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Behind the Scenes: The Corporate Governance Preferences of Institutional Investors

Institutional investors are a dominant force in financial markets today, yet their preferences about corporate governance are generally undisclosed and their activities in this area tend to be performed behind the scenes. We conduct a survey to elicit institutional investors' views on investor protection and corporate governance. We find that among the institutions that respond to our survey, corporate governance is important to their investment decisions and the majority are willing to engage in shareholder activism. When we examine institutional investors' portfolio holdings, we find that their investment decisions appear to be related to their revealed preferences.

Institutional investors influence financial markets worldwide through their predominance as buyers, holders, and sellers of corporate securities. According to the Conference Board (2010), as of December 2009 institutional investors held equities worth more than USD 10 trillion. Further, as of September 2008 institutional investors held over 78% of the corporate equities in the United States.[1] Because of the size of their shareholdings in firms, they affect the way corporations do business as well as corporations' governance structure. Understanding institutional investor preferences regarding corporate governance is thus important for firms trying to attract new investors as well as policy makers considering the regulation of different governance mechanisms.

Prior research frequently attempts to discern the preferences of institutional investors based on inferences of corporate attributes deemed important to institutional investors. For example, previous studies examine market reactions to governance changes, proxy voting, and monitoring by institutional investors.[2] The evidence suggests that institutional investors are less likely to invest in firms with poor corporate governance (see Giannetti and Simonov, 2006 and Leuz, Lins, and Warnock, 2009). These inferences, however, are typically based on indirect evidence[3] as institutional investors' governance-related preferences and actions tend to be private or conducted behind the scenes and thus difficult to observe and measure.[4]

In this paper we take a more direct approach by conducting a survey of a broad base of institutional investors from multiple countries that is designed to elicit these investors' governance-related preferences and activities.[5] We then connect the survey responses to data on investors' portfolio holdings to examine the relationship between their preferences and their investment decisions.

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[1] See the Federal Reserve Flow of Funds database.

[2] See, for example, Pound (1988), Brickley, Lease, and Smith (1988), Agarwal and Mandelker (1992), Gillan and Starks (2000, 2007), Hartzell and Starks (2003), Gaspar, Massa, and Matos (2005), Chen, Harford, and Li (2007), Thomas and Cotter (2007), Renneboog and Szilagyi (2010), and Bushee, Carter, and Gerakos (2010).

[3] Two exceptions are Carleton, Nelson, and Weisbach (1998), who provide evidence on the activities of TIAA-CREF in private negotiations of shareholder activism, and Becht, Franks, Mayer, and Rossi (2009), who provide evidence on the private shareholder activism of the Hermes UK Focus Fund. Further, we are aware of one academic survey on institutional investors and corporate governance, but this paper is rather limited in scope (Useem, Bowman, Myatt, and Irvine, 1993).

[4] As an example of behind-the-scenes governance activities, in the late 1980's, when CalPERS was dissatisfied with the governance of Texaco, they negotiated with Texaco's management to appoint a pro-shareholder candidate to its board of directors (Gillan and Starks, 2007).

[5] Recent surveys in the finance literature include Graham and Harvey (2001), Brav, Graham, Harvey, and Michaely (2005, 2008), Graham, Harvey, and Rajgopal (2005), Ben-David, Graham, and Harvey (2007), Geczy, Minton, and Schrand (2007), Brav, Graham, Harvey, and Michaely (2008), and Jenkinson and Jones (2009).

The survey questions focus on both country-level and firm-level aspects of corporate governance. Specifically, we ask investors for their assessments of a country's investor protection, their preferences with respect to firm-level governance mechanisms, and their willingness to engage in shareholder activism. To be able to conduct an in-depth analysis without making the survey too long and complex for investors to complete, we limit the survey's focus to investments in firms in two countries, namely, the United States and The Netherlands. We choose these two countries because, while they both have well-developed stock markets with considerable institutional investor interest, they have different legal origins, investor protection regimes, and ownership characteristics. In particular, the United States is an English common law country that is generally considered to have high investor protection, low ownership concentration, and high institutional ownership, whereas The Netherlands is a French civil law country that is viewed as having low investor protection, high ownership concentration, and low institutional ownership.[6] The differences in investor protection between these countries allow us the unique opportunity to link variation in investor perceptions (through their survey responses) with actual investment decisions and preferences for firm-level governance mechanisms. Given the survey's country focus, we sent the survey to a group of global institutional investors with investments in both the United States and The Netherlands. We received 118 responses, from which we were able to match 90 to additional information about the investor (e.g., portfolio holdings).

We find that the survey respondents have distinct assessments of the level of investor protection in the United States and The Netherlands, with a significant gap between the two countries. The relative difference in assessments is consistent with the difference suggested by the anti-director index of La Porta, Lopez-de-Silanes, Shleifer, and Vishny (LLSV, 1998) and the anti-self dealing index of Djankov, La Porta, Lopez-de-Silanes, and Shleifer (DLLS, 2008).

This result leads to two implications. The first is that the investor protection gap between the U.S. and The Netherlands should be related to an institutional investor's portfolio holdings to the extent that the investor regards this gap as important in their investment decisions. We examine this conjecture by comparing institutional investors' portfolios to their survey responses. The results support the view that characteristics of the firms held in an institutional investor's portfolio are related to how concerned investors are about the investor protection gap between the

[6] See La Porta, Lopez-de-Silanes, Shleifer, and Vishny (1998), Djankov, La Porta, Lopez-de-Silanes, and Shleifer (2008), La Porta, Lopez-de-Silanes, and Shleifer (2006), and Ferreira and Matos (2008).

United States and The Netherlands. We thus find that investor protection concerns affect institutional investors' portfolio holdings. In particular, our evidence suggests that investors which are more concerned about the investor protection gap prefer to invest in firms which are arguably less exposed to agency problems between shareholders and managers, as indicated by higher leverage, lower cash holdings, fewer M&A transactions, and reduced information asymmetries.

The second implication following from the assessments of an investor protection gap is that some firm-level corporate governance mechanisms may be more important in institutional investors' investment decisions than others. Theory suggests that corporate governance mechanisms should be value-increasing. However, the empirical testing has led to a debate regarding the value of corporate governance mechanisms to shareholders (e.g., Gompers, Ishii, and Metrick, 2003; Cremers and Nair, 2005; Core, Guay, and Rusticus, 2006; Bebchuk, Cohen, and Farrell, 2009). By directly asking institutional investors which mechanisms they consider important, we are able to shed light on this debate. We find that institutional investors consider most firm-level corporate governance mechanisms studied in the previous literature at least somewhat important, with the most important being equity ownership of management, equity-based compensation, board independence, transparency about the holdings of large shareholders, and high free float.[7] The responses to the survey questions suggest that institutional investors focus on issues related to reducing agency conflicts between managers and shareholders (e.g., equity-based pay) as well as between large and small shareholders (e.g., transparency about the holdings of large shareholders). We further find that institutional investors' preferences for different governance mechanisms vary across investor type. The issue of greatest importance to the hedge funds in our sample is equity ownership by managers, while insurance firms are most interested in high free float; mutual funds find both equity ownership by managers and transparency about the holdings of large shareholders to be most important, while pension funds are most concerned about ownership concentration, board independence, and high free float.

We next examine whether institutional investors consider investor protection and firm-level corporate governance mechanisms to be substitutes or complements. A number of studies

[7] A high free float allows firms to liquidate shares easily, allows prices to more accurately reflect managerial effort and thereby increase the efficiency of stock-based compensation (Holmstrom and Tirole, 1993 and Edmans, 2009), and suggests lower holdings of large shareholders and therefore lower agency problems between large and small shareholders.

provide evidence on the relation between these mechanisms as well as on the complementarity versus substitutability of these mechanisms and investor protection (e.g., Coffee, 2002; Reese and Weisbach, 2002; Doidge, Karolyi, and Stulz 2004, 2007; Cremers and Nairs, 2005; Durnev and Kim, 2005; Giroud and Mueller, 2010; Aggarwal, Erel, Stulz, and Williamson, 2009). By incorporating firm-level differences in governance mechanisms into our examination of country-level differences in investor protection (Bebchuk and Weisbach, 2010), our evidence adds to this literature by suggesting that the internal corporate governance mechanisms that we examine are perceived to be substitutes for the external investor protection mechanism. Specifically, we find that investors with more negative views on country-level investor protection rely on a subset of firm-level governance mechanisms to mitigate agency problems that put returns on their invested capital at risk. This subset includes incentive mechanisms (e.g., executive compensation and ownership), board independence, and mechanisms that allow the market for corporate control to operate unimpeded by anti-takeover provisions.

Our survey-based analysis also allows us to address the debate on the superiority of a one-tier or two-tier board system.[8] In the one-tier board system a firm has one board of directors consisting of executive and non-executive directors (as in the United States). In the two-tier board system a firm has two separate boards, namely, a management board, which is responsible for the day-to-day management of the firm, and a supervisory board, which monitors the management board (as in Germany). Because Dutch firms have a choice between the two board structures, The Netherlands provides a unique set-up to ask institutional investors about their board system preferences. We find that institutional investors are split in their views, with the preference for the two-tier system (52%) more than twice as large as that for the one-tier system (21%). Below we show that this result is consistent with the predictions of the Adams and Ferreira (2007) model, which suggests that the two-tier system is optimal when managerial control benefits are higher. Our findings are also consistent with the argument in Graziano and Luponini (2005) that the two-tier system can be preferable in markets with more concentrated ownership, as is the case in The Netherlands.

In our last set of analyses, we address the question of institutional investors' willingness to engage in different types of shareholder activism. Harris and Raviv (2010) argue that in the presence of managerial agency problems, shareholders should have control over corporate

[8] See, for example, O'Hare (2003) for details on this debate.

decisions, that is, should use their "voice", when they do not have private information. Other theoretical studies also argue for the intervention of large shareholders (e.g., Shleifer and Vishny, 1986; Maug, 1998; Kahn and Winton, 1998; Bolton and von Thadden, 1998; Faure-Grimaud and Gromb, 2004). More recent theoretical studies point out, however, that activism through "exit", that is, by selling their shares, can be more effective than activism through voice (e.g., Admati and Pfleiderer, 2008; Edmans 2009; Edmans and Manso, 2010). In our survey, we ask institutional investors how they view engaging in these alternative types of activism. The responses indicate that institutional investors are willing to pursue various types of shareholder activism, with the most prevalent being exit (80% of the investors are willing to use it). This finding is consistent with the theoretical models of Admati and Pfleiderer (2008), Edmans (2009), and Edmans and Manso (2010). However, we also find that, consistent with theory, institutional investors frequently use their voice if they are dissatisfied. For example, more than 50% of the respondents are highly willing to vote against management at the annual meeting and to engage management in discussions. Other activities such as making speeches or proposals at the annual meeting, contacting the firm's supervisory board, making public criticism, or taking legal measures generally receive much less support from institutional investors, although some types of institutions (e.g., hedge funds) are more willing to engage in these additional measures. Importantly, we do not find that the willingness to engage in shareholder activism is related to the investment horizon (measured using share turnover) of the investors' portfolios. Thus, activism in our sample is not solely the focus of long-term or short-term investors. However, we do find that the most important trigger for shareholder activism is not dissatisfaction with a company's stock price performance but rather with its (long-run) corporate strategy, and we find some evidence that the willingness of an investor to engage in activism is related to the characteristics of its portfolio firms. Finally, we find that of our respondents, 59% are willing to coordinate their actions; for the 41% that do not coordinate, over half state legal concerns as the primary reason for not coordinating. Prior researchers have argued that institutional investors could contribute more to corporate governance and firm monitoring by speaking up, particularly using one voice (e.g., Black, 1992). Our results provide preliminary evidence on the extent of coordination, and on why coordination is not higher given the claimed benefits.

In sum, our survey responses provide unique insights into the governance preferences of institutional investors and complement traditional large-sample empirical analyses and clinical studies. One caveat about our data is that those respondents who chose to answer our survey may be more likely to put greater emphasis on governance-related issues and may be more active in monitoring firms. However, even if this is the case, our results continue to be important as these investors arguably have the greatest effect on corporations' governance structures.

The remainder of the paper is organized as follows. In Section I we describe the survey design, delivery, and response. We also present summary statistics about the responding institutional investors, and we discuss the possibility of non-response bias and related concerns. In Section II, we examine survey responses with regard to country-level investor protection and firm-level corporate governance and the relation between the two. We also examine the relation between governance preferences and the characteristics of portfolio firms. In Section III, we examine attitudes toward shareholder activism and the possibility of coordinated actions. We also examine the relation between the willingness to engage in shareholder activism and portfolio characteristics. We conclude in Section VI.

I. Data and Methodology

A. Survey Design

We divide the survey into several sections, each having a specific goal.[9] The purpose of the first section is to gather background information on the responding institutions, such as type of institution, how proxy voting is conducted, and the proportion of the portfolio that is actively invested. The second section is designed to extract institutional investor preferences regarding corporate governance and investor protection issues. The third section focuses on their preferences regarding shareholder activism. The final section of the survey (for the purpose of this paper) features questions designed to elicit information regarding the institutions' voting behavior and their decision making around the firm's annual meeting.[10,11]

The survey questions were developed based on existing corporate governance literature. Before conducting the survey, we circulated it among academics and investor relations research experts to get their feedback and suggestions on the survey design and execution. We then

[9] A copy of the survey is provided in Appendix A-1.

[10] The survey also included an additional section that provides for a deeper analysis of investors' opinions about executive compensation. These questions and their responses are not covered in this paper.

[11] The firm's annual meeting for shareholders is typically termed "annual shareholders meeting" in the United States and "annual general meeting" or AGM in The Netherlands. We will simply call it the "annual meeting" in this paper.

conducted beta tests by having graduate students and some institutional investors fill out the survey.

B. Delivery and Response

In order to reach a large number of institutional investors with international equity holdings, we selected our survey recipients from the FactSet/LionShares database, which is considered a leading data source for characteristics and equity portfolio holdings of institutional investors worldwide. FactSet/LionShares defines institutional investors as professional money managers with discretionary control over assets.[12] Because we ask our survey respondents to make comparisons between investor protection in the United States and The Netherlands, we need to ensure that they have at least some knowledge of the Dutch financial market and the corporate regimes in that country. Consequently, we restrict the survey to those institutions in the database that have at least 5% of their assets under management invested in companies from The Netherlands (as of the end of 2006).

We sent the survey by email to the chief investment officers of a total of 1,178 institutional investors on November 1, 2007. Additional reminders were sent and individual phone calls made in the last weeks of December 2007 to maximize the response rate. The last responses were received in the first weeks of January 2008. A total of 118 surveys were returned, giving us a response rate of about 10%. This response rate can be compared to response rates of 9% in Graham and Harvey (2001), 10% in Graham, Harvey, and Rajgopal (2005), 8% in Brav, Graham, Harvey, and Michaely (2005), and between 15% and 19% in Jenkinson and Jones (2009).[13] We are able to match the identity of the institutional investors and hence the survey responses with data on institutional investor characteristics from FactSet/LionShares for 90 of the 118 investors that returned the survey.

