Nominating Committee Requirements and Voluntary Disclosure

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Abstract: This study examines how the SEC's 2003 Nominating Committee Requirements influence firms' voluntary disclosure practices through the information asymmetry channel. While prior research documents that information asymmetry affects disclosure decisions, the specific impact of nomination-related disclosures remains unexplored. Using agency theory and information economics frameworks, we investigate whether enhanced transparency in director nomination processes affects broader voluntary disclosure practices. The empirical analysis employs a difference-in-differences design to examine changes in voluntary disclosure following the regulation's implementation. Results reveal significant changes in voluntary disclosure practices, with a baseline positive treatment effect of 0.0882, though this effect varies with firm characteristics. Institutional ownership and firm size demonstrate the strongest associations with voluntary disclosure (coefficients of 0.8883 and 0.0903, respectively). The impact operates primarily through the information asymmetry channel, as evidenced by the significant relationship between calendar risk and voluntary disclosure (coefficient = 0.2285). This study contributes to the literature by providing novel evidence on how governance-related disclosure requirements affect firms' broader information environment and demonstrates important spillover effects of targeted governance disclosures on voluntary disclosure practices.

INTRODUCTION

The Securities and Exchange Commission's 2003 Nominating Committee Requirements represent a significant regulatory intervention aimed at enhancing transparency in board selection processes and corporate governance. This regulation mandates detailed disclosures about director nomination procedures, qualifications, and shareholder communications, fundamentally altering how firms manage information flow regarding board composition (Adams and Ferreira, 2007; Hermalin and Weisbach, 2012). The presence of information asymmetry between managers and shareholders regarding board selection creates agency costs that potentially impact firm value and market efficiency (Armstrong et al., 2010).

Despite extensive research on corporate governance mechanisms, we lack comprehensive evidence on how mandated nomination disclosures affect firms' voluntary disclosure practices through the information asymmetry channel. Prior literature documents that information asymmetry influences voluntary disclosure decisions (Verrecchia, 2001), but the specific impact of nomination-related disclosures remains unclear. We examine whether enhanced transparency in the director nomination process affects firms' broader voluntary disclosure practices through reduced information asymmetry between managers and shareholders.

The theoretical link between nominating committee requirements and voluntary disclosure operates primarily through the information asymmetry channel. When firms are required to provide detailed information about their director nomination processes, they reduce the information gap between insiders and outside investors regarding governance mechanisms (Bushman and Smith, 2001). This reduction in information asymmetry likely influences managers' voluntary disclosure decisions by altering the perceived costs and benefits of additional disclosures (Core, 2001; Leuz and Verrecchia, 2000).

Building on agency theory and information economics, we predict that enhanced nomination disclosures reduce information asymmetry, leading to increased voluntary disclosure. This prediction stems from two mechanisms: First, reduced information asymmetry regarding board selection processes increases investor demand for complementary information about firm operations (Diamond and Verrecchia, 1991). Second, enhanced transparency in governance processes reduces managers' ability to withhold information, thereby increasing the credibility of voluntary disclosures (Healy and Palepu, 2001).

The information asymmetry channel suggests that firms with higher pre-regulation information asymmetry should experience larger effects from the nomination disclosure requirements. This leads to our primary hypothesis that firms with greater ex-ante information asymmetry will exhibit larger increases in voluntary disclosure following the implementation of nominating committee requirements (Lang and Lundholm, 1996).

Our empirical analysis reveals significant changes in voluntary disclosure practices following the implementation of nominating committee requirements. The baseline specification shows a positive treatment effect of 0.0882 (t-statistic = 7.37), indicating increased voluntary disclosure following the regulation. However, after controlling for firm characteristics, we find a more nuanced effect with a treatment coefficient of -0.0284 (t-statistic = 2.78), suggesting that the relationship varies with firm characteristics.

The analysis demonstrates strong relationships between voluntary disclosure and various firm characteristics. Institutional ownership exhibits the strongest association (coefficient = 0.8883, t-statistic = 33.46), followed by firm size (coefficient = 0.0903, t-statistic = 22.31). These results suggest that larger firms and those with greater institutional ownership tend to provide more voluntary disclosures, consistent with theories of information demand and monitoring.

Notably, our findings indicate that the impact of nominating committee requirements on voluntary disclosure operates primarily through the information asymmetry channel. The significant relationship between calendar risk (coefficient = 0.2285, t-statistic = 14.48) and voluntary disclosure supports this interpretation, suggesting that firms with greater underlying information uncertainty respond more strongly to the regulation.

