Custom Proxy Voting Advice
2025 Midwest Finance Association (MFA)

Kunal Sachdeva

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The Big Picture

Shareholder Voting Can Be Overwhelming for Investors

- **Shareholder Meetings**
  - → Companies need shareholder approvals (e.g., elect directors, set executive pay, and so on).
  - → Voting typically happens by proxy, few people want to travel just to raise a hand in a half-empty hotel ballroom.

- **The Overwhelming Volume Problem**
  - → Institutions own many stocks.
  - → Each company sends a bulky "please vote on these 18 proposals" document every year.
  - → Multiply by thousands of companies. An overworked analyst probably needs some help!

- **Enter the Proxy Advisors**
  - → Firms like ISS and Glass Lewis read those documents and issue a "thumbs-up or thumbs-down."
  - → Huge timesaver for investors, but proxy advisors also wield substantial influence.

Can a "one-size-fits-all" proxy advice solve the problem? Probably not...

A Shift Toward Custom Proxy Advice

Proxy Advisors Offer Customizations

GLASS LEWIS

Custom Policies to Advance Your Stewardship Goals

Vote according to your outlook and approach to governance matters with a Custom Policy.

Request More Information
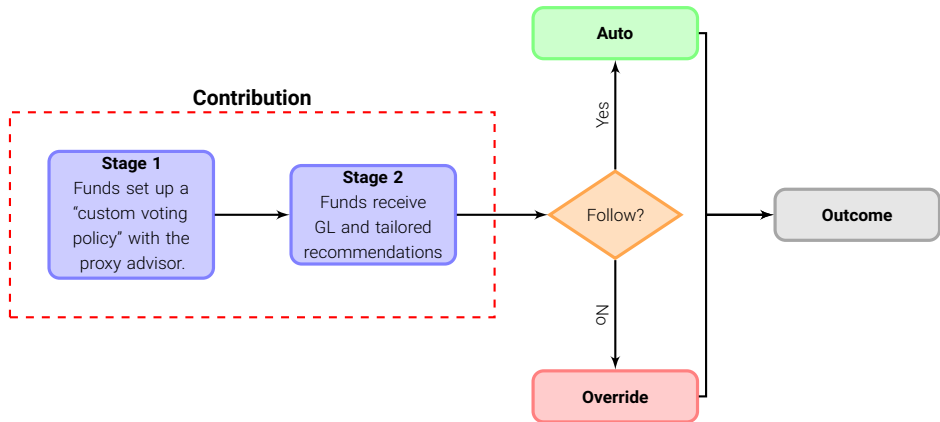
Institutional investors often need to tailor voting

Meeting Date: 11/08/2023

Management

#	ISSUE	BOARD	GL	Wayne Enterprise Policy	
				POLICY	**POLICY RATIONALE**
1.01	Elect Richard E. Belluzzo	FOR	FOR	AGAINST	The nominee serves on Nominating Committee and board gender diversity is less than thirty percent. The company's pay-for-performance is out of line.
1.02	Elect Keith L. Barnes	FOR	FOR	AGAINST	The nominee serves on Nominating Committee and board gender diversity is less than thirty percent. The company's pay-for-performance is out of line.
1.03	Elect Laura Black	FOR	FOR	AGAINST	The nominee serves on Nominating Committee and board gender diversity is less than thirty percent.
1.04	Elect Tor R. Braham	FOR	FOR	FOR	
1.05	Elect Donald A. Colvin	FOR	FOR	FOR	
1.06	Elect Douglas Gilstrap	FOR	FOR	AGAINST	The company's pay-for-performance is out of line.
1.07	Elect Masood A. Jabbar	FOR	FOR	FOR	
1.08	Elect Oleg Khaykin	FOR	FOR	FOR	
1.09	Elect Joanne Solomon	FOR	FOR	FOR	
2.00	Ratification of Auditor	FOR	FOR	FOR	
3.00	Advisory Vote on Executive Compensation	FOR	FOR	AGAINST	The company's pay-for-performance is out of line.
4.00	Frequency of Advisory Vote on Executive Compensation	1 YEAR	1 YEAR	1 YEAR	
5.00	Amendment to the 2003 Equity Incentive Plan	FOR	FOR	FOR	
6.00	Employee Stock Purchase Plan	FOR	FOR	FOR	

Two-Stage Decision Model

Institutions + Advisors Collaborate

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Institutions + Advisors Collaborate

- **Stage 1: Policy Customization**

  - $\rightarrow$ Funds invest time/resources to set up a "custom voting policy" with the proxy advisor.
  - $\rightarrow$ Once established, that policy generates *custom recommendations* for **all** firms in the fund's portfolio.