FactSet/LionShares also contains data on the portfolio holdings of the institutional investors, in particular, the identity of portfolio firms and the size of stakes in these firms. Thus, we are able to match an investor's survey responses with information on their portfolio companies by matching the holdings data with financial data on the portfolio companies from

[12] This database has also been recently employed by Ferreira and Matos (2008) and Li, Moshirian, Pham, and Zein (2006).
[13] The study by Brav, Graham, Harvey, and Michaely (2005) also included surveys distributed in person, which resulted in a much higher response rate.

DataStream/Worldscope. This gives us a combined data set consisting of almost 8,000 investor-portfolio firm observations.

C. Characteristics of Responding Institutional Investors

Table 1 presents summary statistics regarding the institutional investors that respond to our survey, as well as on the matched portfolio holdings data from FactSet/LionShares. Panel A shows that the average institutional respondent has equities worth $632 million under management, of which 10.4% are invested in firms listed in The Netherlands and 9.2% are invested in firms listed in the United States. On average, the responding institutions hold equity securities in 89 firms with an average value of $6.1 million and an average stake of 0.13% of the firms' shares outstanding. These investors show an average quarterly share turnover of 0.16, defined as the value of all buy and sell transactions divided by the market value of the equity portfolio. Below, we refer to investors with above-median assets under management as large investors; in particular, we define investors with above-median equity holdings in firms from the United States (The Netherlands) as investors with large US (NL) holdings. Similarly, if an investor has above-median share turnover, suggesting less rapid turnover, we consider the investor as having a long investment horizon.

Our sample contains survey responses from all important institutional investor types, with a heavy clustering of mutual funds. As Panel B of Table 1 shows, of the responses received, 5.9% were from hedge funds, 7.6% from insurance firms, 62.3% from mutual funds, and 5.9% from pension funds.[14] It should be noted that for mutual funds FactSet/LionShares lists portfolio holdings by fund, rather than aggregated across funds in the same mutual fund complex as is done in the 13f data. Consequently, we also sent the survey to individual funds. This is consistent with the fact that investment decisions, and often governance voting decisions, are made or at least influenced at the individual fund level rather than the complex level. Further, funds within a mutual fund family can have different governance preferences as shown by Morgan, Wolf, and Yang (2009). The maximum number of institutional investor respondents in our sample from the same complex or holding company is two, and we have seven such pairs. Even these cases,

[14] This categorization is based on self-reported information in the surveys. Many portfolio managers are from financial complexes that have multiple divisions. For example, an insurance company with an investment division. Thus, in the survey they were asked how their fund/institution could be best described in order to determine their own definition.

however, the questionnaires were sent to different investment vehicles and were filled out by different people.

Panel C reports investor characteristics by investor type and shows that while the sample pension funds have the largest equity holdings, the sample hedge funds are the most active in trading, exhibiting the highest share turnover. Our respondents were primarily based in Europe (86%), with the rest of the investors coming from North America (14%). The exact breakdown by investor origin can be found in Panel D. The national origin of the investors in this table is based on where investment management takes place, not the legal seat. Information on the legal seats is provided in Appendix A-2. Of the 24 investors whose legal seats are in Luxembourg, only 3 actually operate from there. The other investors are de facto located in the United Kingdom (5 investors), the United States (3 investors), The Netherlands (5 investors), Switzerland (3 investors), Belgium (1 investor), Germany (2 investors), France (1 investor), and Spain (1 investor). Similarly, from the two investors with a legal seat in the Cayman Islands, one actually operates from the UK.

One issue that could complicate the analysis is the possibility that institutional investors with largely passive holdings could be less concerned about corporate governance or shareholder activism (although it is also possible that as captive long-term holders, passive investors could be more concerned about these matters). To ensure that the institutional investors in our sample also conduct active investment decisions, we requested from each investor the percentage of equities actively invested. The median investor reports that 80% of its equities are bought as a result of a positive/active investment decision while the remaining 20% are the result of a passive investment strategy. Panel E also shows that, as expected, hedge funds manage the largest proportion of actively invested funds (94%) and pension funds manage the lowest (60%). This is further illustrated in Figure 1.

In the survey we also asked investors to what extent they make use of proxy voting advisors (e.g., ISS or Glass Lewis) for voting at an annual meeting. We included this question to examine to what extent investors delegate their proxy voting decisions and perhaps activist actions to external advisors. The data reported in Panel F of Table 1 suggests that over half of the institutions in our sample (53%) do not employ proxy voting advisory services at all. In fact, only 7% of the investors state that they always use proxy voting firms for determining their voting decisions. Of those investors that use proxy voting firms to some extent, most use the advice of these firms to determine their own position vis-à-vis the portfolio company of interest.[15]

D. Non-response Bias and Related Concerns

One concern in any survey research is the extent of bias caused by differences between participants who choose to respond to the survey and those who choose not to respond. In Appendix A-3 we evaluate, as suggested by Moore and Reichert (1983) and Graham and Harvey (2001), the level of non-response bias by examining characteristics of responding versus non-responding institutional investors. There are no significant differences in assets under management between the two groups. However, the respondents have significantly more assets invested in The Netherlands and fewer assets invested in the United States than do the non-respondents. Our sample also exhibits an overweighting of investors based in continental Europe (mainly from The Netherlands and Luxembourg), and an underweighting of investors from the U.K. and the U.S. However, almost all of our respondents managed portfolios containing significant positions in firms located outside Europe as well, including the U.S., U.K., and Asia. These differences are similar if we compare our respondents to all other institutional investors in the FactSet/LionShares database that did not participate in the survey. Note that our comparison of investor origin is based on the legal seat of the investor as only the legal (and not the actual) seat is available for the non-respondents.

In a survey of the opinions of economic agents such as this one, there is naturally also a risk that respondents answer in a strategic or untruthful fashion. To mitigate these concerns, we indicated that respondents' individual responses would be treated as confidential. Furthermore, phone conversations indicated that the respondents would not spend time to fill out our survey if they intended to answer untruthfully.

[15] Note that US regulation, for example, requires mutual funds to report how they determine their voting policies as well as what their individual voting decisions are (see the discussion in Cox and Thomas, 2005 and the SEC rule on Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, Exchange Act Release No. 33-8188 (Jan. 31, 2003)). In the mid 1980s, the US Department of Labor began to pressure corporate pension funds to conduct voting themselves rather than delegating that responsibility to their external managers, arguing that voting was part of their fiduciary duty. Similarly, public pension funds in The Netherlands were asked to commit to developing their own proxy voting policies and vote all their shares at annual meetings.

II. Investor Protection and Corporate Governance

A. Importance of Country-level Investor Protection

We first evaluate institutional investors' assessments of investor protection in the United States relative to The Netherlands. As mentioned previously, these two countries have very different legal and governance regimes. The U.S., an English common law country, has an anti-director index (see DLLS) score of 3, whereas The Netherlands, a French civil law country, has a score of 2.5 (the original scores based on LLSV were 5 for the U.S. and 2 for The Netherlands).[16] An alternate measure of shareholder rights is the anti-self-dealing index of DLLS, which is a combination measure reflecting countries' private and public controls of self-dealing.[17] Based on this measure the U.S. has a score of 0.65 and The Netherlands has a score of 0.20. Both measures thus suggest that the U.S. is associated with better investor protection. However, Spamann (2009) indicates that after correcting the LLSV numbers, The Netherlands has a higher score than does the United States.

These results raise two questions about institutional investors' assessments of investor protection. The first question is whether investors perceive differences in investor protection across countries to be important. The second is whether their beliefs are more in line with the results of LLSV (1998), DLLS (2008), and studies such as Reese and Weisbach (2002) and Doidge, Karolyi, and Stulz (2004), who provide evidence that French civil law countries such as The Netherlands have worse investor protection than English common law countries such as the United States, or whether their beliefs are more in line with those of the revised index of Spamann (2009). To address these questions, we examine whether institutional investors with equity holdings in both the United States and The Netherlands perceive differences in investor protection across countries. Rather than potentially confounding investors' perceptions by constructing a summary measure from their responses, we separately measure institutions' assessment of

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[16] The anti-director rights index aggregates six shareholder rights by adding 1 when: (1) the country allows shareholders to mail their proxy vote to the firm; (2) shareholders are not required to deposit their shares prior to the General Shareholders' Meeting; (3) cumulative voting or proportional representation of minorities in the board of directors is allowed; (4) an oppressed minorities mechanism is in place; (5) the minimum percentage of share capital that entitles a shareholder to call for an Extraordinary Shareholders' Meeting is less than or equal to 10 percent (the sample median); or (6) shareholders have preemptive rights that can only be waived by a shareholders' vote. The index can range from 0 to 6, but for developed countries the range is from 2 to 5 (see LLSV, 1998 and the update in DLLS, 2008).

[17] The anti-self-dealing index is based on a set of questions posed to law firms regarding private and public enforcement of anti-self-dealing.

investor protection across four dimensions: protection of minority shareholder rights; ease of shareholders to exercise their rights; whether the companies provide sufficient information for shareholder decisions; and whether appropriate legal measures exist to allow shareholders to influence firm strategy. For each of these questions, investors could indicate the extent to which they disagree or agree on a scale from 1 to 7 (with 1 meaning "strongly disagree" and 7 meaning "strongly agree") for each country.

The results are illustrated graphically in Figure 2 and reported in more detail in Table 2, with the responses regarding the United States in the left four columns and the responses regarding The Netherlands in the following four columns. The final column in the table contains the significance levels from a test for differences across countries in the mean responses. To facilitate comparison, the last two rows of the panel contain the measures for the United States and The Netherlands for the anti-directors index and anti-self-dealing index reported in DLLS (2008). Note that in order to conduct a valid comparison, the table only contains responses of those investors who answered the questions for both the United States and The Netherlands. For each of the investor protection characteristics, there is a significant difference in the mean responses between the United States and The Netherlands, with the score for the United States being higher. Thus, the institutional investors' assessments are broadly consistent with the indexes of investor protection constructed by LLSV and DLLS, and not with that of Spamann (2009). Further evidence consistent with these results is the result of a -8% governance gap between The Netherlands and the United States provided in the analysis of Agarwal, Erel, Stulz, and Williamson (2009).

Since we require that the institutional investors participating in our survey hold at least 5% of their equity holdings in Dutch companies, one might argue that the investors in our sample have a more positive view about investor protection in The Netherlands compared with investors that avoid the country entirely. To the extent that this is the case, the resulting bias should work against finding significant differences in investor protection between The Netherlands and the United States and thus our documented findings are likely to be understating actual perceived differences in the investor protection regimes. This might also explain why the medians in Table 2, as opposed to the means, are not different for two of the four variables.

In unreported analysis we also test whether Dutch institutional investors suffer from an apparent home bias by displaying significantly more positive views about The Netherlands as compared to foreign investors. According to all four measures of investor protection that we employ, we do not detect a significant difference between the views of Dutch investors versus foreign investors about The Netherlands. Similarly, the Dutch investors' views about investor protection in the United States do not differ significantly from those of foreign investors.

B. Investor Protection and Characteristics of Portfolio Firms

Thus far we have provided evidence that institutional investors have distinct views regarding investor protection in the United States and The Netherlands. In this section we examine whether a link exists between the investors' portfolio holdings and their investor protection assessments. Following LLSV (1998) and DLLS (2008), we take the views on investor protection in the United States as proxies for an investor's assessment of investor protection in English common law countries (i.e., generally high investor protection), while we take views on The Netherlands as proxies for assessments of investor protection in French civil law countries (i.e., with generally weaker protection). LLSV (1998) and DLLS (2008) document that English common law countries and French civil law countries are polar legal families when it comes to investor protection, and that the countries within these families are relatively homogenous with respect to their individual levels of protection.[18] Further evidence regarding the differences across civil law and common law countries comes from Reese and Weisbach (2002), who find that firms from French civil law countries are more likely to cross-list on a U.S. exchange than firms from English common law countries, suggesting that greater value exists in the cross-listing for firms from the former.

To examine the relations between institutional investors' portfolio holding characteristics and their views on each of our investor protection variables, we match data on investors' portfolio holdings obtained from FactSet/LionShares with data on the portfolio firms obtained from DataStream/Worldscope. We then construct firm characteristic measures that capture a firm's financial policies and performance using the approach and definitions of Cronqvist and Fahlenbrach (2009), and we construct a variable that captures the ownership structure of the firm.

Next, for each firm characteristic, we run the following regression:

[18] On the one end of the spectrum (high protection), the average English legal origin country has an average value of 4.19 for the (revised) anti-directors index and an average value of .66 for the anti-self-dealing index. On the other end of the spectrum, the average French legal origin country has an average value of only 2.91 for the anti-directors index and of only .33 for the anti-self-dealing index.

$$Firm\ Characteristic_{ci} = Investor\ Protection\ Gap_i + \boldsymbol{X}_c + \boldsymbol{y}_i + \varepsilon_{ci}, \quad (1)$$

where the dependent variable *Firm Characteristic*$_{ci}$ is the Tobin's Q, Leverage, Cash Holdings, Closely held Shares, Investment, or M&A Expenditures of company c held by institutional investor i. We run each of these regressions *separately* for investors' portfolio firms from English common law countries and French civil law countries.[19]

We define *Investor Protection Gap*$_i$ as investor i's assessment of investor protection in the United States minus her assessment of investor protection in The Netherlands. Recall that investors could answer on a scale from 1 (strongly disagree) to 7 (strongly agree) on four aspects of investor protection in the U.S. and The Netherlands. The gap variable thus allows us to measure in relative terms how concerned investors are about differences in investor protection between the United States (i.e., English legal origin countries) and The Netherlands (i.e., French legal origin countries) and the extent to which this concern is related to characteristics of their portfolio firms. If investors do not believe that some firm-level characteristic should be affected by investor protection considerations, then we should find no relation between investors' perceived investor protection gap and that firm characteristic.

Turning to the firm characteristics used in equation (1), we calculate Tobin's Q as the market value of a firm divided by the book value of a firm, leverage as total debt over total assets, cash holdings as the value of cash holdings over assets, investment as capital expenditures over lagged total assets, and M&A expenditures as the value of assets newly acquired over lagged total assets, and cash flow as EBIT over lagged total assets. Our ownership measure, closely held shares (CH shares), is the fraction of all shares that are held by insiders (including those held by directors, officers, or immediate family members).[20]

$\boldsymbol{X}_c$ is a vector of firm-specific control variables, which includes log assets as a control for firm size plus some firm level control variables. All regressions contain a vector of investor-specific controls, $\boldsymbol{y}_i$, which includes the logarithm of assets under management and share turnover. The regressions are estimated using firm data from year-end 2007 (as well as data lagged from

[19] We did not have enough investor-portfolio firm observations to limit the regressions to firms from the United States and The Netherlands. For each firm characteristic regression, we include only one investor protection variable to avoid potential multicollinearity problems.

[20] The corresponding variables are reported in Appendix A-4.

that date). All regressions are estimated with industry dummies and heteroskedasticity-robust standard errors clustered by institutional investor.

The regression results are provided in Table 3. To conserve space, the table reports for each firm characteristic the coefficients from four regressions (one for each investor protection assessment measure). The table also indicates which of the firm and investor controls are included in each regression. The results suggest that characteristics of the firms held in an institutional investor's portfolio are related to how concerned the investor is about the investor protection gap between the United States and The Netherlands. More specifically, the results show that investors who are very concerned about differences in investor protection invest in companies with lower Tobin's Q, higher leverage, lower cash holdings, and lower M&A expenditures. This finding suggests that investor concerns regarding country-level investor protection affect their portfolio holdings. In particular, it suggests that investors which are more concerned about investor protection prefer to invest in firms which are arguably less exposed to agency problems between shareholders and managers due to higher leverage (which disciplines management), lower cash holdings (which reduces free cash flow problems), and fewer M&A transactions (which reduces the risk of inefficient empire building). To the extent that Tobin's Q proxies for information asymmetries between shareholders and managers, investors that are very concerned about investor protection also prefer to invest in firms that are easier to monitor.