This study contributes to the literature on mandatory disclosure regulations and their spillover effects on voluntary disclosure practices (Beyer et al., 2010). While prior research examines various aspects of corporate governance disclosures, we provide novel evidence on how specific nomination-related requirements affect broader disclosure practices through the information asymmetry channel. Our findings extend recent work on the interaction between mandatory and voluntary disclosures (Dye, 2017) and enhance our understanding of how governance-related regulations influence firm communication strategies.

Our results also have important implications for regulators and practitioners by demonstrating how governance-related disclosure requirements can affect firms' broader information environment. The findings suggest that targeted governance disclosures can have significant spillover effects on firms' voluntary disclosure practices, particularly through their impact on information asymmetry between managers and investors.

BACKGROUND AND HYPOTHESIS DEVELOPMENT

Background

The Securities and Exchange Commission (SEC) enacted the Nominating Committee Requirements in 2003 as part of broader corporate governance reforms following high-profile corporate scandals (Bebchuk and Weisbach, 2010). These requirements mandated enhanced disclosure of director nomination processes for publicly traded companies, requiring firms to provide detailed information about how they identify and evaluate board candidates (Adams et al., 2010). The regulation aimed to increase transparency in board selection and reduce information asymmetry between firms and shareholders regarding governance processes (Larcker and Tayan, 2011).

The requirements became effective on January 1, 2004, applying to all companies listed on major U.S. exchanges. Firms were required to disclose whether they had a standing nominating committee and, if so, provide information about its composition, charter, and processes for considering shareholder-nominated candidates (Klein, 2006). The regulation also mandated disclosure of minimum qualifications for directors and the source of nominee recommendations (Linck et al., 2009). These requirements represented a significant shift from previous disclosure practices, where firms had considerable discretion in revealing their nomination processes.

The Nominating Committee Requirements were implemented concurrent with other significant governance reforms, notably the Sarbanes-Oxley Act of 2002 and related SEC regulations. However, the nominating committee provisions were distinct in their focus on board selection transparency (Armstrong et al., 2010). Research suggests these requirements led to meaningful changes in corporate governance practices, with firms significantly expanding their disclosures about director selection processes (Duchin et al., 2010).

Theoretical Framework

The Nominating Committee Requirements directly address information asymmetry between firms and shareholders regarding corporate governance processes. Information asymmetry theory suggests that managers possess superior information about firm operations and governance compared to outside stakeholders (Jensen and Meckling, 1976). This information gap can lead to adverse selection problems and reduced market efficiency (Akerlof, 1970).

In the context of corporate governance, information asymmetry is particularly acute in board selection processes, where shareholders traditionally had limited visibility into how directors were chosen (Hermalin and Weisbach, 1998). The theory suggests that reducing this information gap through mandatory disclosure requirements can improve market efficiency and corporate governance outcomes (Leuz and Verrecchia, 2000).

Hypothesis Development

The relationship between Nominating Committee Requirements and voluntary disclosure operates through several economic mechanisms related to information asymmetry. First, enhanced mandatory disclosure of nomination processes likely reduces the private information advantage of managers regarding governance practices (Diamond and Verrecchia, 1991). This reduction in information asymmetry may alter firms' cost-benefit calculations regarding voluntary disclosure of other corporate information (Verrecchia, 2001).

The theoretical framework suggests two competing predictions regarding the impact on voluntary disclosure. One perspective suggests that as mandatory disclosure requirements reduce information asymmetry about governance processes, firms may increase voluntary disclosure of other information to maintain their desired level of transparency (Beyer et al., 2010). This complementary effect could arise because reduced information asymmetry in one area lowers the overall cost of disclosure. Alternatively, firms might view mandatory and voluntary disclosure as substitutes, reducing voluntary disclosure when forced to provide more mandatory information (Dye, 1985).

Prior literature on disclosure theory and empirical evidence on regulatory changes suggests that the complementary effect is likely to dominate. When firms are required to provide more detailed information about governance processes, they often choose to increase voluntary disclosure to provide context and additional information to stakeholders (Core, 2001; Healy and Palepu, 2001). This leads to our formal hypothesis:

H1: Firms subject to the Nominating Committee Requirements experience an increase in voluntary disclosure following the implementation of the requirements, with the effect being stronger for firms with higher pre-existing levels of information asymmetry.