  ***Predictive of a substitution effect on attention.

- **Stage 2: Potential Overrides**

  - $\rightarrow$ When actual proposals come out, the fund decides whether to:
    1. Follow the custom recommendation (auto-submit), or
    2. Conduct additional research and possibly override the recommendation (manual vote).
  - $\rightarrow$ Setup allows fund to *pre-align* votes with their ideology, freeing them up to concentrate on contentious proposals.

  ***Predictive of a complementary effect on attention.

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>> *How can the paper tease these predictions out? What do they find?*

Summary of the Paper

How Do Institutional Investors Arrive at Their Voting Decisions?

- **Traditional Focus: Benchmark Recommendations**
  - → Academic and policy debates tend to focus on standard ("benchmark") proxy advice.
  - → But the paper shows that **80% of funds actually receive custom recommendations**.

- **Magnitude of Deviations**
  - → The paper finds that **over 20% of ballots** for customizers differ from the benchmark.
  - → This is a big shift from the idea that everyone follows a single ISS/GL "thumbs up/down."
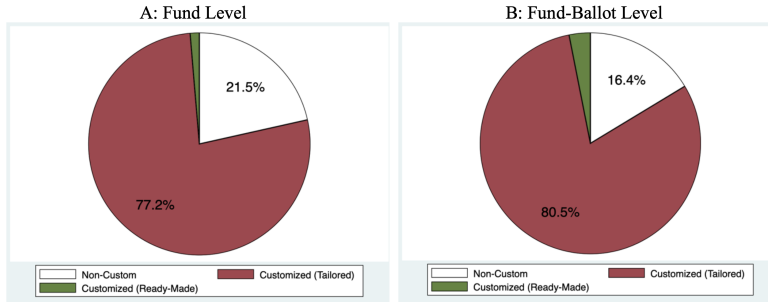
- **Two core roles of customization:**
  1. Facilitates *preference aggregation* (helps funds express ideological stances on issues like ESG).
  2. Improves *attention allocation* (frees up resources by reducing the need to scrutinize every proposal and focuses research on the most crucial votes).

Clever use of great data! Updated my understanding of proxy voting advice

Comment 1

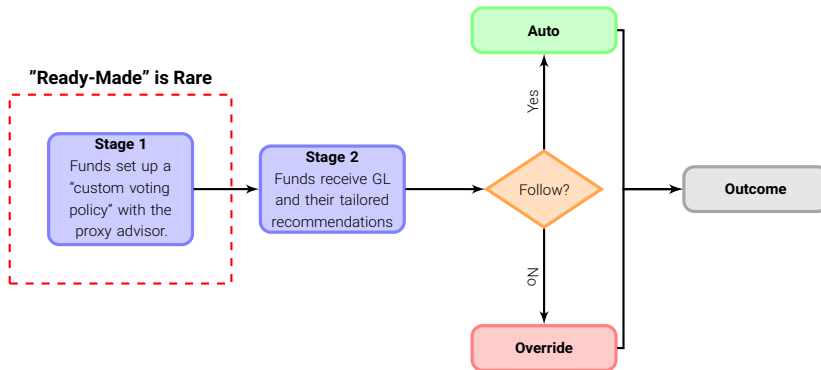*What more can we learn from Ready-Made Solutions?*