C. Importance of Firm-level Corporate Governance Mechanisms in the Presence of Weaker Investor Protection

Given the relatively weaker level of investor protection perceived to exist in The Netherlands, according to both the survey responses and the DLLS (2007) indices, we next restrict our attention to this country and examine the perceived importance of different firm-level corporate governance mechanisms and whether these assessments are affected by the co-existing investor protection regimes.

While the costs and benefits of different governance mechanisms have been addressed extensively in the theoretical literature (see reviews by Shleifer and Vishny, 1997; Becht, Bolton, and Roell, 2003), models analyzing the relative importance of different governance mechanisms are rare. One exception is Burkart, Panunzi, and Shleifer (2003), who provide a formal model of governance mechanisms addressing both the agency conflict between shareholders and managers and the agency conflict between large and small shareholders. Similarly, work by Boot, Gopalan, and Thakor (2006) implies that certain corporate governance mechanisms can actually exacerbate agency problems by constraining management from actions that could increase shareholder wealth.

Through our survey instrument, we ask institutional investors how important different firm-level governance mechanisms are when making an investment decision in The Netherlands. We divide the firm-level governance mechanisms into the following categories: issues related to anti-takeover devices, issues related to the supervisory board and independence of director committees, issues related to executive compensation, voting issues, and ownership and capital structure issues. For each mechanism or control device, investors could assign a score using a scale from 1 to 7, where 1 indicates very important and 7 indicates not important at all.

Table 4 reports the percentage responses along with the means, medians, standard deviations, and number of responses. The last column of the table shows the percentage of responses that considered an issue to be at least somewhat important. Figure 3 presents a graphical representation of the mean responses. As the table shows, institutional investors consider a number of governance mechanisms to be important in making their investment decisions. Most are regarded as at least somewhat important, with the highest percentages for equity ownership of management (87%), use of equity-based compensation (86%), supervisory board independence (86%), transparency about the holdings of large shareholders (85%), and high free float (85%). The perceived importance of these governance mechanisms is consistent with those that receive the most attention from shareholder proxy proposals in the United States – Gillan and Starks (2007) find that over the 2001-2005 period, the mechanisms most likely to be submitted as proxy proposals were related to executive compensation or the board of directors. Table 4 also shows that few of the governance mechanisms are considered less important, unimportant, or not important at all; only a few control devices are viewed as at least somewhat important by less than 50% of the respondents: small supervisory board size (49%), limitation on director terms (50%), confidential voting (49%), and share certificates (44%).[21]

[21] Share certificates are often observed in The Netherlands. They arise when a company issues shares to a foundation, which in return issues share certificates that do not have voting rights. Investors can then buy these certificates from the foundation but not the shares directly, leaving the control rights associated with the shares at the foundation. The foundation thus effectively controls the company and is often made up of manager-friendly directors.

The institutional investors' responses to the survey questions suggest that they are interested in reducing agency conflicts between managers and shareholders as well as between large and small shareholders. Specifically, while the investors indicate the greatest interest in executive compensation incentive devices that reduce agency conflicts between management and shareholders through executives' stock ownership and options, they also indicate strong interest in mechanisms that reduce agency conflicts between large and small shareholders through generally dispersed ownership structures, transparency regarding large blockholdings, and the presence of independent directors on the board.[22]

Previous studies fail to find direct evidence that investors value board independence. Indirect evidence, however, suggests that board independence is important, as extant research documents that independent directors are more likely to replace a poorly performing CEO, the likelihood of hiring a replacement CEO from outside the firm increases with the percentage of independent directors, and shareholders react more positively to decisions made by boards dominated by independent directors.[23] Further, evidence suggests that having more independent directors reduces the likelihood of earnings management or financial fraud and increases the likelihood of accounting conservatism.[24] Our survey evidence provides direct evidence on the value that investors place on board independence. We find that a high percentage of respondents (86%) think that board independence is at least somewhat important or of great importance. This result supports the indirect evidence in prior literature. This result is also consistent with Bruno and Claessens (2007), who find that the two most important governance mechanisms across countries are independence of the board and independence of the board committees, and with Aggarwal, Erel, Stulz, and Williamson (2009) and Dahya, Dimitrov, and McConnell (2008), who show that board independence is particularly important in countries with weak investor protection.

Turning to the effect of board size, Jensen (1986) and Yermack (1996) argue that smaller boards are more efficient as they are associated with fewer coordination and communication

[22] The Dutch corporate governance system employs a system of co-optation that allows large blockholders and management-friendly shareholders to control the supervisory board by excluding independent board directors. In such cases small shareholders effectively have no influence on the election or removal of individual supervisory board members (see De Jong and Roell, 2005).

[23] See Weisbach (1988), Brickley, Coles, and Terry (1994), and Borokhovich, Parrino, and Trapani (1996). See also Hermalin and Weisbach (2003), Adams, Hermalin, and Weisbach (2010), and Becht, Bolton, and Roell (2003) for surveys of studies on board independence.

[24] See, for example, Beasley (1996), Dechow, Sloan, and Sweeney (1996), Klein (2002), and Beekes, Pope, and Young (2004).

problems. In contrast, Adams, Hermalin, and Weisbach (2010) argue that the Hermalin and Weisbach (1998) model of boards implies that firms with larger boards are likely to outperform those with smaller boards. The empirical evidence is mixed. While Yermack (1996) finds that firm performance (Tobin's Q) is negatively related to board size, Coles, Daniel, and Naveen (2008) find that firm performance is increasing in board size when one controls for the type of firm. Our results provide evidence on institutional investors' perceptions of this debate. In particular, we find that the majority of survey respondents do not view a small board as at least somewhat important in their investment decisions.

Bebchuk, Cohen, and Farrell (2009) examine which of the 24 governance provisions in the Gompers, Ishii, and Metrick (2003) framework are the most important and form an entrenchment index using six governance provisions. They find that poison pills, golden parachutes, staggered boards, limits to shareholder by-law amendments, and supermajority requirements for mergers and charter amendments drive the relationship between firm performance and governance provisions. We find that poison pills, golden parachutes, and supermajority provisions are regarded as important by institutional investors. However, these mechanisms are not considered as important as some of the other governance mechanisms in our survey, many of which are not included among the 24 mechanisms in Gompers, Ishii, and Metrick (2003).

The dispersion in responses in Table 4 indicates that, as one might expect, not all institutional investors view corporate governance mechanisms identically. To determine whether there exists systematic variation in preferences across investor types (hedge funds, insurance funds, mutual funds, pension funds, and other types of funds), in Table 5 we report the mean and median scores for each governance mechanism according to investor type. We find that diversity in preferences across institution types does exist. For example, the governance mechanism of greatest importance to the hedge funds in the sample is equity ownership by managers (with a mean score of 6.25 out of 7). This issue is not nearly as important to insurance companies (mean score of 5.33), which are instead most interested in high free float (mean score of 6.00). Mutual funds find both equity ownership by managers and transparency about the holdings of large shareholders to be highly important (mean scores of 5.97), while pension funds are most concerned about ownership concentration, board independence, and high free float (mean scores of 6.17).[25]

D. Country-level Investor Protection and Firm-level Corporate Governance

Previous research (e.g., La Porta, Lopez-de-Silanes, and Shleifer, 1999; Claessens, Djankov, and Lang, 2000; Faccio and Lang, 2002) argues that poor firm-level corporate governance is associated with weaker country-level investor protection, in which case firm-level corporate governance may be of increased importance when investing in low investor protection countries. In contrast, Aggarwal, Erel, Stulz, and Williamson (2009) argue that firms in countries with higher investor protection are more likely to have good firm-level governance. In light of this research, in this section we examine whether institutions view country-level protection and firm-level corporate governance as substitutes or complements. This analysis is distinct from that in the previous section because here we study the importance of firm-level governance variables *conditional* on investors' assessment of country-level investor protection. As a proxy for assessments of investor protection we focus on how investors rate minority shareholder protection. This analysis complements recent studies on whether investors take firm-level governance into account when investing in countries with low investor protection (e.g., Leuz, Lins, and Warnock, 2009). In particular, while these studies are generally limited to measuring firm-level governance by looking at ownership structures, we use our survey methodology to test for the relevance of a much wider range of governance mechanisms.

To test whether investors view firm-level corporate governance as substitutes or complements for country-level investor protection, for each corporate governance mechanism we run the following specification using an ordered logit model:

$$CG\ Mechanism_{\mathrm{i}} = f(\ Minority\ Shareholder\ Protection_i + \mathbf{y}_{\mathrm{i}} + \varepsilon_i). \quad (2)$$

The dependent variable, $CG\ Mechanism_{\mathrm{i}}$, captures how important institutional investor i considers a given firm-level corporate governance mechanism when making investments in The

[25] In unreported tables we also tested whether the governance preferences of Dutch investors differ from those of foreign investors. With the exception of target share placements and ownership concentration, which are both considered more important by Dutch investors compared with foreign investors, we found no evidence that governance mechanism preferences differ significantly between domestic and foreign investors. This provides weak evidence for a home bias towards or against familiar governance mechanisms (e.g., share certificates) among Dutch investors.

Netherlands. Assessments as to the importance of these governance mechanisms are indicated on a scale from 1 (not important at all) to 7 (very important). The main independent variable, *Minority Shareholder Protection*$_i$, measures the extent to which institutional investor *i* agrees with the statement that minority shareholders are adequately protected in The Netherlands (*Minority Shareholder Protection*). This variable ranges from 1 (strongly disagree) to 7 (strongly agree). The regressions also include a vector of investor-specific controls, $\mathbf{y}_i$, which contain the logarithm of assets under management, the fraction of assets invested in firms in The Netherlands, and a set of investor type and legal origin dummies.[26] The results of these regressions are provided in Table 6. In conserve space, we only report results for those regressions in which the investor protection proxy (*Minority Shareholder Protection*) is significantly related to the firm-level governance variable.

As Table 6 shows, investors with very negative assessments of country-level investor protection appear to rely on a subset of firm-level governance mechanisms to mitigate agency problems and ensure that they get a return on their invested capital. First, institutional investors appear to rely on incentive compensation via equity ownership to align their interests with those of management. Second, they emphasize the presence of independent representatives on the supervisory board. And third, they prefer mechanisms that ensure a well-functioning market for corporate control (i.e., they prefer to invest in firms that have no poison pills, golden parachutes, supermajority provisions, greenmail payments, or target share placements).

Our results add to the empirical debate on the complementarity versus substitutability of corporate governance mechanisms. Aggarwal, Erel, Stulz, and Williamson (2009), for example, find that firm-level governance and investor protection are complements in the sense that firms in countries with higher investor protection are more likely to have good firm-level corporate governance. Cremers and Nairs (2005) provide empirical evidence that firm- and country-level corporate governance mechanisms can be complements, while Giroud and Mueller (2010) find that they are substitutes. Gillan, Hartzell, and Starks (2007) find that board structures can substitute for the internal mechanisms (i.e., charter provisions) examined in Cremers and Nair (2005) and Giroud and Mueller (2010). Durnev and Kim (2005) document that firms in countries with poor investor protection adapt to the poor legal environment by establishing efficient governance practices, suggesting that firm- and country-level governance are substitutes. Our

[26] All regressions are estimated with heteroskedasticity-robust standard errors.

results are more consistent with the substitute argument, as we find that from the perspective of institutional investors, firm-level mechanisms are viewed as substitutes for external investor protection.

E. One-tier versus Two-tier Board Systems

In recent literature, the question of whether a one-tier or two-tier board system is superior has been the subject of considerable debate.[27] One of the key concerns is whether board members are more likely to be captured by management, undermining their ability to monitor, under one system or the other. On the one hand, non-executive directors in the one-tier system are often closer to management and hence less likely to be objective when it comes to corrective actions (see Becht, Bolton, and Roell, 2003). On the other hand, Almazan and Suarez (2003) argue that under certain circumstances, weak (one-tier) boards may actually be optimal. Graziano and Luponini (2005), in contrast, argue that in the presence of large shareholders (more concentrated ownership), as is the case in many European countries, the two-tier board system may be optimal because it can limit the interference of a large shareholder, encouraging managers to exert effort. Adams and Ferreira (2007) develop a model of boards in which they are able to analyze differences between one-tier and two-tier board structures. In their model, under certain conditions shareholders would prefer a two-tier board structure, which entails a separation between the advisory role (management board) and the monitoring role (supervisory board). They find that board independence is particularly valuable for a supervisory board in the two-tier board structure, but it may not be valuable in the one-tier system due to the conflicting advisory and monitoring roles. In their model, which board structure is optimal depends on the level of managerial control benefits: under high benefits, the two-tier structure is better. Adams and Ferreira conclude that the choice of board structure should depend on shareholder preferences.

We address the debate on board structure by directly asking institutions to indicate their preferences with respect to type of board system. The Netherlands provides a unique set-up to address this question as Dutch firms have a choice between the two board structures. This allows us to elicit board system preferences while holding the economic and legal framework constant. Table 7 summarizes the survey responses. As can be seen from the table, our evidence suggests that the debate about the costs and benefits of the two structures is far from settled. Specifically,

[27] See, for example, O'Hare (2003).

we find that the institutional investors are split, although preference for the two-tier system (52%) almost twice that for the one-tier system (21%). This split preference result obtains across all investor types, with hedge funds having the most favorable view of the one-tier system. These results are consistent with Adams and Ferreira's (2007) model, as in many firms in The Netherlands managerial control benefits are relatively high (see LLSV, 1998 and DLLS, 2008). Our survey findings are also consistent with Graziano and Luponini's (2005) argument that the two-tier system may be preferable in markets (such as The Netherlands) with more concentrated ownership. Interestingly, our data do not suggest that investors used to a one-tier system in their home countries (e.g., investors from the United States and UK) also prefer a one-tier system when they invest abroad. Instead, our figures suggest that investors are aware that the optimality of a certain board structure depends on country-specific circumstances.

III. Shareholder Activism

A. Exit and Voice: Shareholder Activism Measures

If institutional investors become dissatisfied with the companies they invest in, they have three choices: 1) 'vote with their feet' and sell the shares (exit); 2) hold their shares and undertake actions to influence changes in the company (voice), or 3) hold their shares and do nothing (loyalty) (Hirschman, 1979). Traditional models of shareholder activism focus on the benefits of corrective actions through direct intervention and voice (e.g., Shleifer and Vishny 1986; Huddart, 1993; Admati, Pfleiderer, and Zechner, 1994; Maug, 1998; Kahn and Winton, 1998; Bolton and von Thadden, 1998; Faure-Grimaud and Gromb, 2004). However, recent theoretical models show that activism through exit can be effective and perhaps more beneficial (e.g., Attari, Banerjee, and Noe, 2006; Admati and Pfleiderer, 2008; Gopalan, 2008; Edmans, 2009; Edmans and Manso, 2010). These theories raise the question: which of these two sets of mechanisms is more widely used by institutional investors in response to dissatisfaction.

