0.886)	1.400*** (0.390)	-0.855 (1.472)	0.573* (0.293)
ISS & Mgmt Agree	Absorbed	0.430*** (0.068)	Absorbed	0.408*** (0.031)
Turnover Ratio	0.000 (0.000)	0.001** (0.000)	0.018 (0.046)	0.000 (0.000)
Expense Ratio	-0.000 (0.000)	-0.002 (0.003)	3.903 (8.101)	0.006*** (0.002)
Net Flow	-0.001 (0.026)	0.024 (0.019)	0.144 (0.495)	0.012 (0.014)
Fund Age	-0.000 (0.000)	0.000 (0.000)	0.000 (0.002)	0.000 (0.000)
log(TNA)	0.002 (0.001)	-0.000 (0.002)	0.003 (0.014)	-0.001 (0.001)
Passive \times % of Shares Outstanding	-1.536 (1.412)	-0.948 (0.671)	3.085*** (0.838)	-0.145 (0.582)
CRSP Fund Style FE	Yes	Yes	Yes	Yes
Fund Family \times Year FE	Yes	Yes	Yes	Yes
Firm \times Year FE	Yes	Yes	Yes	Yes
ISS Agenda Type \times Year FE	Yes	Yes	Yes	Yes
Observations	31,235	155,739	362	319,281
Adjusted R ²	0.718	0.399	0.478	0.515

Significance levels 10%, 5%, and 1% are denoted by *, **, ***, respectively. Standard errors in parentheses are clustered at the firm and fund levels. Mutual funds are categorized as passive funds if their names contain at least one of the following strings: Index, Idx, Indx, Ind_ (where _ indicates a space), Russell, S & P, S and P, S&P, SandP, SP, DOW, Dow, DJ, MSCI, Bloomberg, KBW, NASDAQ, NYSE, STOXX, FTSE, Wilshire, Morningstar, 100, 400, 500, 600, 900, 1000, 1500, 2000, and 5000. We also use the classification variable provided by CRSP to identify passive mutual funds. TNA is total net assets under fund management. Contested agenda items are those that received (lacked) at most 5 percent above (below) the vote passing threshold.

A.1 Shareholder Rights

The shareholder rights category generally include agenda items related to adopting a poison pill, requiring supermajority votes, declassifying boards, and giving equal voting rights to all shareholders (e.g., one share one vote). Regardless of whether ISS agrees with management, we find that passive mutual funds consistently disagree more with management than active mutual funds within same fund family. All else equal, passive mutual funds within a fund family are 4.7% more likely to disagree with management. This finding suggests that on average passive mutual funds do not necessarily blindly follow what ISS recommends.

[Insert Table 13]

A.2 Executive Compensation

The executive compensation category includes agenda items related to approving executive salaries, stock and stock option grants, and bonuses. Similar to shareholder rights related agenda items, we find that passive mutual funds are on average more likely to disagree with management regardless of whether ISS supports management recommendations. Controlling for ISS recommendations, passive mutual funds are about 2.5% more likely than active mutual funds to disagree with management recommendations. The magnitude of disagreement is much larger when ISS and management have conflicting recommendations: passive mutual funds disagree with management 10 percentage points more than active mutual funds.

A.3 Social Issues

Social issues related agenda items include proposals addressing energy efficiency, fair labor, and climate change, etc. For social issues, we find no significant differences in how passive and active mutual funds vote (Tables 13).

A.4 Board Issues

The board issues category is dominated by director elections, but may also include proposals to expand/reduce board size or to create more independent committees. As Table 13 shows, passive and active funds essentially vote the same way.