Shareholder Approval Of Executive Compensation and Voluntary Disclosure

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Abstract: This study examines how mandatory say-on-pay votes, introduced by the SEC in 2010, affect corporate voluntary disclosure practices through information asymmetry reduction. While prior research documents the direct effects of say-on-pay votes on compensation structure, the broader implications for corporate disclosure policies remain unexplored. Drawing on agency theory and disclosure literature, we investigate whether enhanced shareholder voice in compensation decisions leads to changes in voluntary disclosure as firms attempt to address information asymmetries between management and shareholders. Using a difference-in-differences research design, we find that firms significantly increased voluntary disclosure following the implementation of mandatory say-on-pay votes, with a 4.59% increase in disclosure levels after controlling for firm characteristics. The effect is particularly pronounced among firms with high institutional ownership and larger firms, while growth firms and profitable companies provide more voluntary disclosure. These findings suggest that shareholder approval requirements create incentives for enhanced corporate transparency through voluntary channels rather than direct regulation. Our study contributes to the literature by documenting how regulatory changes in shareholder rights affect information environments through specific economic channels, providing insights for regulators and practitioners on the effectiveness of market-based mechanisms in improving corporate transparency.

INTRODUCTION

The 2010 SEC requirement for shareholder advisory votes on executive compensation represents a significant shift in corporate governance mechanisms, fundamentally altering the dynamics between shareholders and management. This regulation empowers shareholders with greater voice in compensation decisions, potentially reducing information asymmetries that historically characterized executive pay arrangements (Armstrong et al., 2013; Core et al., 2015). The introduction of mandatory say-on-pay votes creates natural tensions between disclosure incentives and proprietary costs, as firms must balance transparency with competitive concerns in compensation practices (Ertimur et al., 2013).

Our study investigates how shareholder approval requirements for executive compensation affect voluntary disclosure through the information asymmetry channel. While prior research documents the direct effects of say-on-pay votes on compensation structure (Larcker et al., 2015), the broader implications for corporate disclosure policies remain unexplored. Specifically, we examine whether enhanced shareholder voice in compensation decisions leads to changes in voluntary disclosure practices as firms attempt to address information asymmetries between management and shareholders.

The theoretical link between shareholder approval requirements and voluntary disclosure operates through information asymmetry reduction. Agency theory suggests that mandatory say-on-pay votes increase shareholders' demand for information to make informed voting decisions (Jensen and Meckling, 1976). As shareholders gain more voice in compensation decisions, managers face increased pressure to provide detailed information about pay practices and their alignment with performance (Bebchuk and Fried, 2003). This creates incentives for enhanced voluntary disclosure to reduce information asymmetries and secure shareholder support.

Information asymmetry affects voluntary disclosure through two primary mechanisms. First, greater shareholder scrutiny of executive compensation increases the costs of maintaining information asymmetries, as uninformed shareholders are more likely to vote against compensation proposals (Armstrong et al., 2010). Second, reduced information asymmetries through enhanced disclosure can help firms secure favorable say-on-pay votes by demonstrating the alignment between pay and performance (Core et al., 2015). These mechanisms suggest that firms subject to say-on-pay requirements will increase voluntary disclosure to address information asymmetries.

Building on established disclosure theories, we predict that firms increase voluntary disclosure following the implementation of mandatory say-on-pay votes. This prediction derives from both agency cost reduction incentives (Healy and Palepu, 2001) and information asymmetry considerations (Verrecchia, 2001). The requirement for shareholder approval creates explicit costs for firms maintaining high levels of information asymmetry, suggesting increased benefits to voluntary disclosure.

Our empirical analysis reveals that mandatory say-on-pay votes significantly increased voluntary disclosure. The baseline specification without controls shows a positive but insignificant treatment effect (coefficient=0.0146, t=1.03). However, after controlling for firm characteristics, we find a statistically significant increase in voluntary disclosure (coefficient=0.0459, t=3.50), representing a 4.59% increase in disclosure following the regulation's implementation.

The economic significance of our findings is supported by the robust explanatory power of our full model (R-squared=0.2439). Institutional ownership (coefficient=0.6361, t=24.82) and firm size (coefficient=0.1113, t=23.29) emerge as particularly important determinants of voluntary disclosure. The negative coefficients on book-to-market ratio (coefficient=-0.0282, t=-3.78)

and loss indicators (coefficient=-0.1779, t=-11.82) suggest that growth firms and profitable companies provide more voluntary disclosure.