To shed light on this question, we ask institutional investors to indicate their preferences with respect to various forms of shareholder activism. Investors could provide multiple responses to indicate their willingness to engage across these different forms of engagement. The use of a survey to gather this information is important. Although one can observe activism undertaken by institutional investors who choose to make such activity public (predominantly public pension funds, union funds, and hedge funds), institutional shareholder activism often takes place behind the scenes, making it difficult to observe and measure. As a result, previous evidence has primarily been derived from shareholder proposals, case studies, and activism by hedge funds or pension funds.[28] A survey allows us to retrieve more general information about institutional investor attitudes and activities related to shareholder activism.

Panel A of Table 8 reports investors' responses to these questions, with Figure 4 further illustrating the relative importance of different types of corrective actions. We find that the form of activism that the investors are most willing to take is to vote with their feet – 80% of the investors are willing to sell their shares in the portfolio company. Such a preference is consistent with the theoretical evidence discussed above as well as with empirical evidence that suggests institutional selling can have a governance effect (Parrino, Sias, and Starks, 2003). Further, the fact that the institutional investors we survey would be in the position of being one of multiple blockholders supports the arguments of Edmans and Manso (2010) that while voice is effective for single blockholders, exit may be more effective in the case of multiple blockholders.

Although not as prevalent as the exit choice, the voice option also receives strong support from the survey respondents. In particular, the second-most important form of activism according to our institutional investor respondents is to vote against the company at the annual meeting, with 66% of the investors stating they would take such an approach.

One of the most striking results from the survey is that 55% of the investors indicate that would be willing to engage in discussions with the firm's executives. This finding suggests that the majority of our institutional investors consider themselves as potentially active shareholders in terms of voice. Comparing these results with those of Brav, Jiang, Partnoy, and Thomas (2008), who document that some hedge funds are very active in seeking communication with management, further suggests that discussions with management are not restricted to this investor type but rather are a much more general phenomenon. We also find that 22% of the investors would be willing to contact the supervisory board. The two most extreme actions receive surprisingly high votes, with 12% of the institutional investors willing to take legal measures and 11% willing to make public criticism. These responses are consistent with recent evidence surrounding specific firms (e.g., ABN Amro, Generali, Deutsche Börse). Surprisingly, the

[28] See Gillan and Starks (2000, 2007), Becht, Franks, Mayer, and Rossi (2009), Smith (1996), Klein and Zur (2009), Brav, Jiang, Partnoy, and Thomas (2008), and Carleton, Nelson, and Weisbach (1998). Choi and Fisch (2007) provide survey evidence on shareholder activism conducted by public pension funds.

responses in favor of legal actions exceed those documented in Brav, Jiang, Partnoy, and Thomas (2008).

In subsample analysis, we first examine the results by investor type and find that hedge funds show the greatest willingness to take extreme actions, though they are by no means the only type of investor to do so. Even some pension funds, mutual funds, and insurance companies indicate that they are willing to make public criticism and to take legal actions. We next report the preferences of so-called independent and grey investors, where we follow the categorizations of the FactSet/LionShares database by Ferreira and Matos (2008) and classify hedge funds and mutual funds as independent investors and insurance firms and pension funds as grey investors.[29] Grey investors are considered potentially more conflicted because they may also do business with the target firms, in which case they may be less likely to engage in shareholder activism. Our survey responses suggest that differences do exist in some areas of corporate governance. Specifically, independent investors are more likely to engage in discussions with the executive board and to disclose their voting decisions than are gray investors.[30] In a third analysis we separate the investors into two groups according to their share turnover, which we use to get their implied investment horizons. The results are shown in the last two columns of Table 8, Panel A. We find that the willingness to engage is unrelated to the institution's investment horizon, suggesting that shareholder activism is not primarily a phenomenon of short-term investors. These results are very interesting given that it is often claimed in the public debate in Europe that shareholder activism is primarily a phenomenon of short-term investors. In 2005, for example, former German Vice-Chancellor Franz Müntefering referred to active investors as "locusts" that enter companies, strip firms of assets and jobs to extract short-term benefits, and leave shortly thereafter. Our results, in contrast, do not support the view that shareholder activism is related to the investment horizon of investors.

To further examine institutions' willingness to engage in shareholder activism we construct a composite shareholder activism measure that is an investor-specific index of shareholder activism. This index is calculated by summing the corrective actions an investor is willing to take (e.g., adds a value of 1 if an investor is willing to make critical speeches at annual

[29] This categorization is somewhat different from that of previous papers that use 13-f data (e.g., Parrino, Sias, and Starks, 2003). Further, there are no public pension funds in our dataset.

[30] Choi and Fisch (2007) find that some public pensions (which are likely to be more independent than private pension funds) can be very active in corporate governance (e.g., in shareholder litigation).

meetings). The measure thus ranges between 0 (if an investor is not willing to take any actions) and 9 (if an investor is willing to take all actions), with a higher number suggesting that an investor is willing to take on a more activist role. An advantage of our index is that it is based on the *actual* willingness of an investor to engage in activism rather than on an ex ante assumption that certain investor types are more or less activist. Summary statistics for this measure are presented in Panel B of Table 8.[31] As might be expected given media coverage of their activities, the hedge funds in our sample are clearly more likely to engage in shareholder activism than are the other investors in our sample.

B. Triggers of Shareholder Activism

Having examined the governance measures institutions are willing to take, we next investigate the corporate actions or events that trigger corrective actions, and whether these triggers are different for activist versus non-activist investors based on our engagement index. To address these questions, our survey asks the institutions to indicate what types of events would trigger shareholder activism in firms listed in the United States and The Netherlands. Panel A of Table 9 shows that the most important triggers are related to corporate strategy issues. More specifically, the three-most important triggers are dissatisfaction with the goals and strategy of a firm, with planned acquisitions, and with corporate strategy in general. These results hold across countries. Interestingly, dissatisfaction with company performance does not appear to be a key driver, although it is still important. This finding is consistent with the results of Karpoff, Malatesta, and Walkling (1996), who study of the characteristics of targets for shareholder proposals.

In Panel B of Table 9 we take investors’ assessments of the triggers and divide them by the index of potential shareholder activism. We then split the sample institutions at the median willingness to engage in activism (score of 3) and report the mean level of importance for the United States and The Netherlands separately. The results show that for a number of the triggers, there is no significant difference across activist and non-activist investors’ assessments. The highest scores (in absolute terms) for the activist investors are again strategy-related issues.

[31] We also use the shareholder activism measure to separate our sample into activist and non-activist investors. An investor is considered an activist investor if the activism measure is above the sample median of 3 (i.e., if the investor is willing to take more corrective actions than the median number); an investor is considered non-activist otherwise. This categorization gives us 36% activists and 64% non-activists.

However, the scores on goals and strategies are actually lower for the activists as compared to the non-activists. In addition, poor accounting performance is even less important for activists compared to non-activists.

C. Coordination of Shareholder Activism

Researchers have advocated for some time that institutional investors are likely to contribute more to corporate governance and firm monitoring by speaking up, and in one voice (see, for example, Black, 1992). A question that then arises, but has not been well-established, is to what extent institutional investors coordinate with respect to shareholder activism. In many jurisdictions, acting in concert is illegal if it is not made public and can have material effects on the investors. The survey thus asks whether the investors would consider coordinating corrective actions, and if not, if legal considerations were the primary reason.

The survey responses are provided in Table 10. We find that of our respondents, 59% state that they would consider coordinating their actions. For the 41% that indicate they would not coordinate, over half state that the reasons is primarily related to legal concerns (e.g., the risk of violating Rule 13D in the United States or the risk of having to make a public offer in The Netherlands if the joint stakes exceed 30%). The institutional investors most likely to coordinate actions are pension funds and hedge funds, as well as larger investors and those with shorter horizons.

Given that the annual shareholders meeting is often an important podium for shareholder activism, a question that arises is how institutional investors prepare for these meetings. We therefore ask the institutional investors a series of questions related to their preparation for such meetings. The responses are provided in Table 11 with responses for holdings in the United States in Panel A and those in The Netherlands in Panel B. In Panels C and D we further divide the country-level responses into activist and non-activist investors according to our shareholder activism index.

The responses in Panels A and B imply that the sample investors, who are primarily European investors, do not engage in as much preparation for the annual meetings of their holdings in the United States as they do for their holdings in The Netherlands. For the annual meetings in the United States, 34% of the investors prepare their own point of view about agenda items, while for the meetings in The Netherlands, 54% prepare their own point of view. Across both countries there is only limited coordinated action with other institutional investors prior to the meeting, although the typical case is to have none. Similarly, the responses show that some investors contact firm management, vote in concert with other institutional investors, and make use of an external proxy adviser, but these activities are not widespread. In Panels C and D we find that with respect to their holdings in both countries, activist investors are significantly more active than non-activist investors in preparing their own views regarding agenda items. In The Netherlands activist investors are also more likely to contact the Executive Board of the company. Moreover, in both countries activist investors are more likely to make use of proxy voting advisors.

D. Shareholder Activism and Portfolio Firm Characteristics

In this section, we ask whether a link exists between the characteristics of investors' portfolio firms and their willingness to engage in shareholder activism. To do so, we employ the data on investors' portfolio holdings used earlier in the paper. For each firm characteristic, we run the following regression:

$$\textit{Firm Characteristic}_{ci} = \textit{Activism Measure}_i + \boldsymbol{X}_c + \boldsymbol{y}_i + \varepsilon_{ci}, \qquad (3)$$

where the dependent variable, $\textit{Firm Characteristic}_{ci}$, is the Tobin's Q, Leverage, Cash Holdings, Closely held Shares, Investment, or M&A Expenditures of company c held by institutional investor i.

For this analysis we employ two different variables for shareholder activism. The first is a composite measure of the nine different shareholder actions that the institutional investors could respond to. The second variable is a subset of these actions, which we term voice activism. For this measure we omit the exit action (i.e., selling shares) as it does not entail voice and we omit the disclosure of votes at annual meetings since mutual fund investors in the United States are required to do so. If investors do not consider potential actions in their holdings of shares, then we should find no relation between these variables and firm characteristics.

The regressions are again estimated using firm data from year-end 2007 (as well as data lagged from that date). All regressions are estimated with industry dummies and heteroskedasticity-robust standard errors clustered by institutional investor. The results are provided in Table 12. To conserve space, for a given firm characteristic Table 12 shows the regression coefficients for the primary independent variables of interest. The table also indicates which of the firm and investor controls are included in each of the regressions.

Our results suggest that characteristics of the firms held in an institutional investor's portfolio are related to the investor's willingness to engage in activism. In particular, those investors more willing to engage in activism are more likely to hold securities with higher leverage, fewer closely held shares, and greater investment. These results imply that investors' attitudes toward shareholder activism affect their portfolio preferences.

V. Conclusion

Institutional investors are a dominant force in world financial markets, yet we have little direct information about their preferences regarding investor protection and corporate governance. By conducting a survey of institutional investors with significant portfolio holdings in two countries that have different investor protection regimes, we are able to provide insights into investors' preferences and the relation between those preferences and their portfolio holdings.

We show that for firms in the United States and The Netherlands, institutional investors' relative investor protection assessments are in line with those indicated by the anti-director index (La Porta, Lopez de Silanes, Shleifer, and Vishny, 1998; Djankov, La Porta, Lopez de Silanes, and Shleifer, 2008) and the anti-self-dealing index (Djankov, La Porta, Lopez-de-Silanes, and Shleifer, 2008). Further, we find that the investors' assessments of the investor protection regimes are related to their views of the importance of firm-level corporate governance mechanisms as well as portfolio firm characteristics. An implication of these results is that investor concerns about investor protection affect their portfolio holdings.

We also find that conditional on weaker investor protection, firm-level corporate governance mechanisms are highly important, with the most important being mechanisms that mitigate agency conflicts between managers and shareholders (through incentives provided by executive compensation) as well as mechanisms that mitigate potential agency conflicts between large and small shareholders (through dispersed ownership structures, transparency regarding large blockholdings, and independent board structures). An important implication of these results is that firms in countries with weak legal regimes may be able to attract investors through stronger corporate governance mechanisms.

Finally, we find that the majority of institutional investors that responded to our survey are willing to engage in shareholder activism. Their preferred methods would be, first, to vote with their feet (i.e., simply sell the shares), second, to vote against the company at the annual meeting, and third, to engage in discussions with the firm's executives. Further, a substantial number of the investors would consider contacting the firm's directors to discuss their concerns and some would even employ the more extreme measure of taking legal action. The strength of these responses combined with the fact that only a small percentage of the investors would engage in public criticism imply that behind-the-scenes shareholder activism may be more prevalent than previously thought.

In conclusion, our survey evidence regarding institutional investors' preferences with respect to country-level investor protection and firm-level corporate governance suggests that these factors are interrelated and highly important in investment decisions. The results also suggest that institutional investors that actively monitoring their portfolio holdings are willing to engage in shareholder activism, even behind the scenes, to achieve their investments in their portfolio firms. These results have implications for firm management and boards in their decisions about corporate governance structures and the relation between those structures and the prevailing investor protection regime. They also have implications for regulators in their decisions about governance requirements.

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Table 1: Institutional Investor Characteristics

Panel A of this table summarizes descriptive statistics of the main characteristics of the institutional investors that returned our questionnaires (total of 118 responses). It contains information on the assets under management of the investors (value of equity portfolio measured in 1000 USD), on the fraction of shares which are invested in firms listed in The Netherlands (in %) as well as in the U.S. (in %), and on the share turnover of the investors. The share turnover is measured as the value of all buy and sell transactions in a quarter divided by the market value of the equity portfolio. The data source for these investor characteristics is FactSet/LionShares. The number of observations varies and is smaller than 118 due to limited data availability in FactSet/LionShares. Panel A further reports data on the size of the equity stakes (in %) that the institutional investors hold in their portfolio firms and reports the market values (in 1000 USD) of these stakes. This data is also from FactSet/LionShares. Panel B shows the distribution of the 118 survey respondents by investor-type. The investor-type categorization is based on self-reported information in the returned questionnaires. Panel C reports main characteristics of the different investors (assets under management, shares invested in The Netherlands and U.S., and share turnover) by investor-type. Panel D reports the national origins of the investors (actual seat and not legal seat). This information is hand-collected. Panel E lists self-reported information on which parts of the investor's equity portfolios are invested as a result of an active (positive) investment decision or as a result of a passive investment decision (for diversification or index tracking only). The data source for this information is the returned questionnaires. Panel F records whether and to what extent the institutional investors make use of external proxy voting advisors (e.g. ISS or Glass Lewis) when determining how to vote in a Dutch annual meeting (AGM). Conditional on using such firms (i.e. if the answer is not 'Never'), the panel also contains information on the extent to which the advice of the proxy voting firms is used. The data source for this information is also the returned questionnaires. The exact survey questions can be found in Appendix A-1. The FactSet/LionShares variables are calculated for the year-end 2007.