Frequency of customization – roughly 1% uses "Ready-Made" solutions

The low frequency of "Ready-Made" solutions has testable implications

Comment 1

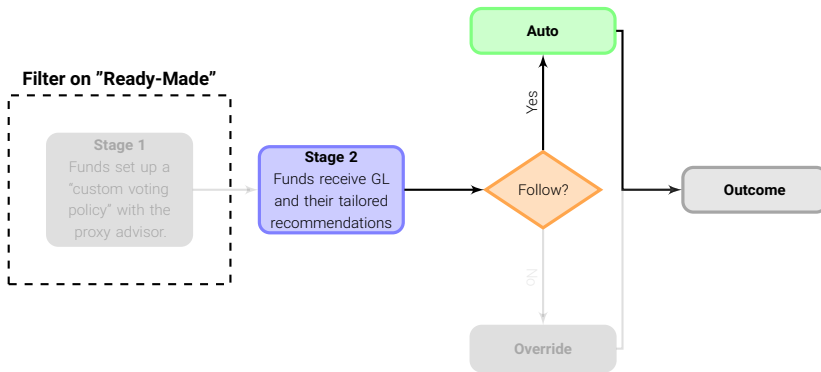*What more can we learn from Ready-Made Solutions?*

This likely suggests:

- "Ready-made" is not much better than the benchmark, once accounting for the costs.
- We also know costs for "ready-made" are lower than tailored solutions.

Comment 1

What more can we learn from Ready-Made Solutions?

May be able to back out degree of customization

Filter on "Ready-Made"

Stage 1
Funds set up a "custom voting policy" with the proxy advisor.

Stage 2
Funds receive GL and their tailored recommendations

Follow?

Yes

No

Auto

Override

Outcome

*Subject to terms of use of data.

Comment 1

What more can we learn from Ready-Made Solutions?

Use the Ready-Made Solution To Better Understand Tailored Solutions

Suggestion 1: Develop a lower bound, relative to benchmark

- Within ready-made, look at those that auto-submit their proxy. Then use voting outcomes at the fund level to back out

- This can be compared to the Glass-Lewis benchmark for the same ballot. Compute aggregate measure

*** Any level of customization would deepen how we understand custom proxy advice.

Suggestion 2: "Ready-Made" provides an auxiliary tests

- Substitution effect should be smaller for these funds – should see more manual voting

- Complementarity effect should be smaller too – should see more

*** Finding counterfactual evidence is fine, may suggest selection, justify dropping observations.

What are the return predictions for custom proxy advice?

- **Model Setup Example:**

$$\text{Value if proposal passes} = (X + \beta Y) \cdot s,$$

$$X \in \{-1, 1\} \quad \text{(common value/economic dimension)},$$

$$Y \in \{0, 1\} \quad \text{(ideological dimension, e.g. ESG indicator)},$$

$$\beta > 0 \quad \text{(fund's weight on ideology)}.$$
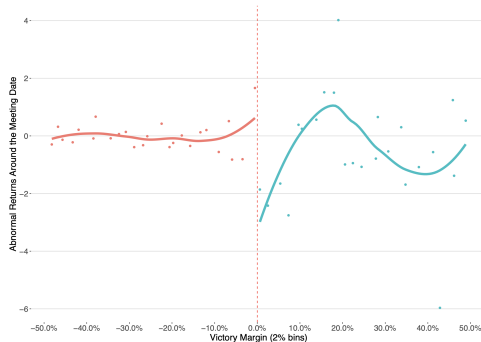
- **Interpretation:**

  $\rightarrow$ If $Y = 1$ (ideological component) but $X = -1$ (negative economic effect), a high-β fund may still vote "yes,"

  $\rightarrow$ **Economic trade-off:** In the short run, this might lower returns if the negative-X signal dominates. Over time, however, some investors may derive non-pecuniary benefits or expect long-term gains from ESG.

  $\rightarrow$ **Policy concern:** Do these votes align with fiduciary duties or broader regulatory goals? Regulators may worry that *consistent short-run underperformance* could conflict with shareholder interests

Comment 2

Testable Implications of the Model

- **Consider Strong ESG Preference**
  - $\rightarrow$ If β is large, the fund backs ESG proposals even when $X = -1$ (immediate net cost).
  - $\rightarrow$ Outcome: Potential short-run underperformance in exchange for meeting ideological goals.
  - $\rightarrow$ Data might show negative abnormal returns around such "ideology-heavy" votes.