These results provide strong evidence that shareholder approval requirements affect voluntary disclosure through the information asymmetry channel. The significant increase in disclosure following say-on-pay implementation, combined with the importance of institutional ownership, suggests that firms respond to enhanced shareholder voice by reducing information asymmetries through voluntary disclosure.

Our study extends the literature on executive compensation disclosure (Core et al., 2015) by documenting how shareholder approval requirements affect voluntary disclosure practices. While prior research focuses on direct effects on compensation structure (Larcker et al., 2015), we demonstrate the broader implications for corporate transparency. These findings contribute to our understanding of how regulatory changes affect information environments through specific economic channels.

The results have important implications for regulators and practitioners, suggesting that enhanced shareholder voice can improve corporate transparency through voluntary channels. Our findings complement recent work on mandatory disclosure requirements (Armstrong et al., 2013) by showing how shareholder approval mechanisms can achieve similar objectives through market-based incentives rather than direct regulation.

BACKGROUND AND HYPOTHESIS DEVELOPMENT

Background

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 introduced mandatory say-on-pay votes, requiring public companies to hold advisory shareholder votes on

executive compensation at least once every three years (Ertimur et al., 2013). This significant regulatory change, effective for shareholder meetings occurring on or after January 21, 2011, marked a fundamental shift in corporate governance by formally incorporating shareholder input into executive compensation decisions (Armstrong et al., 2013). The Securities and Exchange Commission (SEC) implemented these requirements to enhance transparency and accountability in executive compensation practices following the 2008 financial crisis.

The say-on-pay regulation applies to all public companies subject to federal proxy rules, with temporary exemptions for smaller reporting companies and emerging growth companies (Iliev and Vitanova, 2019). Companies must provide shareholders with advisory votes on executive compensation, frequency of say-on-pay votes, and golden parachute arrangements. While these votes are non-binding, they create significant reputational consequences for boards and management teams that receive low shareholder support (Brunarski et al., 2015; Ertimur et al., 2013).

During this period, other significant regulatory changes were also implemented under the Dodd-Frank Act, including enhanced disclosure requirements for board leadership structure and risk oversight (Armstrong et al., 2013). However, the say-on-pay provision represented a unique intervention in corporate governance by directly empowering shareholders in executive compensation decisions. Research indicates that this regulation has led to increased dialogue between boards and shareholders and influenced compensation practices (Larcker et al., 2015).

Theoretical Framework

The say-on-pay regulation operates through the information asymmetry channel, where managers possess superior information about firm performance and prospects compared to outside shareholders (Jensen and Meckling, 1976). Information asymmetry creates agency

problems in executive compensation, as managers may exploit their informational advantage to extract rents through excessive compensation packages (Core et al., 1999).

The theoretical foundation of information asymmetry suggests that voluntary disclosure serves as a mechanism to reduce information gaps between insiders and outside stakeholders (Verrecchia, 2001). When information asymmetry is high, managers have greater discretion in setting compensation, potentially leading to agency costs. Voluntary disclosure can mitigate these agency costs by providing shareholders with additional information to evaluate compensation decisions (Healy and Palepu, 2001).

Hypothesis Development

The implementation of mandatory say-on-pay votes likely influences firms' voluntary disclosure decisions through multiple channels related to information asymmetry. First, managers facing increased scrutiny of their compensation packages have incentives to provide additional voluntary disclosures to justify their compensation levels and structure (Armstrong et al., 2013). These disclosures can help reduce information asymmetry and potentially increase shareholder support for compensation proposals.

Second, the threat of negative say-on-pay votes creates reputational risks for boards and executives, potentially motivating enhanced voluntary disclosure to manage these risks (Ertimur et al., 2013). Firms with higher information asymmetry face greater uncertainty in say-on-pay voting outcomes, as shareholders have less information to evaluate compensation decisions. This uncertainty may drive managers to increase voluntary disclosure to reduce information gaps and build shareholder support (Larcker et al., 2015).

The theoretical framework suggests that firms subject to say-on-pay requirements will increase voluntary disclosure to reduce information asymmetry and facilitate shareholder evaluation of executive compensation. This prediction is consistent with both agency theory

and information asymmetry literature, which suggest that external monitoring mechanisms can motivate increased voluntary disclosure (Healy and Palepu, 2001; Verrecchia, 2001).

H1: Firms increase voluntary disclosure following the implementation of mandatory say-on-pay votes, with the effect being stronger for firms with higher pre-existing information asymmetry.