Panel A: Institutional Investor Characteristics

Investor Characteristic	**Mean**	**Median**	**STD**	**5%**	**95%**	**Obs.**
Assets under Management (in 1000 USD)	623,000	140,000	1,260,000	9,540	3,550,000	90
Fraction of Assets invested in NL (in %)	10.38%	6.85%	13.96%	0.00%	33.38%	90
Fraction of Assets invested in US (in %)	9.21%	0.00%	18.93%	0.00%	48.23%	90
Share Turnover	0.16	0.13	0.13	0.04	0.32	87
Number of Firms in Portfolio	89	60	135	20	292	89

Ownership Position in Portfolio Firms	**Mean**	**Median**	**STD**	**5%**	**95%**	**Obs.**
Percentage Ownership Stake (in %)	0.131	0.006	0.573	0.000	0.534	7919
Value of Ownership Stake (in 1000 USD)	6,103	841	20,100	44	29,400	7919

Panel B: Type of Institution

	All Investors		**Hedge Fund**		**Insurance**		**Mutual Fund**		**Pension Fund**		**Other Investors**	
	Number	Percent	Number	Percent	Number	Percent	Number	Percent	Number	Percent	Number	Percent
Questionnaire Responses	118	100.0%	7	5.9%	9	7.6%	74	62.7%	7	5.9%	21	17.8%

Panel C: Characteristics by Investor-Types

	All Investors		Hedge Fund		Insurance		Mutual Fund		Pension Fund		Other Investors	
	Mean	Median	Mean	Median	Mean	Median	Mean	Median	Mean	Median	Mean	Median
Assets under Management (in 1000 USD)	623,000	140,000	98,700	87,500	200,000	115,000	774,000	193,000	1,380,000	719,000	154,000	64,900
Fraction of Assets invested in NL (in %)	10.38%	6.85%	13.04%	13.08%	5.41%	6.55%	10.91%	6.95%	5.62%	5.29%	10.77%	6.83%
Fraction of Assets invested in US (in %)	9.21%	0.00%	25.75%	1.51%	6.35%	0.00%	7.53%	0.00%	0.00%	0.00%	15.34%	6.97%
Share Turnover	0.16	0.13	0.21	0.18	0.29	0.18	0.15	0.14	0.09	0.05	0.13	0.09
Obs.*	90	90	4	4	7	7	62	62	3	3	14	14

*Note: Share Turnover is calculated based on 87 observations (only 59 Obs. for Mutual Funds)

Panel D: Investor Origin (Actual Seat)

	All Investors		Hedge Fund		Insurance		Mutual Fund		Pension Fund		Other Investors	
	Number	Percent	Number	Percent	Number	Percent	Number	Percent	Number	Percent	Number	Percent
The Netherlands	12	13%	2	50%	0	0%	7	11%	1	33%	2	14%
UK	12	13%	0	0%	1	14%	7	11%	1	33%	3	21%
Germany	8	9%	0	0%	1	14%	7	11%	0	0%	0	0%
France	9	10%	0	0%	2	29%	5	8%	0	0%	2	14%
Luxembourg	3	3%	0	0%	0	0%	1	2%	0	0%	2	14%
Other European Countries **	33	37%	1	25%	3	43%	26	42%	0	0%	3	21%
US	9	10%	0	0%	0	0%	6	10%	1	33%	2	14%
Other North American (Canada, Caymans)	4	4%	1	25%	0	0%	3	5%	0	0%	0	0%
Total	90	100%	4	100%	7	100%	62	100%	3	100%	14	100%

**Note: Each European country in this category (BE, CH, NO, IE, IT, FI, ES) has five or less investors in the sample

Panel E: Active versus Passive Investments

	All Investors		Hedge Fund		Insurance		Mutual Fund		Pension Fund		Other Investors	
	Mean	Median	Mean	Median	Mean	Median	Mean	Median	Mean	Median	Mean	Median
Active Investment (in %)	69%	80%	93%	94%	60%	65%	72%	80%	49%	60%	61%	70%
Passive Investment (in %)	31%	20%	7%	6%	40%	35%	28%	20%	51%	40%	39%	30%
Obs.	99	99	6	6	8	8	60	60	7	7	18	18

Panel F: Importance of Proxy Voting Advisors

Usage of Proxy Voting Advisors	Always	That depends on the company	That depends on the agenda item	That depends on the circumstances	Never	Sum	Obs.
Percent of Responses	17%	10%	7%	13%	53%	100%	118

Manner of Usage of Proxy Voting Advice	Always follow advice fully	Use advice to determine own position	Use advice in case of own doubts	Others		Sum	Obs.
Percent of Responses	9%	65%	13%	13%		100%	55

Table 2: Assessment of Investor Protection by Institutional Investors

This table contains information on how institutional investors think about investor protection in the U.S. and The Netherlands. Investors could answers on a scale from 1 (strongly disagree) to 7 (strongly agree) to a set of statements regarding investor protection in these two countries. It contains the mean and median values of the responses as well as the number of available survey responses (Obs.). We also tested whether the mean response for the U.S. differed significantly from the mean response for The Netherlands and report corresponding *p*-values. Note that the table only contains responses of those investors which answered the questions both with regard to the U.S. and The Netherlands. The table also contains the anti-director rights index from La Porta, Lopez de Silanes, Shleifer and Vishny (1998) and the anti-self-dealing index from Djankov, La Porta, Lopez de Silanes and Shleifer (2008). For both indexes, higher values imply stronger investor protection. The exact survey questions can be found in Appendix A-1.

	United States				**The Netherlands**				**Diff Sign**
	Mean	**Median**	**STD**	**Obs.**	**Mean**	**Median**	**STD**	**Obs.**	***p*-value**
Survey Responses									
Minority Shareholders Protection	4.38	4.00	1.53	72	3.79	4.00	1.38	72	0.0028
Easy to Exercise Rights	4.49	5.00	1.43	72	4.00	4.00	1.45	72	0.0180
Public Information Sufficient	5.07	6.00	1.49	72	4.65	5.00	1.48	72	0.0091
Legal Rights in Place	4.01	4.00	1.43	72	3.53	4.00	1.37	72	0.0042
Indexes from Country Data									
Anti-Directors Index (LLSV, 1998) revised	3.00				2.50				
Ant-Self-Dealing Index (DLLS, 2008)	0.65				0.20				

Table 3: Investor Protection Gap and Portfolio Firm Characteristics

This table summarizes coefficient estimates of regressions of portfolio firm characteristics on the gap in the investor protection assessments by institutional investors. The investor protection gap is defined as the perception of investor protection in the US minus the assessment of investor protection in The Netherlands. Investor protection is measured using four different measures (e.g., how minority shareholders are protected and how easy it is to exercise rights). The sample consists of the holdings in portfolio firms held by 89 out of 118 institutional investors that returned our questionnaire. We include all holdings which make up at least 1% of the portfolio value of the individual investors. For each investor protection gap variable, the table reports the coefficient of a separate regression of a given portfolio firm characteristic (e.g. Tobin's Q) on the investor protection gap variable. We run individual regressions for each of the investor protection variables to avoid multicollinearity problems (the investor protection variables are highly correlated with each other). Investors could answers on a scale from 1 (strongly disagree) to 7 (strongly agree) to a set of statements regarding investor protection in the US and in The Netherlands. The sample consists of firms that are being held in the portfolios of the institutional investors by the end of 2007. The firm characteristics are also for the year 2007. Robust t-statistics are reported in parentheses. Standard are clustered at the institutional investor level. The regressions control for a set of firm and institutional investor characteristics. Tobin's Q is the market value of a firm divided by the book value of a firm, leverage is total debt over total assets, cash holdings is the value of cash holdings over assets, CH shares is the fraction of all shares that are held by insiders (including those held by directors, officers or immediate family members), investment is capital expenditure over lagged total assets, and M&A Expenditures is the value of acquired assets over lagged total assets. The total number of observations varies between 957 and 1,744 firms due to limited data availability on the firm characteristics. The source of data for the portfolio holdings is FactSet/LionShares and for the firm characteristics DataStream/Worldscope. * means significant at 10%, ** at 5%, *** at 1%.

	Tobin's Q	**Leverage**	**Cash Holdings**	**CH Shares**	**Investment**	**M&A Exp.**
	(1)	(2)	(3)	(4)	(5)	(6)
	-0.0470**	0.0063*	-0.0069**	0.4615	-0.0007	-0.0050***
Minority Shareholder Protection Gap	(-2.08)	(1.91)	(-2.10)	(1.12)	(-0.45)	(-2.72)
	-0.0415**	0.0030	-0.0093***	0.5133	-0.0023	-0.0032*
Easy to Exercise Rights Gap	(-2.34)	(0.90)	(-2.85)	(1.06)	(-1.19)	(-1.90)
	-0.0444	0.0050	-0.0009	-0.2424	-0.0013	-0.0036
Public Information Sufficient Gap	(-1.43)	(1.30)	(-0.22)	(-0.44)	(-0.99)	(-1.25)
	-0.0433*	0.0100**	-0.0058*	0.3446	0.0006	-0.0042***
Legal Rights in Place Gap	(-1.85)	(2.57)	(-1.89)	(0.77)	(0.41)	(-2.75)
Firm Controls						
Log(Total Assets)	Yes	Yes	Yes	Yes	Yes	Yes
R&D Exp.	Yes	No	No	No	No	No
Leverage	Yes	No	No	No	No	No
Cash Flow	No	Yes	Yes	Yes	Yes	Yes
RoA	No	Yes	Yes	Yes	Yes	Yes
Tobin's Q	No	No	Yes	Yes	Yes	Yes
Investor Controls						
Log(Assets under management)	Yes	Yes	Yes	Yes	Yes	Yes
Turnover	Yes	Yes	Yes	Yes	Yes	Yes
Industry Dummies	Yes	Yes	Yes	Yes	Yes	Yes
Standard Errors Clustered by Investor	Yes	Yes	Yes	Yes	Yes	Yes

Table 4: Relevance of Corporate Governance Mechanisms

This table tabulates responses on the assessment of a wide range of different firm-level corporate governance mechanisms by institutional investors. Institutional investors were asked to assess how important they consider different corporate governance and control devices when making investment decisions in The Netherlands. The governance and control devices range from issues related to anti-takeover devices, supervisory board and committee independence, equity compensation, voting as well as ownership and capital structure. Responses were measured on a scale from 1 (not important at all) to 7 (very important). The data source for this table is the returned questionnaires. The exact survey questions can be found in Appendix A-1.

	Not important at all (=1)	Un-important (=2)	More or less unimportant (=3)	Neutral (=4)	Somewhat Important (=5)	Important (=6)	Very important (=7)	At least somewhat important	Mean	Median	STD	Obs.
Issues Related to Anti-Takeover Devices												
Poisson Pills	3%	5%	8%	10%	20%	28%	26%	74%	5.26	6	1.64	92
Golden Parachutes	5%	5%	8%	12%	26%	30%	13%	69%	4.91	5	1.62	92
Supermajority Provisions	3%	5%	15%	18%	13%	27%	17%	57%	4.84	5	1.67	92
Prohibition of Greenmail Payments	2%	9%	8%	32%	16%	20%	17%	53%	4.63	4	1.55	90
Target Share Placements	2%	8%	8%	15%	15%	35%	16%	66%	5.05	6	1.59	91
Supervisory Board and Committee Independence Issues												
Supervisory Board Independence	2%	2%	2%	8%	18%	34%	34%	86%	5.74	6	1.37	92
Small Supervisory Board Size	2%	9%	10%	29%	26%	18%	5%	49%	4.46	4.5	1.39	92
Limitation on Director Terms	3%	17%	8%	22%	25%	19%	6%	50%	4.31	5	1.61	93
Possibility to Nominate Directors	3%	5%	4%	24%	25%	25%	14%	64%	4.91	5	1.49	93
Director Attendance at Meetings	2%	2%	3%	15%	16%	36%	25%	77%	5.48	6	1.41	92
Executive Compensation Issues												
Use of Equity Based Compensation	1%	3%	3%	6%	29%	37%	20%	86%	5.51	6	1.27	93
Equity Ownership by Managers	0%	3%	2%	8%	15%	37%	35%	87%	5.85	6	1.23	92
Voting Issues												
Confidential Voting	1%	9%	6%	35%	9%	27%	13%	49%	4.74	4	1.52	93
Multiple Voting Shares	2%	5%	5%	32%	15%	27%	13%	55%	4.86	5	1.47	92
Supermajority Voting Shares	2%	4%	5%	21%	16%	34%	16%	66%	5.13	6	1.48	91
Right to Call Special Shareholder Meetings	3%	7%	4%	16%	17%	33%	20%	70%	5.14	6	1.60	92
Preferred Shares	5%	11%	2%	30%	17%	25%	9%	51%	4.53	5	1.63	92
Share Certificates	5%	11%	4%	35%	18%	21%	5%	44%	4.33	4	1.55	91
Priority Shares	5%	7%	2%	24%	18%	30%	14%	62%	4.88	5	1.64	91
Ownership and Capital Structure Issues												
Ownership Concentration	0%	5%	4%	11%	23%	35%	22%	80%	5.43	6	1.35	93
Large Holdings of Institutional Investors	1%	12%	2%	19%	25%	32%	9%	66%	4.86	5	1.48	93
Cross-Shareholdings	0%	7%	3%	16%	23%	36%	15%	74%	5.24	6	1.35	92
Transparency about Holdings of Large Shareh.	0%	0%	6%	9%	12%	41%	32%	85%	5.84	6	1.16	93
Shareholder Agreements	1%	2%	8%	12%	19%	35%	23%	77%	5.43	6	1.37	93
High Free Float	0%	4%	1%	10%	15%	43%	27%	85%	5.72	6	1.24	93
High Leverage	2%	2%	4%	27%	17%	25%	23%	65%	5.19	5	1.45	93

Table 5: Relevance of Corporate Governance Mechanisms for Different Investor-Types

This table contains responses on the assessment of different corporate governance mechanisms for different institutional investor-types (hedge funds, insurance companies, mutual funds, pension funds, other investors). Investors were asked to assess how important they consider different corporate governance and control devices when taking investment decisions in The Netherlands. The governance and control devices range form issues related to anti-takeover devices, supervisory board and committee independence, equity compensation, voting as well as ownership and capital structure. Responses were measured on a scale from 1 (not important at all) to 7 (very important). For all different investor-types, the table contains the mean value and median value of the responses, as well as the number of available responses (Obs.). The data source for the table is the returned questionnaires. The exact survey questions can be found in Appendix A-1.