Li, Naaraayanan, Sachdeva (2023)

Comment 2

Testable Implications of the Model

Complementarity Effect – Evidence of manual voting on contentious proposals

Dep. Variable: Manual Submission	(1)	(2)	(3)
Custom	6.90***		
	(1.78)		
ISS Opposes Mgmt x Custom	5.67***	2.21***	1.99***
	(0.83)	(0.45)	(0.46)
GL Opposes Mgmt x Custom	7.54***	5.68***	4.48***
	(0.76)	(0.49)	(0.54)
Special Meeting x Custom	11.07***	10.20***	10.97***
	(1.79)	(1.34)	(1.34)
Activist Connected to Meeting x Custom	12.64***	6.90***	3.41***
	(1.63)	(0.94)	(0.85)
Intercept	23.05***	31.41***	31.53***
	(1.28)	(0.27)	(0.29)
Mean dep. variable	35.67	35.66	34.92
N	4,554,262	4,548,139	3,433,767
R^2	0.17	0.68	0.81
Fixed Effects	Meeting	Meeting and Fund-Year	Meeting, Fund-Year, and Fund-Firm

Comment 2

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>> *Does this increased attention benefit investors?*

Comment 2

Testable Implications of the Model

Evidence about the potential effects on shareholders will deepen the contribution

- **Suggestion 1: Passive vs. Active Funds**

  $\rightarrow$ Hypothesis: *Active* funds may override (custom) advice if they detect large negative X signals; *passive* funds may be more likely to follow pre-set ideological policies.

  $\rightarrow$ Compare abnormal returns and voting outcomes on contested proposals across these fund types.

  *** Contributes to our understanding of how funds use voting to affect returns.

- **Suggestion 2: Manual vs. Automatic Voting**

  $\rightarrow$ Identify proposals where funds manually submit their proxy vs. automatic, who are less likely to deviate.

  $\rightarrow$ Compare short-window returns to measure if manual overriding advice leads to systematically different (potentially lower) returns.

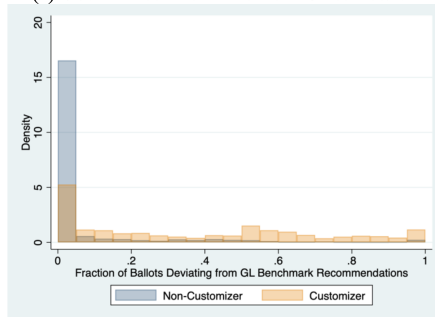 *** Offers insight on whether deviations are related to shareholder returns.

Comment 3

Optimal Deviations from Customizers?

Despite Customizing, They Are Deviating More

Part of this is selection, but can we think about how this fits into a rational inattention story?

(a) Overall Deviation Rate from Glass Lewis

Comment 3

Optimal Deviations from Customizers?

Can the paper provide more evidence of rational inattention by funds?

- **Suggestion 1: Busy-Season or Regulatory Shocks**
  - $\rightarrow$ Attention is costlier during the peak proxy season or after new SEC rules on proxy-advisor obligations.
  - $\rightarrow$ Funds under heavier workload will have (i) fewer total deviations but (ii) more pronounced deviations on the most contentious items—indicating they are allocating scarce research resources optimally.

  *** Evidence would support inattention story, suggest proposals may be overlooked when funds are stretched thin.

- **Suggestion 2: Within-Family Variation/Switching (Unsure if possible with data)**
  - $\rightarrow$ Some families use both custom and non-custom recommendations (or switch policies over time).
  - $\rightarrow$ Examine whether switching to a custom policy reduces "unnecessary" deviations while still preserving (or even increasing) deviations for the most significant votes—evidence of an optimal trade-off.

  *** This would be the most direct test of rational inattention.

Excited for This Paper!
It Updates Our Perspective on Proxy Advice

Important contribution on how we think about proxy advice and the allocation of attention to proposals

- Clever use of great data, carefully executed

- Two-stage framework, updates how we think about proxy advice, expect to receive many citations!

- Speaks to ongoing debates about the role of proxy advisors, customization, and regulation