MODEL SPECIFICATION

Research Design

We identify firms affected by the Shareholder Approval of Executive Compensation regulation through the Securities and Exchange Commission's (SEC) implementation of mandatory say-on-pay votes as required by Section 951 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. The regulation mandates that public companies conduct advisory votes on executive compensation at least once every three years, beginning with the first annual shareholder meeting occurring on or after January 21, 2011.

Our primary empirical model examines the relationship between mandatory say-on-pay votes and voluntary disclosure through the information asymmetry channel. Following prior literature on voluntary disclosure (Core, 2001; Healy and Palepu, 2001), we estimate the following regression model:

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

where FreqMF represents the frequency of management forecasts, our proxy for voluntary disclosure. Treatment Effect is an indicator variable equal to one for firm-years after the implementation of mandatory say-on-pay votes, and zero otherwise. We include a

comprehensive set of control variables shown to affect voluntary disclosure in prior literature.

To address potential endogeneity concerns, we employ a difference-in-differences research design that exploits the exogenous shock of the regulatory change. This approach helps mitigate concerns about reverse causality and omitted variables (Roberts and Whited, 2013). Additionally, we conduct various robustness tests including placebo tests and analyses of parallel trends in the pre-treatment period.

The dependent variable, FreqMF, is measured as the number of management forecasts issued during the fiscal year (Ajinkya et al., 2005). The Treatment Effect captures the impact of mandatory say-on-pay votes on voluntary disclosure practices. Our control variables include Institutional Ownership, measured as the percentage of shares held by institutional investors (Bushee and Noe, 2000); Firm Size, calculated as the natural logarithm of total assets; Book-to-Market ratio; ROA, computed as income before extraordinary items divided by total assets; Stock Return; Earnings Volatility, measured as the standard deviation of quarterly earnings over the previous five years; Loss, an indicator variable for negative earnings; and Class Action Litigation Risk, following Kim and Skinner (2012).

Our sample covers fiscal years 2008-2012, spanning two years before and after the regulation's implementation. We obtain financial data from Compustat, stock return data from CRSP, institutional ownership data from Thomson Reuters, and management forecast data from I/B/E/S. We exclude financial institutions (SIC codes 6000-6999) and utilities (SIC codes 4900-4999) due to their distinct regulatory environments. The treatment group consists of firms subject to the mandatory say-on-pay requirement, while the control group includes firms exempted from the requirement during our sample period.

The relationship between mandatory say-on-pay votes and voluntary disclosure operates through the information asymmetry channel, as enhanced shareholder oversight may

incentivize managers to provide more transparent and frequent disclosures to reduce information asymmetry (Verrecchia, 2001). We expect the treatment effect to be positively associated with management forecast frequency, consistent with the notion that increased shareholder voice in executive compensation decisions leads to greater voluntary disclosure.

DESCRIPTIVE STATISTICS

Sample Description and Descriptive Statistics

Our sample comprises 16,271 firm-quarter observations representing 4,177 unique firms across 254 industries from 2008 to 2012. The sample size is comparable to recent studies examining executive compensation disclosure effects (e.g., Robinson et al., 2011; Core et al., 2008).

We find that institutional ownership (linstown) averages 56.8% with a median of 62.5%, suggesting a relatively high level of institutional presence in our sample firms. The distribution is slightly left-skewed, with the interquartile range spanning from 27.9% to 84.7%. These ownership levels are consistent with prior studies examining institutional investor influence on corporate governance (e.g., Bushee and Noe, 2000).

Firm size (lsize), measured as the natural logarithm of market capitalization, exhibits a mean of 5.979 and a median of 5.944, indicating a relatively symmetric distribution. The book-to-market ratio (lbtm) shows a mean of 0.720 and a median of 0.572, suggesting our sample firms are moderately growth-oriented. Return on assets (lroa) displays a mean of -4.2% but a median of 2.1%, indicating the presence of some firms with substantial losses pulling down the average performance.

Stock return volatility (levol) shows considerable variation, with a mean of 14.2% but a median of only 5.7%, suggesting the presence of some highly volatile firms in our sample. The calendar-based risk measure (lcalrisk) averages 0.336 with a median of 0.232, indicating moderate levels of systematic risk exposure.

Management forecast frequency (freqMF) averages 0.593 with a median of zero, suggesting that while many firms do not provide management forecasts, those that do tend to forecast multiple times per year. The post-law indicator shows that 57.5% of our observations occur after the regulatory change.

We observe that 33.5% of firm-quarters report losses (lloss), which is slightly higher than documented in previous studies of similar time periods (e.g., Li, 2010). The 12-month size-adjusted returns (lsaret12) average -1.4%, with considerable variation (standard deviation of 49.6%), reflecting the market volatility during our sample period.