Mechanism	Hedge Fund			Insurance			Mutual Fund			Pension Fund			Other Investors		
	Mean	Median	Obs.	Mean	Median	Obs.	Mean	Median	Obs.	Mean	Median	Obs.	Mean	Median	Obs.
Issues Related to Anti-Takeover Devices															
Poison Pills	4.80	5.00	5	4.83	5.00	6	5.28	6.00	57	5.33	5.50	6	5.44	6.00	18
Golden Parachutes	4.20	5.00	5	4.50	5.00	6	4.82	5.00	57	5.33	6.00	6	5.39	6.00	18
Supermajority Provisions	5.20	6.00	5	3.83	4.00	6	4.81	5.00	57	5.17	5.50	6	5.06	5.00	18
Prohibition of Greenmail Payments	4.80	6.00	5	4.00	4.00	6	4.70	5.00	56	4.83	5.50	6	4.53	4.00	17
Target Share Placements	5.60	7.00	5	4.67	5.00	6	4.96	5.00	56	5.83	6.00	6	5.06	5.00	18
Supervisory Board and Committee Independence Issues															
Supervisory Board Independence	5.60	7.00	5	5.83	7.00	6	5.63	6.00	57	6.17	6.00	6	5.94	6.00	18
Small Supervisory Board Size	4.20	4.00	5	4.83	5.00	6	4.46	5.00	57	4.83	5.50	6	4.28	4.00	18
Limitation on Director Terms	4.80	6.00	5	4.33	4.50	6	4.14	4.00	58	5.33	5.00	6	4.39	4.00	18
Possibility to Nominate Directors	4.80	5.00	5	4.33	4.00	6	4.88	5.00	58	5.17	5.00	6	5.17	5.00	18
Director Attendance at Meetings	4.80	5.00	5	5.67	6.00	6	5.47	6.00	58	5.33	5.50	6	5.71	6.00	17
Executive Compensation Issues															
Use of Equity Based Compensation	5.20	6.00	5	5.17	5.00	6	5.66	6.00	58	5.17	6.00	6	5.33	5.00	18
Equity Ownership by Managers	6.25	6.50	4	5.33	5.50	6	5.97	6.00	58	5.50	6.00	6	5.67	6.00	18
Voting Issues															
Confidential Voting	4.20	4.00	5	3.67	3.50	6	4.79	4.00	58	5.33	6.00	6	4.89	5.00	18
Multiple Voting Shares	4.20	4.00	5	5.00	5.00	6	4.98	5.00	57	4.00	4.00	6	4.89	5.00	18
Supermajority Voting Shares	3.60	4.00	5	5.33	5.50	6	5.05	5.00	56	5.00	5.50	6	5.78	6.00	18
Right to Call Special Shareholder Meetings	4.80	5.00	5	4.67	4.50	6	5.11	6.00	57	5.17	5.50	6	5.50	6.00	18
Preferred Shares	3.00	2.00	5	4.83	5.50	6	4.49	4.00	57	4.33	4.00	6	5.06	5.00	18
Share Certificates	2.40	2.00	5	4.17	4.50	6	4.32	4.00	56	4.33	4.50	6	4.94	5.00	18
Priority Shares	3.60	4.00	5	4.67	5.50	6	4.82	5.00	56	5.83	6.00	6	5.17	5.50	18
Ownership and Capital Structure Issues															
Ownership Concentration	5.40	6.00	5	4.67	5.00	6	5.43	6.00	58	6.17	6.00	6	5.44	6.00	18
Large Holdings of Institutional Investors	4.20	4.00	5	4.50	5.00	6	4.72	5.00	58	5.50	6.00	6	5.39	6.00	18
Cross-Shareholdings	5.20	6.00	5	4.83	5.00	6	5.32	6.00	57	5.00	5.00	6	5.22	5.50	18
Transparency about Holdings of Large Shareh.	6.00	6.00	5	5.67	6.00	6	5.97	6.00	58	5.33	6.00	6	5.61	6.00	18
Shareholder Agreements	5.40	6.00	5	5.83	6.00	6	5.48	6.00	58	5.67	6.00	6	5.06	5.00	18
High Free Float	4.80	4.00	5	6.00	6.00	6	5.76	6.00	58	6.17	6.00	6	5.61	6.00	18
High Leverage	5.20	5.00	5	5.33	5.50	6	5.22	5.00	58	5.50	6.00	6	4.94	5.00	18

Table 6: Investor Protection and Corporate Governance

This table contains estimates of ordered response models (ordered logit models) at the institutional investor level. The dependent variables in these regressions capture how important institutional investors consider a set of firm-level corporate governance mechanisms. The importance of these governance mechanisms was measured on a scale from 1 (not important at all) to 7 (very important). The main independent variable measures to what extent institutional investors agree to the statement that minority shareholders are adequately protected in The Netherlands (country-level minority shareholder protection). This variable has a possible range between 1 (=strongly disagree) and 7 (=strongly agree). Control variables are the assets under management of an investor, the fraction of shares that are invested in The Netherlands and dummy variables for the investor-type as well as for the national origin of the investors (actual seat). In the interest of saving space, we only report those regressions where the investor protection proxy is significantly related to the firm level governance variable. Robust t-statistics are reported in parentheses. * means significant at 10%, ** significant at 5%, and *** significant at 1%.

Dependent Variable:	Poison Pills	Golden Parachutes	Supermajority Provisions	Prohibition of Greenmail Payments	Target Share Placements	Supervisory Board Independence	Equity Ownership by Managers	Multiple Voting Shares	Supermajority Voting Shares	Priority Shares
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Minority Shareholders Protection	-0.502***	-0.360**	-0.333*	-0.371*	-0.403***	-0.354**	-0.501***	-0.450***	-0.418**	-0.378**
	(-2.92)	(-2.30)	(-1.90)	(-1.94)	(-2.59)	(-2.16)	(-2.94)	(-2.72)	(-2.15)	(-2.57)
Assets under Mgmt	6.08e-10*	8.41e-11	2.49e-10	2.29e-10	7.37e-10***	1.14e-10	2.93e-10	4.82e-10**	2.59e-11	3.73e-10*
	(1.79)	(0.41)	(1.43)	(1.46)	(3.82)	(0.69)	(1.38)	(2.14)	(0.16)	(1.67)
Fraction of Assets invested in NL	-1.769	1.762	1.393	1.556	-1.926	1.229	3.690	6.034***	5.166**	7.338***
	(-0.96)	(0.86)	(0.57)	(0.74)	(-0.82)	(0.51)	(1.29)	(3.10)	(2.05)	(2.70)
Institutional Investor Types Dummy	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES
Investor Origin Dummy	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES
Obs.	69	69	69	68	69	70	70	70	69	69
Pseudo R-Square	0.123	0.123	0.103	0.065	0.091	0.124	0.040	0.076	0.138	0.093

Table 7: One Tier versus Two Tier Board Structure

This table tabulates information on the preferences of the institutional investors with regard to the board structures of firms. Investors could express their preference with respect to (i) a one tier board structure (a system with executive and non-executive directors on the same board), (ii) a two tier board structure (a system with separate management and supervisory boards), or could state that they had (iii) no preference. The table contains the percentage of responses for each of the three categories. We summarize the information for different investor types (hedge funds, insurance companies, mutual funds, pension funds, other investors) and for several other characteristics of the investors (size of investor, fraction of US and NL share holdings, investment horizon and investor origin). An investor is considered to be large if its assets under management are above the sample median. An investor is considered to have large US (NL) holdings, if its fraction of equity holdings invested in the US (NL) are above the sample median. An investor is considered to have a long investment horizon if its share turnover is below the sample median. We measure investor origin by looking at the actual seats of an investor. The exact survey question can be found in Appendix A-1.

	Preference over Board Systems			
	One Tier System	**Two Tier System**	**No Preference**	**Obs.**
All Investors	21%	52%	27%	92
Hedge Fund	40%	60%	0%	5
Insurance	17%	50%	33%	6
Mutual Fund	22%	47%	31%	59
Pension Fund	0%	67%	33%	6
Other Investors	19%	63%	19%	16
Large Investor (>=Median)	26%	42%	32%	38
Small Investor (>Median)	21%	52%	27%	33
Large US Holdings (>=Median)	19%	52%	29%	31
Small US Holdings (<Median)	28%	43%	30%	40
Large NL Holdings (>=Median)	20%	51%	29%	35
Small NL Holdings (<Median)	28%	42%	31%	36
Long Horizon (Share Turnover<Median)	27%	41%	32%	37
Short Horizon (Share Turnover>=Median)	21%	52%	27%	33
Investor Origins:				
The Netherlands	17%	58%	25%	12
UK	33%	44%	22%	9
Germany	17%	33%	50%	6
France	0%	80%	20%	5
Luxembourg	0%	33%	67%	3
Other European	35%	46%	19%	26
US	13%	38%	50%	8
Other North American	50%	0%	50%	2

Table 8: Shareholder Activism by Institutional Investors: Corrective Actions

Panel A of this table contains information on the measures institutional investors are prepared to take as corrective actions (shareholder activism) against companies they have invested in. The information is presented for different investor-types (hedge funds, insurance company, mutual fund, or pension fund), according to whether an investor is an independent or grey investor, and according to whether investors have a long (Share Turnover>Median) or short investment horizon (Share Turnover<=Median). Based on Ferreira and Matos (2008), we consider hedge funds and mutual funds as independent investors and insurance firms and pension funds as grey investors. Panel B contains a self-constructed activism measure. It is constructed as an index that linearly adds the corrective actions an investor is willing to take. It can therefore range between 0 (no actions) and 9 (all actions). A higher number suggests that an investor is willing to be more active and to take more actions against a company. The panel shows the activism measure for different investor-types and investment horizons. An investor is considered to be an Activist Investor if the activism measure from is above the sample median (i.e. if the investor is willing to take more corrective actions than the median); and a Non-Activist Investor otherwise. The exact survey questions can be found in Appendix A-1.

Panel A: Corrective Actions

	Overall	**Hedge Funds**	**Insurance**	**Mutual Funds**	**Pension Funds**	**Other Investors**	**Indep. Investors**	**Grey Investors**	**Long Horizon**	**Short Horizon**
Selling Shares	80%	75%	71%	79%	83%	88%	78%	77%	82%	73%
Voting Against Comp. at the Annual Meeting	66%	75%	57%	67%	0%	53%	68%	77%	58%	65%
Critical Speeches at Annual Meeting	19%	25%	14%	20%	17%	18%	20%	15%	16%	11%
Proposals at Annual Meeting	20%	50%	14%	21%	17%	12%	23%	15%	18%	22%
Discussion with Executive Board	55%	75%	29%	59%	33%	53%	60%	31%	53%	51%
Contact Supervisory Board	22%	75%	14%	21%	17%	18%	25%	15%	18%	22%
Public Criticism	11%	25%	14%	10%	0%	12%	11%	8%	8%	11%
Disclosure of Voting at Annual Meeting	21%	50%	14%	23%	0%	18%	25%	8%	21%	19%
Legal Measures	12%	50%	0%	7%	17%	24%	9%	8%	5%	14%

Panel B: Self-Constructed Activism Measure

Shareholder Activism										
Mean	3.05	5.00	2.28	3.07	2.83	2.94	3.18	2.54	2.63	2.80
Median	3.00	5.00	2.00	2.80	2.00	3.00	3.00	2.00	2.00	3.00
Min	0.00									
Max	9.00									
STD	2.16									

Investors Category	
Activist Investors	34 (36%)
Non-Activist Investors	61 (64%)

Table 9: Triggers of Shareholder Activism in the United States and in The Netherlands

Panel A of this table lists information on the importance of a set of corporate events for triggering a corrective action (shareholder activism) against a target firm held by an institutional investor. We have information on the relative importance of such triggers for target firms listed in the United States and in The Netherlands. The investors could indicate the relevance of a certain trigger on a scale from 1 (not important at all) to 7 (very important). The table contains the mean and median response values. Multiple responses were possible. Note that the table only contains responses of those investors which answered the questions both with regard to the U.S. and The Netherlands. We also tested whether the mean response values for the US and The Netherlands are significantly different from each other and report the respective *p*-values. Panel B reports the importance of certain triggers for activist and non-activist investors. An investor is considered to be an activist if the activism measure from Table 7 is above the sample median (i.e. if the investor is willing to take more corrective actions than the median). The exact survey questions can be found in Appendix A-1.

Panel A: Triggers for Shareholder Activism

	Target in United States				Target in The Netherlands				Diff. Sign?
	Mean	**Median**	**STD**	**Obs.**	**Mean**	**Median**	**STD**	**Obs.**	***p*-value**
Poor accounting performance	5.28	6.00	1.63	67	5.30	6.00	1.61	67	0.709
Poor stock price performance (absolute performance)	4.60	5.00	1.67	68	4.63	5.00	1.68	68	0.418
Poor stock price performance relative to peers	4.99	5.00	1.62	68	5.03	5.00	1.60	68	0.182
Excessive compensation packages	5.09	5.00	1.51	68	5.10	5.00	1.51	68	0.568
Low payments to shareholders despite high cash hold.	5.07	5.00	1.34	68	5.04	5.00	1.35	68	0.418
Suboptimal capital structure	5.24	5.00	1.16	68	5.24	5.00	1.16	68	1.000
Poor corporate strategy	5.59	6.00	1.21	68	5.59	6.00	1.22	68	1.000
Rights issues	4.90	5.00	1.25	68	4.93	5.00	1.24	68	0.159
Significant asset sales	5.13	5.00	1.12	68	5.18	5.00	1.12	68	0.182
Planned acquisitions	5.61	6.00	1.09	67	5.63	6.00	1.07	67	0.321
Goals & strategy	6.00	6.00	1.16	68	6.04	6.00	1.11	68	0.260

Panel B: Triggers for Activist versus Non-Activist Investors

	Activist Investors (Shareholder Activism Measure>Median)				Non-Activist Investors (Shareholder Activism Measure<=Median)					
	Target in US		**Target in NL**		**Target in US**		**Target in NL**		**US Diff. Sign.**	**NL Diff. Sign.**
	Mean	**Median**	**Mean**	**Median**	**Mean**	**Median**	**Mean**	**Median**	***p*-value**	***p*-value**
Poor accounting performance	4.71	5.00	4.75	5.00	5.60	6.00	5.60	6.00	0.0246	0.0442
Poor stock price performance (absolute performance)	4.42	5.00	4.46	5.00	4.70	5.00	4.73	5.00	0.4858	0.6834
Poor stock price performance relative to peers	4.88	5.00	4.92	5.00	5.05	5.00	5.09	5.00	0.6792	0.9053
Excessive compensation packages	5.13	5.00	5.13	5.00	5.07	5.00	5.09	6.00	0.8792	0.8389
Low payments to shareholders despite high cash hold.	5.21	5.00	5.17	5.00	5.00	5.00	4.98	5.00	0.5855	0.1748
Suboptimal capital structure	5.54	6.00	5.58	6.00	5.07	5.00	5.05	5.00	0.1219	0.2107
Poor corporate strategy	5.46	5.00	5.50	6.00	5.66	6.00	5.64	6.00	0.4570	0.5940
Rights issues	5.08	5.00	5.17	6.00	4.80	5.00	4.80	5.00	0.3345	0.0176
Significant asset sales	4.92	4.50	4.96	5.00	5.25	5.00	5.30	5.00	0.2168	0.1210
Planned acquisitions	5.57	6.00	5.61	6.00	5.64	6.00	5.64	6.00	0.9441	0.6173
Goals & strategy	5.50	5.50	5.67	6.00	6.27	7.00	6.25	7.00	0.0061	0.0421

Table 10: Coordination of Shareholder Activism by Institutional Investors

Panel A of this table contains information on whether institutional investors consider coordinating their shareholder activism (corrective actions) with other investors. The table also subdivides the sample according to different investor criteria. We summarize the information for different investor-types (hedge funds, insurance companies, mutual funds, pension funds, other investors) and for several other characteristics of the investors (size of investor, fraction of US and NL share holdings, investment horizon and investor origin). An investor is considered to be large if its assets under management are above the sample median. An investor is considered to have large US (NL) holdings, if its fraction of equity holdings invested in the US (NL) are above the sample median. An investor is considered to have a long investment horizon if its share turnover is below the sample median. We measure investor origin by looking at the actual seats of an investor. Panel B contains information on the reasons why investors do not coordinate their shareholder actions (if the answer in the previous question was no). The exact survey questions can be found in Appendix A-1.