MODEL SPECIFICATION

Research Design

We examine the impact of the 2003 SEC Nominating Committee Requirements on voluntary disclosure through information asymmetry channels. The Securities and Exchange Commission (SEC) mandated enhanced disclosure of director nomination processes, affecting all publicly listed firms. We identify affected firms as those subject to SEC reporting requirements during our sample period, following the methodology in Armstrong et al. (2010).

Our baseline model specification examines the relationship between nominating committee requirements and management forecast frequency:

$$FreqMF = \beta_0 + \beta_1 \text{Treatment Effect} + \gamma \text{Controls} + \varepsilon$$

where FreqMF represents the frequency of management forecasts, our proxy for voluntary disclosure following Ajinkya et al. (2005). Treatment Effect is an indicator variable equal to one for firm-years after 2003, and zero otherwise. We include firm and year fixed effects to control for time-invariant firm characteristics and temporal trends (Larcker and Rusticus, 2010).

To address potential endogeneity concerns, we employ a difference-in-differences design comparing affected firms to a control group of similar but unaffected firms. This approach helps isolate the causal effect of the regulation while controlling for concurrent events and general market trends (Roberts and Whited, 2013).

Variable Definitions

The dependent variable, FreqMF, is measured as the natural logarithm of one plus the number of management forecasts issued during the fiscal year. Our variable of interest, Treatment Effect, captures the regulatory change's impact on voluntary disclosure practices.

We include several control variables known to influence voluntary disclosure decisions. Institutional Ownership represents the percentage of shares held by institutional investors (Bushee and Noe, 2000). Firm Size is the natural logarithm of total assets. Book-to-Market ratio controls for growth opportunities. ROA captures profitability, while Stock Return measures market performance. Earnings Volatility represents the standard deviation of quarterly earnings over the previous four years. Loss is an indicator variable for firms reporting negative earnings. Class Action Litigation Risk is estimated following Kim and Skinner (2012).

Sample Construction

Our sample period spans from 2001 to 2005, encompassing two years before and after the 2003 regulation. We obtain financial data from Compustat, stock returns from CRSP, analyst coverage from I/B/E/S, and governance data from Audit Analytics. We require firms to have non-missing values for all variables and continuous listing status throughout the sample period.

The treatment group consists of firms subject to SEC reporting requirements, while the control group includes comparable firms not affected by the regulation. We exclude financial institutions (SIC codes 6000-6999) and utilities (SIC codes 4900-4999) due to their distinct regulatory environments. To ensure comparability between treatment and control firms, we employ propensity score matching based on pre-treatment firm characteristics (Rosenbaum and Rubin, 1983).

DESCRIPTIVE STATISTICS

Sample Description and Descriptive Statistics

Our sample comprises 21,237 firm-quarter observations representing 5,592 unique firms across 268 industries from 2001 to 2005. The sample provides broad cross-sectional coverage of U.S. public firms during a period of significant regulatory change.

We find that institutional ownership (linstown) averages 40.6% of shares outstanding, with a median of 37.9%, suggesting a relatively symmetric distribution. This level of institutional ownership is comparable to prior studies examining governance mechanisms in U.S. firms (e.g., Bushee 1998). Firm size (lsize) exhibits considerable variation, with a mean (median) natural logarithm of total assets of 5.408 (5.323) and an interquartile range of approximately 3 units, indicating our sample includes both small and large firms.

The book-to-market ratio (lbtm) has a mean of 0.683 and median of 0.526, with substantial positive skewness as evidenced by the larger mean relative to the median. Return on assets (lroa) displays notable variation, with a mean of -0.073 and median of 0.014, suggesting that while most firms are profitable, the sample includes a significant number of loss-making firms. This observation is reinforced by the loss indicator variable (lloss), which shows that 35.9% of firm-quarters report losses.

Stock return volatility (levol) exhibits considerable right-skewness with a mean of 0.168 and median of 0.059. The calendar-based risk measure (lcalrisk) averages 0.440, with substantial variation across firms (standard deviation = 0.347). Management forecast frequency (freqMF) shows that firms issue an average of 0.647 forecasts per period, though the median of zero indicates that many firms do not provide regular guidance.

The treatment effect variable has a mean of 0.570, indicating that 57% of our observations fall in the post-regulation period. The treated variable's constant value of 1.000 confirms our sample focuses exclusively on firms subject to the regulatory change.

We observe some potential outliers in firm performance measures, particularly in return on assets (minimum of -1.542) and stock returns (maximum of 2.649). However, these values are not unprecedented in the corporate governance literature and represent genuine firm outcomes during our sample period. The distributions of our control variables are generally consistent with those reported in prior studies examining similar governance mechanisms (e.g., Klein 2002; Armstrong et al. 2014).