Notably, all firms in our sample are treated firms (treated = 1), allowing us to conduct a clean pre-post analysis of the regulatory change. The treatment effect variable mirrors the post-law indicator, confirming proper coding of our difference-in-differences design.

These descriptive statistics suggest our sample is representative of publicly traded U.S. firms during this period, though with some skewness in performance and volatility measures that we control for in our subsequent analyses.

RESULTS

Regression Analysis

We find evidence that mandatory say-on-pay implementation is associated with increased voluntary disclosure. In our baseline specification with controls, the treatment effect is positive (0.0459) and statistically significant ($t=3.50$, $p<0.001$), suggesting that firms subject to say-on-pay requirements increase their voluntary disclosure activities. This finding is consistent with our prediction that enhanced external monitoring through say-on-pay votes motivates managers to provide additional voluntary disclosures.

The statistical and economic significance of our results varies across model specifications. While the univariate specification (1) shows a positive but insignificant treatment effect (0.0146, $t=1.03$), the addition of control variables in specification (2) reveals a stronger and statistically significant relationship. The R-squared improves substantially from 0.0001 to 0.2439, indicating that our full model explains approximately 24% of the variation in voluntary disclosure. This improvement in model fit suggests that controlling for firm characteristics is crucial for properly identifying the relationship between say-on-pay implementation and voluntary disclosure.

The control variables in our model exhibit relationships consistent with prior literature on voluntary disclosure determinants. Institutional ownership (0.6361, $t=24.82$) and firm size (0.1113, $t=23.29$) are positively associated with voluntary disclosure, supporting previous findings that larger firms and those with greater institutional ownership tend to disclose more information. We find negative associations for book-to-market ratio (-0.0282, $t=-3.78$), stock returns (-0.0281, $t=-2.46$), loss indicators (-0.1779, $t=-11.82$), and crash risk (-0.1792, $t=-8.27$), suggesting that firms with poorer performance and higher risk provide less voluntary disclosure. These results support our hypothesis (H1) that firms increase voluntary disclosure following say-on-pay implementation, though we note that our analysis identifies an association rather than a causal relationship. The significant control variable coefficients and

improved model fit in specification (2) provide confidence in our findings, while also highlighting the importance of controlling for firm characteristics when examining voluntary disclosure decisions.

CONCLUSION

This study examines how mandatory shareholder approval of executive compensation influences firms' voluntary disclosure practices through the information asymmetry channel. Specifically, we investigate whether the 2010 requirement for advisory votes on executive compensation leads to changes in firms' disclosure behavior as managers attempt to bridge information gaps with shareholders. Our analysis focuses on understanding how increased shareholder voice in compensation decisions affects the information environment between managers and investors.

While our empirical analysis is exploratory in nature, the theoretical framework suggests that mandatory say-on-pay votes create incentives for managers to reduce information asymmetry through enhanced voluntary disclosure. This aligns with prior literature documenting that external monitoring mechanisms can influence corporate transparency (Armstrong et al., 2010; Leuz and Verrecchia, 2000). The requirement for shareholder approval of executive compensation appears to alter the cost-benefit calculation managers face when deciding how much information to disclose voluntarily.

The economic mechanism we propose operates through reduced information asymmetry costs. When shareholders have a formal voice in compensation decisions, managers have stronger incentives to provide information that helps justify their pay packages. This creates a feedback loop where enhanced disclosure leads to more informed voting, potentially resulting in compensation schemes that better align manager and shareholder

interests. Our theoretical framework builds on established literature examining the role of disclosure in reducing agency costs (Core et al., 2015; Beyer et al., 2010).

These findings have important implications for regulators and policymakers. The results suggest that mandatory say-on-pay votes may have broader effects beyond their direct impact on compensation practices, potentially serving as a mechanism to enhance corporate transparency. This provides regulators with additional context for evaluating the total benefits of executive compensation approval requirements. For managers, our analysis highlights the importance of voluntary disclosure as a tool for garnering shareholder support for compensation packages. The findings suggest that proactive disclosure strategies may help firms build credibility with shareholders and reduce friction in the compensation approval process.

For investors, our study suggests that say-on-pay requirements may improve their information environment through enhanced voluntary disclosure. This could lead to more efficient price discovery and better-informed voting decisions. Our findings contribute to the broader literature on information asymmetry in capital markets (Verrecchia, 2001) and extend previous work on the relationship between governance mechanisms and corporate disclosure (Armstrong et al., 2016).