Panel A: Coordination of Activism

	Would you consider coordinating a corrective action?		
Type of Investor	**No**	**Yes**	**Obs.**
All Investors	41%	59%	91
Hedge Fund	25%	75%	4
Insurance Company	40%	60%	5
Mutual Fund	41%	59%	59
Pension Fund	17%	83%	6
Other Investors	53%	47%	17
Large Investor (>=Median)	32%	68%	38
Small Investor (>Median)	55%	45%	33
Large US Holdings (>=Median)	50%	50%	32
Small US Holdings (<Median)	36%	64%	39
Large NL Holdings (>=Median)	47%	53%	34
Small NL Holdings (<Median)	38%	62%	37
Long Horizon (Share Turnover<Median)	50%	50%	36
Short Horizon (Share Turnover>=Median)	35%	65%	34
Investor Origins:			
The Netherlands	33%	67%	12
UK	33%	67%	12
Germany	80%	20%	5
France	20%	80%	5
Luxembourg	100%	0%	3
Other European	48%	52%	27
US	38%	63%	8
Other North American	50%	50%	2

Panel B: Reasons for Non-Coordination

Why No Coordination?	**Legal Risks**	**Other Reasons**	**Obs.**
	59%	41%	37

Table 11: Preparation of Annual Meeting

This table tabulates information on the measures taken by institutional investors to prepare for the annual meeting of a company. Panel A provides this information for annual meetings of firms in the United States while Panel B provides this information for annual meetings of companies in The Netherlands. Panel C and D separate the sample according to the shareholder activism measure from Table 8. This measure is constructed as an index that linearly adds the corrective actions an investor is willing to take. It can therefore range between 0 (no actions) and 9 (all actions). A higher number suggests that an investor is willing to be more active and to take more actions against a company. The data source for this information is the returned questionnaires. Multiple answers were possible. The exact survey questions can be found in Appendix A-1.

Panel A: Annual Meetings in the United States

	No		**Yes**		**Obs.**
Summary Statistics	**Responses**	**Percent**	**Responses**	**Percent**	
Prepare your own point of view in relation to agenda of the company	59	66%	31	34%	90
Contact other institutional investors	85	94%	5	6%	90
Contact the Executive Board of the company	84	93%	6	7%	90
Get legal advice	86	96%	4	4%	90
Decide to vote in concert with other institutional investors	79	88%	11	12%	90
Make use of an external proxy voting advisor	67	74%	23	26%	90

Panel B: Annual Meetings in The Netherlands

	No		**Yes**		**Obs.**
Summary Statistics	**Responses**	**Percent**	**Responses**	**Percent**	
Prepare your own point of view in relation to agenda of the company	41	46%	49	54%	90
Contact other institutional investors	78	87%	12	13%	90
Contact the Executive Board of the company	79	88%	11	12%	90
Get legal advice	86	96%	4	4%	90
Decide to vote in concert with other institutional investors	77	86%	13	14%	90
Make use of an external proxy voting advisor	56	62%	34	38%	90

Table 11 (continued)

Panel C: Annual Meetings In the US for Activist and Non-Activist Investors	Activist Investors (Shareholder Activism Measure>Median)				Non-Activist Investors (Shareholder Activism Measure<=Median)				Diff. Sign.
	No		Yes		No		Yes		
	Responses	Percent	Responses	Percent	Responses	Percent	Responses	Percent	*p*-value
Prepare your own point of view in relation to agenda of the company	16	52%	15	48%	43	73%	16	27%	0.0442
Contact other institutional investors	28	90%	3	10%	57	97%	2	3%	0.2204
Contact the Executive Board of the company	28	90%	3	10%	56	95%	3	5%	0.4122
Get legal advice	29	94%	2	6%	57	97%	2	3%	0.5085
Decide to vote in concert with other institutional investors	28	90%	3	10%	51	86%	8	14%	0.5980
Make use of an external proxy voting advisor	17	55%	14	45%	50	85%	9	15%	0.0017

Panel D: Annual Meetings in the Netherlands for Activist and Non-Activist Investors	Activist Investors (Shareholder Activism Measure>Median)				Non-Activist Investors (Shareholder Activism Measure<=Median)				Diff. Sign.
	No		Yes		No		Yes		
	Responses	Percent	Responses	Percent	Responses	Percent	Responses	Percent	*p*-value
Prepare your own point of view in relation to agenda of the company	5	16%	26	84%	36	61%	23	39%	0.0000
Contact other institutional investors	25	81%	6	19%	53	90%	6	10%	0.2278
Contact the Executive Board of the company	23	74%	8	26%	56	95%	3	5%	0.0040
Get legal advice	29	94%	2	6%	57	97%	2	3%	0.5085
Decide to vote in concert with other institutional investors	27	87%	4	13%	50	85%	9	15%	0.7662
Make use of an external proxy voting advisor	11	35%	20	65%	45	76%	14	24%	0.0001

Table 12: Shareholder Activism and Portfolio Firm Characteristics

This table summarizes coefficient estimates of regressions of portfolio firm characteristics on two variables capturing institutional investor shareholder activism. The first variable, Shareholder Activism, is a composite measure of the 9 different potential activities in which the investors could engage. The second variable, Voice Activism, is also a composite measure but consists of the 7 activities that would constitute "voice activism." The sample consists of the holdings in portfolio firms held by 89 out of 118 institutional investors that returned our questionnaire. We include all holdings which make up at least 1% of the portfolio value of the individual investors. For each activism variable, the table reports the coefficient of a separate regression of a given portfolio firm characteristic (e.g. Tobin's Q) on the variable. The sample consists of firms that are being held in the portfolios of the institutional investors by the end of 2007. The firm characteristics are also for the year 2007. Robust t-statistics are reported in parentheses. Standard are clustered at the institutional investor level. The regressions control for a set of firm and institutional investor characteristics. Tobin's Q is the market value of a firm divided by the book value of a firm, leverage is total debt over total assets, cash holdings is the value of cash holdings over assets, CH shares is the fraction of all shares that are held by insiders (including those held by directors, officers or immediate family members), investment is capital expenditure over lagged total assets, and M&A Expenditures is the value of acquired assets over lagged total assets and cash flow is EBIT over lagged total assets. The total number of observations varies between 1,181 and 2,176 firms due to limited data availability on the firm characteristics. The source of data for the portfolio holdings is FactSet/LionShares and for the firm characteristics DataStream/Worldscope. * means significant at 10%, ** at 5%, *** at 1%.

	Tobin's Q	**Leverage**	**Cash Holdings**	**CH Shares**	**Investment**	**M&A Exp.**
	(1)	(2)	(3)	(4)	(5)	(6)
Shareholder Activism	0.0076	0.0062*	0.0015	-0.7367**	0.0022*	0.0012
	(0.50)	(1.90)	(0.69)	(-2.18)	(1.91)	(0.76)
Voice Activism	0.0111	0.0085**	0.0014	-1.1391***	0.0027*	0.0011
	(0.64)	(2.16)	(0.51)	(-2.79)	(1.93)	(0.59)
Firm Controls						
Log(Total Assets)	Yes	Yes	Yes	Yes	Yes	Yes
R&D Exp.	Yes	No	No	No	No	No
Leverage	Yes	No	No	No	No	No
Cash Flow	No	Yes	Yes	Yes	Yes	Yes
RoA	No	Yes	Yes	Yes	Yes	Yes
Tobin's Q	No	No	Yes	Yes	Yes	Yes
Investor Controls						
Log(assets under management)	Yes	Yes	Yes	Yes	Yes	Yes
Turnover	Yes	Yes	Yes	Yes	Yes	Yes
Standard Errors Clustered by Investor	Yes	Yes	Yes	Yes	Yes	Yes
Industry Dummies	Yes	Yes	Yes	Yes	Yes	Yes

Figure 1: Active versus Passive Investments

This figure lists self-reported information on the parts of the portfolios of the institutional investors that are invested as a result of an active (positive) investment decision or as a result of a passive investment decision (for diversification or index tracking only). The data source for this information is the returned questionnaires.

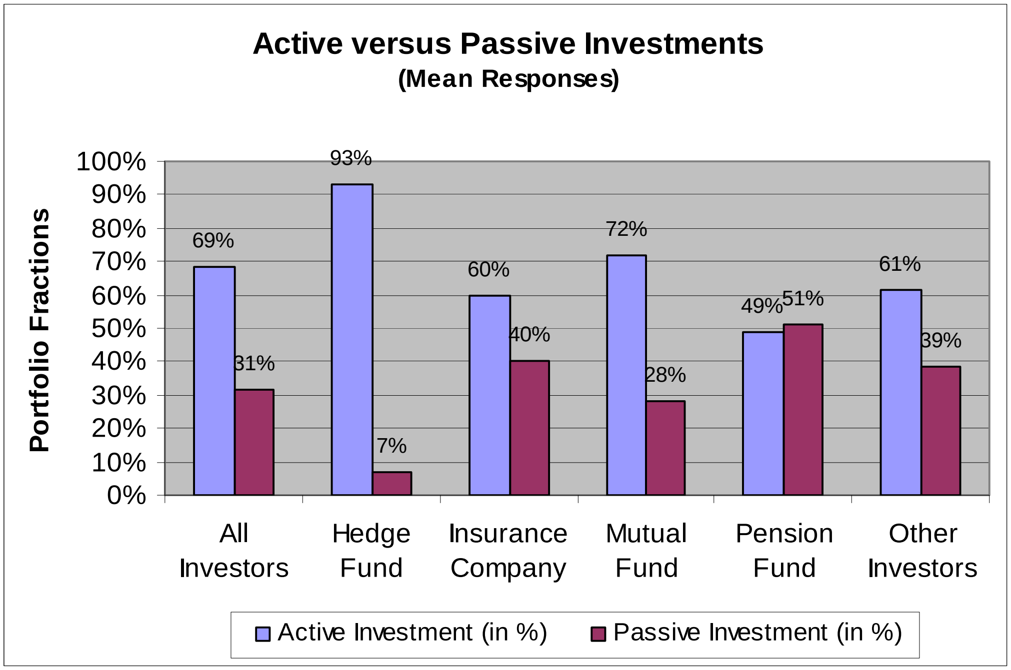


Figure 2: Assessment of Investor Protection

This figure contains information on how institutional investors think about investor protection in the United States and in The Netherlands. Investors could provide answers on a scale from 1 (strongly disagree) to 7 (strongly agree) to a set of statements regarding investor protection in the two countries. The exact questions can be found in the survey (see Appendix A-1).

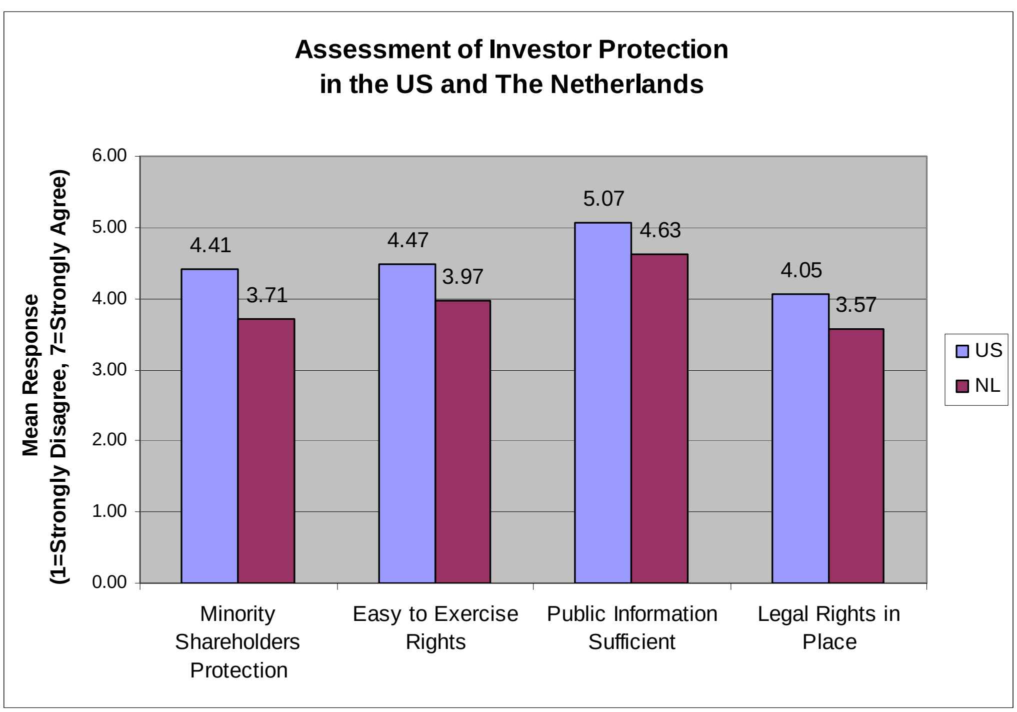


Figure 3: Assessment of Corporate Governance Mechanisms

This figure shows the five firm-level corporate governance mechanisms that are considered to be most and least important for their investment decisions according to the institutional investors. The governance and control devices range form issues related to anti-takeover devices, supervisory board and committee independence issues, equity compensation issues, to voting issues and ownership and capital structure issues. Responses were measured on a scale from 1 (not important at all) to 7 (very important).