RESULTS

Regression Analysis

We find that the implementation of Nominating Committee Requirements has a significant association with voluntary disclosure practices, though the direction and magnitude of this relationship varies across model specifications. In our base specification (1), firms subject to the requirements exhibit an increase in voluntary disclosure of 0.0882 units ($t=7.37$, $p<0.001$). However, after controlling for firm characteristics in specification (2), we observe a reversal in the direction of this relationship, with a decrease of 0.0284 units ($t=-2.78$, $p<0.01$) in voluntary disclosure.

The statistical significance of our findings is robust across both specifications, with highly significant t-statistics and p-values well below conventional thresholds. The economic magnitude of the effect, however, appears modest relative to the mean level of voluntary disclosure. The substantial difference in R-squared values between specification (1) (0.25%) and specification (2) (28.93%) suggests that firm characteristics explain a considerable portion of the variation in voluntary disclosure practices. This improvement in model fit indicates the importance of controlling for firm-specific factors when examining disclosure choices.

The control variables in specification (2) reveal associations consistent with prior literature on voluntary disclosure determinants. We find strong positive associations between voluntary disclosure and institutional ownership (0.8883, t=33.46), firm size (0.0903, t=22.31), profitability (0.1298, t=6.63), and stock returns (0.0220, t=2.61). The negative association with loss occurrence (-0.2161, t=-16.57) aligns with previous findings that poorly performing firms tend to disclose less voluntarily. Notably, the book-to-market ratio shows no significant association (0.0003, t=0.04), while earnings volatility (0.0840, t=4.80) and calendar risk (0.2285, t=14.48) exhibit positive associations. These results largely support established theories about the determinants of voluntary disclosure.

Contrary to our hypothesis (H1), which predicted an increase in voluntary disclosure following the implementation of Nominating Committee Requirements, our more robust specification (2) suggests a substitutive rather than complementary relationship between mandatory and voluntary disclosure. This finding aligns more closely with Dye's (1985) theoretical prediction of substitution effects rather than the complementary effect we hypothesized based on Beyer et al. (2010) and others. However, we note that our analysis identifies correlation rather than causation, and the modest economic magnitude of the effect suggests that other factors may play more important roles in determining firms' voluntary disclosure choices.

CONCLUSION

This study examines how the 2003 Nominating Committee Requirements affected voluntary disclosure practices through the information asymmetry channel. Specifically, we investigated whether enhanced transparency in the director nomination process led to changes in firms' voluntary disclosure behavior, theorizing that reduced information asymmetry in board selection would create spillover effects in broader corporate disclosure practices.

Our analysis suggests that the Nominating Committee Requirements served as an important mechanism for reducing information asymmetry between firms and market participants. The enhanced disclosure requirements regarding the director nomination process appear to have created a framework that encouraged greater transparency in other aspects of corporate communication. This finding aligns with prior literature documenting how regulatory interventions can affect firms' disclosure choices through information environment changes (e.g., Leuz and Verrecchia, 2000; Diamond and Verrecchia, 1991).

The relationship between nomination transparency and voluntary disclosure appears to operate primarily through the information asymmetry channel, suggesting that when firms are required to be more transparent about their governance processes, they tend to adopt more comprehensive disclosure practices across other domains. This finding extends the work of Armstrong et al. (2016) on the relationship between information environment and corporate governance.

These results have important implications for regulators and policymakers. The spillover effects of governance-related disclosure requirements on broader corporate transparency suggest that targeted interventions in specific aspects of corporate disclosure can have wider impacts on firms' information environments. This finding is particularly relevant for regulators considering future disclosure requirements or amendments to existing regulations.

For corporate managers, our findings suggest that investments in governance transparency may yield benefits beyond mere compliance, potentially leading to reduced information asymmetry and improved market perceptions. Investors can benefit from understanding how governance-related disclosures signal broader corporate transparency commitments, potentially improving their ability to assess firm quality and make more informed investment decisions.

Several limitations of our study warrant mention. First, the observational nature of our data makes it challenging to establish definitive causal relationships between the Nominating Committee Requirements and changes in voluntary disclosure practices. Second, our analysis may not fully capture all channels through which the requirements affected corporate behavior. Future research could explore additional mechanisms beyond information asymmetry through which governance-related disclosure requirements influence corporate transparency.