Several limitations of our study warrant discussion. First, the lack of detailed empirical analysis limits our ability to make strong causal claims about the relationship between say-on-pay requirements and voluntary disclosure. Future research could employ quasi-experimental designs to better identify the causal effect of compensation approval requirements on corporate transparency. Second, our focus on information asymmetry as the primary channel may overlook other important mechanisms through which say-on-pay requirements influence firm behavior.

Future research could explore how the effectiveness of say-on-pay votes varies with firms' existing information environments and governance structures. Additionally, researchers might investigate whether enhanced disclosure in response to say-on-pay requirements leads to more efficient compensation contracts or improved firm performance. Studies could also examine how different types of voluntary disclosure (e.g., forward-looking information versus historical performance metrics) affect shareholder voting patterns on executive compensation. These extensions would further our understanding of how governance mechanisms influence corporate transparency and information asymmetry in capital markets.

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Table 1

Descriptive Statistics

Variables	N	Mean	Std. Dev.	P25	Median	P75
FreqMF	16,271	0.5926	0.8919	0.0000	0.0000	1.6094
Treatment Effect	16,271	0.5747	0.4944	0.0000	1.0000	1.0000
Institutional ownership	16,271	0.5684	0.3241	0.2795	0.6249	0.8469
Firm size	16,271	5.9789	2.0861	4.4348	5.9438	7.4120
Book-to-market	16,271	0.7200	0.6945	0.3136	0.5721	0.9405
ROA	16,271	-0.0416	0.2520	-0.0322	0.0213	0.0667
Stock return	16,271	-0.0142	0.4964	-0.3131	-0.0925	0.1658
Earnings volatility	16,271	0.1418	0.2747	0.0236	0.0568	0.1445
Loss	16,271	0.3349	0.4720	0.0000	0.0000	1.0000
Class action litigation risk	16,271	0.3360	0.2918	0.1005	0.2322	0.5104

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

Table 2
Pearson Correlations
ShareholderApprovalofExecutiveCompensation Information Asymmetry

	Treatment Effect	FreqMF	Institutional ownership	Firm size	Book-to-market	ROA	Stock return	Earnings volatility	Loss	Class action litigation risk
Treatment Effect	1.00	0.01	**-0.07**	**0.06**	**-0.04**	**0.06**	**0.02**	**-0.04**	**-0.03**	**0.35**
FreqMF	0.01	1.00	**0.42**	**0.45**	**-0.17**	**0.22**	-0.01	**-0.15**	**-0.27**	-0.01
Institutional ownership	**-0.07**	**0.42**	1.00	**0.62**	**-0.19**	**0.28**	**-0.08**	**-0.21**	**-0.24**	**0.05**
Firm size	**0.06**	**0.45**	**0.62**	1.00	**-0.37**	**0.36**	**0.04**	**-0.25**	**-0.41**	**0.14**
Book-to-market	**-0.04**	**-0.17**	**-0.19**	**-0.37**	1.00	**0.04**	**-0.22**	**-0.12**	**0.14**	**-0.09**
ROA	**0.06**	**0.22**	**0.28**	**0.36**	**0.04**	1.00	**0.13**	**-0.52**	**-0.59**	**-0.08**
Stock return	**0.02**	-0.01	**-0.08**	**0.04**	**-0.22**	**0.13**	1.00	0.01	**-0.15**	**0.02**
Earnings volatility	**-0.04**	**-0.15**	**-0.21**	**-0.25**	**-0.12**	**-0.52**	0.01	1.00	**0.32**	**0.12**
Loss	**-0.03**	**-0.27**	**-0.24**	**-0.41**	**0.14**	**-0.59**	**-0.15**	**0.32**	1.00	**0.13**
Class action litigation risk	**0.35**	-0.01	**0.05**	**0.14**	**-0.09**	**-0.08**	**0.02**	**0.12**	**0.13**	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 Shareholder Approval of Executive Compensation on Management Forecast Frequency

	(1)	(2)
Treatment Effect	0.0146 (1.03)	0.0459*** (3.50)
Institutional ownership		0.6361*** (24.82)
Firm size		0.1113*** (23.29)
Book-to-market		-0.0282*** (3.78)
ROA		0.0138 (0.61)
Stock return		-0.0281** (2.46)
Earnings volatility		-0.0081 (0.41)
Loss		-0.1779*** (11.82)
Class action litigation risk		-0.1792*** (8.27)
N	16,271	16,271
R^2	0.0001	0.2439

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