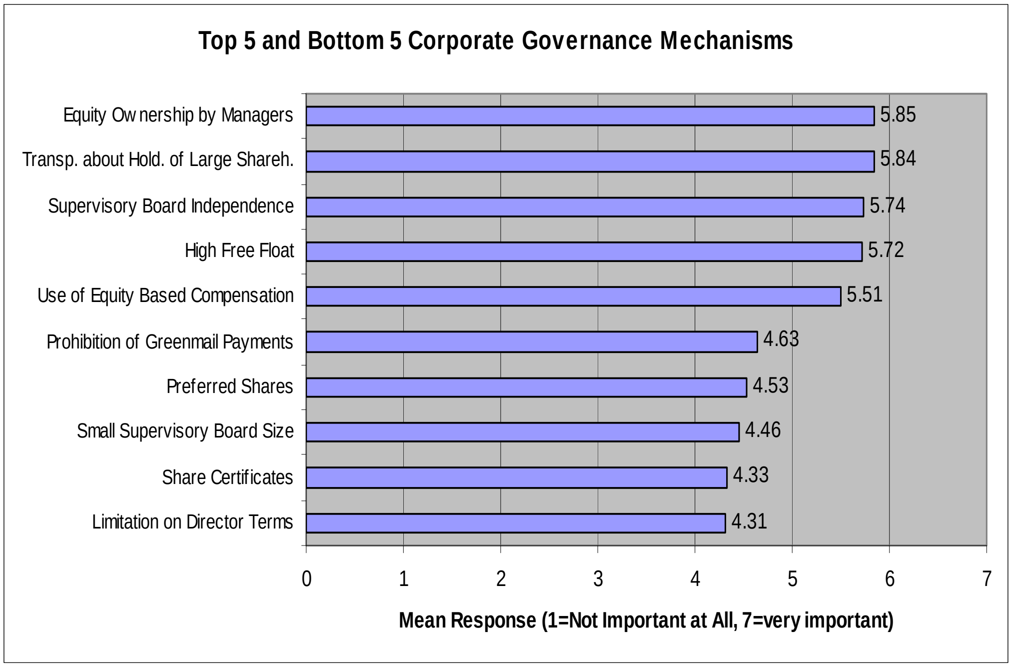
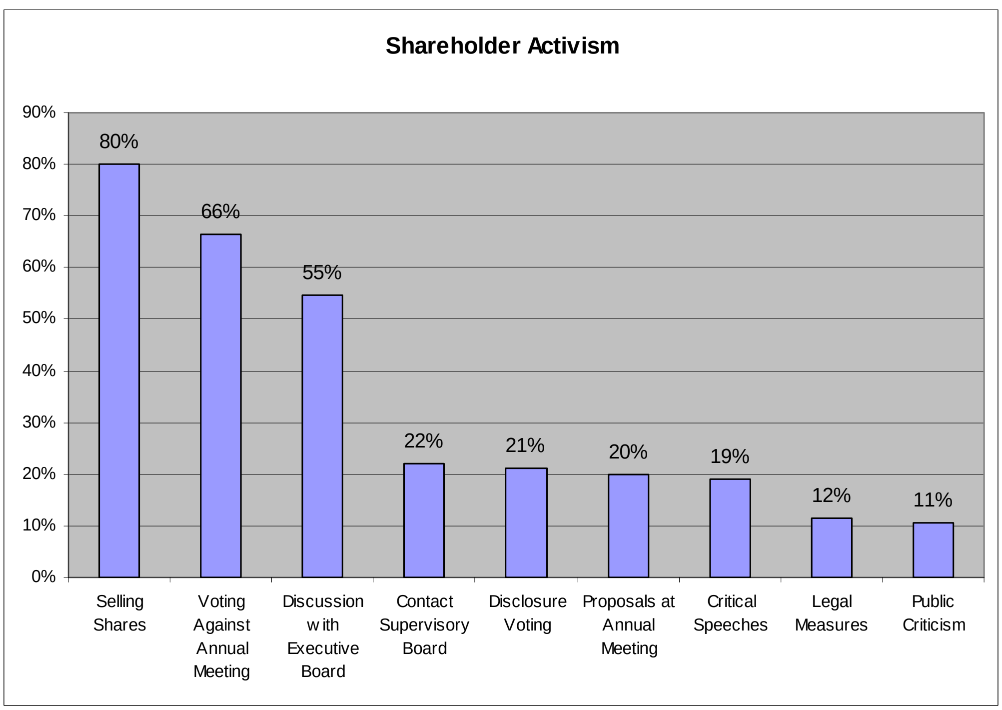


Figure 4: Shareholder Activism

This figure contains information on the measures investors are prepared to take as corrective actions (shareholder activism) against the companies they have invested in. The table reports the fraction of investors that are willing to take a certain action. Multiple responses were possible.



Appendix A-1: Questionnaire

Introduction

Thank you very much for participating in this survey.

As a token of our appreciation for your co-operation you can apply for a complimentary copy of one of the following books:

- ☐ The Age of Turbulence: Adventures in a New World by Alan Greenspan
- ☐ Pay without Performance: The Unfulfilled Promise of Executive Compensation by Lucian Bebchuk and Jesse Fried
- ☐ Corporate Governance (2nd Edition) by Kenneth A. Kim and John R. Nofsinger

We would like to make use of all provided answers. In case you unexpectedly did not fill in the questionnaire completely, we will make use of the answers you already handed over to us. We assume that you have no objection to this, in case you have, please tick the box below.

☐ I do not want my answers to be processed if I have not completed the survey entirely.

In this survey we use a 7 point scale. There are two different types of questions in which this scale is used. Below both scales are written down, in the explanation of the specific question only the extremes of the scale are written down.

1. not important at all	1. strongly disagree
2. unimportant	2. disagree
3. more or less unimportant	3. somewhat disagree
4. neutral	4. neutral
5. somewhat important	5. somewhat agree
6. important	6. agree
7. very important	7. strongly agree

Part A: General information regarding institution/fund

This part of the questionnaire contains some general questions about the fund/institution you work for.

A1 You work for a fund/institution which can be <u>best</u> described as:

☐ hedge fund ☐ pension fund ☐ endowment, charity
☐ insurance company ☐ private equity fund ☐ other, namely: ____________________
☐ mutual fund

A2.a Do you make use of an external proxy voting advisor (like ISS or Glass Lewis) when determining how to vote in a Dutch annual general meeting?

☐ always ☐ that depends on the agenda item ☐ never
☐ that depends on the company ☐ that depends on the circumstances

In case the answer of question A2.a is not 'never'.

A2.b In what manner do you use the external proxy voting advisor?

☐ I always follow their advice blindly (full proxy)
☐ I use their advice to determine my own position
☐ In case I have (some) doubts about my own position, the advice of the external proxy voting advisor is binding for me
☐ other, namely: ____________________

A3 Which part of your shares portfolio (in percentages) is the result of a positive investment decision (active, satellite) and which part is the result of diversification (passive, core)?

_____ positive investment (active, satellite)

_____ diversification (passive, core)

Part B: Your perception of shareholder participation and corporate governance

In part B questions are asked about your perception of the internal and external mechanisms in the Netherlands and the preparation for the AGM.

B1 How important do you consider the following corporate governance and control devices when taking investment decisions in the Netherlands? *(Scale from 1 not important at all to 7 very important)*

Internal mechanisms

Issues related to Anti-takeover devices

_____ poison pills
_____ golden parachutes
_____ supermajority provisions
_____ prohibition of greenmail payments
_____ target share placements

Supervisory Board and Committee Independence Issues

_____ supervisory board independence (majority of independent directors)
_____ small supervisory board size
_____ limitations on director terms
_____ possibility to nominate directors
_____ director attendance at meetings

Executive Compensation Issues

_____ use of equity-based compensation
_____ equity ownership by executives

External mechanisms

Voting Issues

_____ confidential voting
_____ multiple voting shares
_____ supermajority voting requirements
_____ right to call special shareholder meetings
_____ preferred shares
_____ share certificates
_____ priority shares

Ownership and Capital Structure Issues

_____ ownership concentration
_____ large holdings of institutional investors
_____ cross-shareholdings
_____ transparency about the holdings of large shareholders
_____ shareholder agreements
_____ high free float
_____ high leverage

B2 What would be your preference with respect to the board structure?

☐ one tier board (executive and non-executives directors) ☐ no preference
☐ two tier board (management and supervisory board)

B3 Do you agree with the following statements? *(Scale from 1 strongly disagree to 7 strongly agree)*

US (standard)

_____ minority shareholders interests are adequately protected
_____ it is easy for shareholders to exercise their rights in the companies they invest
_____ the public information provided by companies is sufficient for shareholders to make significant decisions
_____ the appropriate legal measures are in place to allow shareholders to influence the general strategy of the company in which I invest

The Netherlands

_____ minority shareholders interests are adequately protected
_____ it is easy for shareholders to exercise their rights in the companies they invest
_____ the public information provided by companies is sufficient for shareholders to make significant decisions
_____ the appropriate legal measures are in place to allow shareholders to influence the general strategy of the company in which I invest

Part C: Corrective Actions

Shareholders in recent years have become considerably more willing to take corrective actions in relation to the companies in which they own shares. Part C contains questions about this subject.

C1 What kind of corrective actions are you prepared to take on behalf of your investments?

- ☐ none
- ☐ selling shares held in the company
- ☐ voting against at AGM
- ☐ critical speeches at the AGM
- ☐ proposals at the AGM
- ☐ discussions with executive board members
- ☐ contacting the supervisory board to seek management change
- ☐ publicly criticizing executive board members
- ☐ disclosure of voting (against) at AGM
- ☐ use of lawsuits against managers

C2. How important are the following events for potentially triggering a corrective action? *(Scale from 1 not important at all to 7 very important)*

US (standard)	**NL**	
____	____	poor accounting performance (e.g. missing of pre-set EBIT or sales figures)
____	____	poor stock price performance (absolute performance)
____	____	poor stock price performance relative to peers
____	____	excessive compensation packages
____	____	low payments to shareholders despite high cash holdings
____	____	suboptimal capital structure
____	____	poor corporate strategy (e.g. firm is too diversified)
____	____	rights issues
____	____	significant asset sales
____	____	planned acquisitions
____	____	goals & strategy

C3. Would you consider coordinating such a corrective action with other investors?

☐ yes ☐ no

In case the answer of question C3.a is 'no'.

C4. What is the reason for not coordinating your actions with other investors?

☐ legal risks (acting in concert) ☐ other reason: ____________________

Part D: Voting behavior and decision making in the AGM

The final part of the questionnaire contains questions about your voting behavior in the Annual General Meeting in the Netherlands compared to the US and decision making in the Annual General Meeting in both countries.
(In case the answer to question A.2b is 'I always follow their advice blindly (full proxy)', the questions below are skipped)

D1 Prior to an annual general shareholder meeting of a company, do you:

US (standard)
- ☐ prepare your own point of view in relation to agenda of the company
- ☐ contact other institutional investors
- ☐ have meetings with other institutional investors
- ☐ contact the Executive Board of the company
- ☐ get legal advice
- ☐ decide to vote in concert with other institutional investors
- ☐ make use of an external proxy voting advisor

The Netherlands
- ☐ prepare your own point of view in relation to agenda of the company
- ☐ contact other institutional investors
- ☐ have meetings with other institutional investors
- ☐ contact the Executive Board of the company
- ☐ get legal advice
- ☐ decide to vote in concert with other institutional investors
- ☐ make use of an external proxy voting advisor

Appendix A-2: Legal Seat of Investors

This table reports the legal seat of the investors which responded to our survey. This table complements the figures in Table 1-D which reports the actual seats of the investors (i.e., where the operations take place) of the 24 investors that have their legal seat in Luxembourg, only 3 actually operate from there. The other investors are de facto located in the United Kingdom (5 investors), the United States (3 investors), The Netherlands (5 investors), Switzerland (3 investors), Belgium (1 investor), Germany (2 investors), France (1 investor) and Spain (1 investor). From the two investors with a legal seat on the Cayman Islands, one operates from the UK. The data is from FactSet/LionShares.

	All Investors		**Hedge Fund**		**Insurance**		**Mutual Fund**		**Pension Fund**		**Other Investors**	
	Number	Percent	Number	Percent	Number	Percent	Number	Percent	Number	Percent	Number	Percent
The Netherlands	7	8%	2	50%	0	0%	3	5%	1	33%	1	7%
UK	6	7%	0	0%	1	14%	3	5%	1	33%	1	7%
Germany	6	7%	0	0%	1	14%	5	8%	0	0%	0	0%
France	8	9%	0	0%	2	29%	5	8%	0	0%	1	7%
Luxembourg	24	27%	0	0%	0	0%	17	27%	0	0%	7	50%
Other European Countries **	28	31%	1	25%	3	43%	22	35%	0	0%	2	14%
US	6	7%	0	0%	0	0%	4	6%	1	33%	1	7%
Other North American (Canada, Caymans)	5	6%	1	25%	0	0%	3	5%	0	0%	0	0%
Total	90	100%	4	100%	7	100%	62	100%	3	100%	14	93%

**Note: Each European country in this category (BE, CH, NO, IE, IT, FI, ES) has five or less investors in the sample

Appendix A-3: Evaluation of Non-Response Bias

Panel A of this table compares descriptive statistics of the institutional investors that returned our questionnaires with all non-responding investors as well as all other institutional investors in the FactSet/LionShares data base. It contains information on the Assets Under Management of the investors (measured in 1000 USD), and on the fraction of all assets of the investors that are invested in firms listed in The Netherlands (in %), on the fraction of all assets that are invested in firms listed in the US (in %). The table contains means, medians, and standard deviations (STD) of the respective variables. It also contains the number of available observations (Obs.). The table also contains p-values of t-tests comparing the mean values of a variable for the respondents with the mean values of the non-respondents/other investors in FactSet/LionShares. Panel B compares the national origins (legal seats) of the respondents and the non-respondents. The data source for the variables is FactSet/LionShares. The number of observations varies due to limited data availability in FactSet/LionShares.

Panel A: Investor Characteristics

	Respondents			
	Mean	**Median**	**STD**	**Obs**
Assets under Mgmt (in 1000 USD)	623,000	140,000	1,260,000	90
Fraction of Assets invested in NL (in %)	10.4%	6.9%	14.0%	90
Fraction of Assets invested in US (in%)	9.2%	0.0%	18.9%	90

	Non-Respondents				Diff Sign?
	Mean	**Median**	**STD**	**Obs**	**p-value**
Assets under Mgmt (in 1000 USD)	1,060,000	216,000	4,100,000	1060	0.4916
Fraction of Assets invested in NL (in %)	9.9%	8.0%	9.3%	1060	0.0033
Fraction of Assets invested in US (in%)	19.8%	13.5%	20.6%	376	0.0000

	All Other Investors in FactSet/LionShares				Diff Sign?
	Mean	**Median**	**STD**	**Obs**	**p-value**
Assets under Mgmt (in 1000 USD)	2,030,000	256,000	9,910,000	3730	0.1982
Fraction of Assets invested in NL (in %)	4.4%	2.9%	6.5%	3730	0.0000
Fraction of Assets invested in US (in%)	37.8%	29.2%	32.9%	2257	0.0009

Panel B: Distribution of National Origins (Legal Seats) of Institutional Investors

Countries	**Respondents**	**Non-Respondents**	**All Other Inv. in FactSet/LionShares**
The Netherlands	8%	4%	2%
UK	7%	16%	14%
US	7%	11%	29%
Germany	7%	8%	7%
France	9%	10%	9%
Luxembourg	27%	22%	18%
Others	37%	22%	22%
Total	100%	100%	100%

Appendix A-4: Portfolio Firms of Institutional Investors

This table provides financial information on the firms that are held in the portfolios of the institutional investors that returned our survey. We have the equity portfolio holdings for 89 out of the total of 118 investors. We include all holdings which make up at least 1% of the portfolio value of the individual investors. The portfolio holding data is from FactSet/LionShares. We matched the holding data with financial data on the firms in the portfolios. This data is from DataStream/Worldscope. Tobin's Q is the market value of a firm divided by the book value of a firm, ROA (Return on Assets) is EBITDA over lagged total assets, leverage is total debt over total assets, dividends (div.) is dividends over earnings, cash holdings is the value of cash holdings over assets, CH shares is the fraction of all shares that are held by insiders (including those held by directors, officers or immediate family members), investment is capital expenditure over lagged total assets, R&D Expenditures is R&D expenditures over lagged total assets, cash flow is EBIT over lagged total assets, and ROA is EBITDA over lagged total assets and M&A Expenditures is the value of acquired assets over lagged total assets. The total number of observations varies due to data limitations in DataStream/Worldscope. The data is for the year-end 2007.

Characteristics of Portfolio Firms

	Mean	Median	5%	95%	STD	Obs.
Tobin's Q	1.783	1.477	1.004	3.608	1.048	2672
RoA	0.165	0.151	0.012	0.387	0.135	2636
Leverage	0.256	0.231	0.024	0.526	0.165	2665
Dividends	-0.106	0.191	0.000	0.578	5.813	2577
Cash Holdings	0.149	0.081	0.012	0.516	0.224	2121
CH Shares (in %)	20.5	12.7	0.04	63.9	21.8	2039
Investment	0.061	0.044	0.001	0.172	0.124	2559
R&D Expenditures	0.037	0.016	0.000	0.151	0.054	1434
M&A Expenditures	0.050	0.006	0.000	0.189	0.156	2260