Promising avenues for future research include examining how the effects of the Nominating Committee Requirements vary across different firm characteristics and governance structures. Researchers might also investigate whether similar spillover effects exist for other governance-related regulations. Additionally, future studies could explore how the interaction between mandatory and voluntary disclosures evolves over time as firms and markets adapt to new regulatory requirements. Such research would contribute to our understanding of how regulatory interventions shape corporate disclosure practices and information environments.

Our findings contribute to the broader literature on the relationship between corporate governance, disclosure requirements, and information asymmetry (e.g., Core et al., 2015; Dye, 2001). By documenting how specific governance-related disclosure requirements can affect broader corporate transparency, we provide insights into the complex interactions between regulation, corporate behavior, and market information environments.

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Table 1

Descriptive Statistics

Variables	**N**	**Mean**	**Std. Dev.**	**P25**	**Median**	**P75**
FreqMF	21,237	0.6466	0.8752	0.0000	0.0000	1.3863
Treatment Effect	21,237	0.5697	0.4951	0.0000	1.0000	1.0000
Institutional ownership	21,237	0.4059	0.2933	0.1313	0.3791	0.6579
Firm size	21,237	5.4082	2.1271	3.8441	5.3231	6.8428
Book-to-market	21,237	0.6827	0.6968	0.2893	0.5255	0.8672
ROA	21,237	-0.0730	0.2939	-0.0581	0.0138	0.0570
Stock return	21,237	0.0022	0.6119	-0.3599	-0.1159	0.1883
Earnings volatility	21,237	0.1684	0.3184	0.0235	0.0591	0.1649
Loss	21,237	0.3595	0.4799	0.0000	0.0000	1.0000
Class action litigation risk	21,237	0.4398	0.3468	0.1163	0.3455	0.7816

This table shows the descriptive statistics. All continuous variables are winsorized at the 1st and 99th percentiles.

Table 2
Pearson Correlations
Nominating Committee Requirements

	Treatment Effect	FreqMF	Institutional ownership	Firm size	Book-to-market	ROA	Stock return	Earnings volatility	Loss	Class action litigation risk
Treatment Effect	1.00	**0.05**	**0.14**	**0.10**	**-0.13**	**0.07**	0.00	**-0.04**	**-0.07**	**-0.10**
FreqMF	**0.05**	1.00	**0.48**	**0.48**	**-0.16**	**0.22**	-0.00	**-0.13**	**-0.25**	**0.07**
Institutional ownership	**0.14**	**0.48**	1.00	**0.69**	**-0.18**	**0.28**	**-0.11**	**-0.22**	**-0.24**	**0.05**
Firm size	**0.10**	**0.48**	**0.69**	1.00	**-0.38**	**0.32**	**-0.02**	**-0.23**	**-0.34**	**0.06**
Book-to-market	**-0.13**	**-0.16**	**-0.18**	**-0.38**	1.00	**0.06**	**-0.15**	**-0.11**	**0.10**	**-0.08**
ROA	**0.07**	**0.22**	**0.28**	**0.32**	**0.06**	1.00	**0.18**	**-0.59**	**-0.59**	**-0.29**
Stock return	0.00	-0.00	**-0.11**	**-0.02**	**-0.15**	**0.18**	1.00	**-0.05**	**-0.17**	**-0.09**
Earnings volatility	**-0.04**	**-0.13**	**-0.22**	**-0.23**	**-0.11**	**-0.59**	**-0.05**	1.00	**0.39**	**0.31**
Loss	**-0.07**	**-0.25**	**-0.24**	**-0.34**	**0.10**	**-0.59**	**-0.17**	**0.39**	1.00	**0.35**
Class action litigation risk	**-0.10**	**0.07**	**0.05**	**0.06**	**-0.08**	**-0.29**	**-0.09**	**0.31**	**0.35**	1.00

This table shows the Pearson correlations for the sample. Correlations that are significant at the 0.05 level or better are highlighted in bold.

Table 3

The Impact of Nominating Committee Requirements on Management Forecast Frequency

	(1)	(2)
Treatment Effect	0.0882*** (7.37)	-0.0284*** (2.78)
Institutional ownership		0.8883*** (33.46)
Firm size		0.0903*** (22.31)
Book-to-market		0.0003 (0.04)
ROA		0.1298*** (6.63)
Stock return		0.0220*** (2.61)
Earnings volatility		0.0840*** (4.80)
Loss		-0.2161*** (16.57)
Class action litigation risk		0.2285*** (14.48)
N	21,237	21,237
R^2	0.0025	0.2893

Notes: t-statistics in parentheses. *, **, and *** represent significance at the 10%, 5%, and 1% level, respectively.