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"THE GOLDILOCKS DILEMMA": A RESPONSE TO LUCIAN BEBCHUK AND SCOTT HIRST

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The following Piece reflects the revised and extended remarks given by Barbara Novick at the Harvard Roundtable on Corporate Governance, November 6, 2019.

Thank you to Lucian Bebchuk for inviting me to share some thoughts on investment stewardship to kick off the 2019 Corporate Governance Roundtable.

I. ACADEMIC THEORIES ON INVESTMENT STEWARDSHIP

Corporate governance and investment stewardship have caught the attention of companies, asset owners, asset managers, academics—including several here at Harvard—as well as nongovernmental organizations (NGOs), policy makers, and the media.[1] This heightened attention has generated a number of academic articles focusing on these topics,[2] and many people have formed views based on specific studies.

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1. See generally, e.g., Ceres, Envtl. Def. Fund & KKS Advisors, The Role of Investors in Supporting Better Corporate ESG Performance: Influence Strategies for Sustainable and Long-Term Value Creation (2019), https://www.ceres.org/sites/default/files/reports/2019-04/Investor_Influence_report.pdf [https://perma.cc/9D4C-XYT7]; Jeff Sommer, Want a Bigger Say on Corporate Behavior? Move Your Money, N.Y. Times (Dec. 12, 2019), https://www.nytimes.com/2019/12/12/business/corporate-behavior-move-your-money.html [https://perma.cc/KS5A-A9S8].

2. See generally, e.g., Ian R. Appel, Todd A. Gormley & Donald B. Keim, Passive Investors, Not Passive Owners, 121 J. Fin. Econ. 111 (2016); Lucian Bebchuk & Scott Hirst, Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy, 119 Colum. L. Rev. 2029 (2019) [hereinafter Bebchuk & Hirst, Index Funds and the Future]; Lucian Bebchuk & Scott Hirst, The Specter of the Giant Three, 99 B.U. L. Rev. 721 (2019) [hereinafter Bebchuk & Hirst, The Specter]; Jill Fisch, Assaf Hamdani & Steven Davidoff Solomon, The New Titans of Wall Street: A Theoretical Framework for Passive Investors, 168 U. Pa. L. Rev. 17 (2020); Sean J. Griffith & Dorothy S. Lund, Conflicted Mutual Fund Voting in Corporate

While many of these theories are interesting, as one works through the various papers in which they appear, it becomes apparent that several theories conflict with each other. For example, John Coates has *The Problem of Twelve*, in which a small group of individuals, predominately from index fund managers, will effectively have control over the majority of U.S. public companies.[3] Meanwhile, Lucian Bebchuk and Scott Hirst have a theory that index fund managers do not have sufficient incentive to pursue stewardship activities and therefore only pursue superficial efforts. In *The Specter of the Giant Three*, they look at the same facts as John Coates and conclude that these same asset managers do not sufficiently use their potential influence on companies.[4] My remarks will focus on why each of these hypotheses is false, and I will provide a practitioner's perspective on how we at BlackRock approach investment stewardship as part of the overall investment process.

FIGURE 1: ACADEMIC THEORIES OF INVESTMENT STEWARDSHIP

The Problem of Twelve John C. Coates IV	*Conflicted Mutual Fund Voting in Corporate Law* Dorothy S. Lund & Sean J. Griffith	*Specter of the Giant Three* Lucian A. Bebchuk & Scott Hirst
Passive Investors, Not Passive Owners R. Appel, Todd A. Gormley & Donald B. Keim	*Index Funds and the Future of Corporate Governance* Lucian A. Bebchuk & Scott Hirst	*The New Titans of Wall Street* Jill E. Fisch, Assaf Hamdani & Steven Solomon

II. WHO CONTROLS THE ASSETS?

The issue of "control" is central to this discussion of investment stewardship. To start, the "largest shareholder" is not necessarily the same as the

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Law, 99 B.U. L. Rev. 1151 (2019); John C. Coates, The Future of Corporate Governance Part I: The Problem of Twelve (Harvard Law Sch., Harvard Pub. Law Working Paper No. 19-07, 2019), https://ssrn.com/abstract=3247337 (on file with the *Columbia Law Review*).

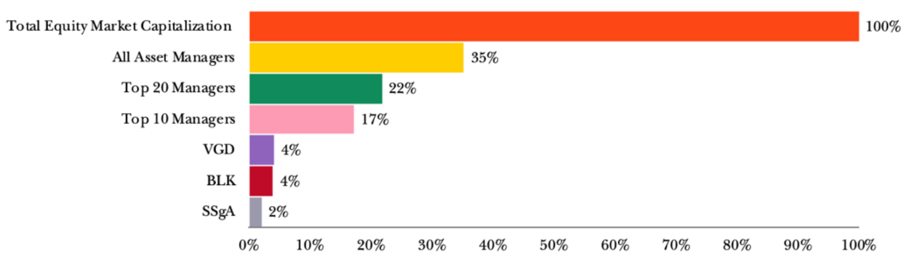
3. Coates, supra note 2, at 13–19 (explaining that these individuals may exercise significant influence over corporate governance).

4. See Bebchuk & Hirst, Index Funds and the Future, supra note 2, at 2035; Bebchuk & Hirst, The Specter, supra note 2, at 741.

"controlling shareholder." Examining the majority of U.S. public companies—and certainly "large-cap" public companies—the largest shareholder holds only a single digit percentage of shares outstanding.[5]

Let us look at some numbers that address who owns stocks and who manages these equity assets. One of the overlooked facts here is that the majority of equity assets globally are managed directly by asset owners. Aggregating across all external asset managers as of year-end 2017, this cohort represents 35% of equity ownership. Furthermore, the top ten asset managers represent only 17% of equity ownership, as shown in Figure 2. The missing pieces include assets managed in-house, primarily by pension plans and sovereign wealth funds. Another important factor is activist investors who take concentrated stakes in specific companies.[6] Furthermore, activist investors often take seats on companies' boards where they have a significant holding.[7]

FIGURE 2: BREAKDOWN OF GLOBAL EQUITY MARKET CAPITALIZATION[8]



5. See David Peetz & Georgina Murray, Who Owns the World? Tracing Half the Corporate Giants' Shares to 30 Owners, Conversation (Apr. 11, 2017), http://theconversation.com/who-owns-the-world-tracing-half-the-corporate-giants-shares-to-30-owners-59963 [https://perma.cc/3FKW-CVCL] ("In 56% of very large corporations the top shareholding was less than 15%. In one in ten of these corporations the top-ranked shareholding was 5% or less.").

6. See Rachel Butt, Here Are the 10 Biggest Activist Money Managers and Some of Their Most Impressive Bets, Bus. Insider (June 17, 2016), https://www.businessinsider.com/top-10-biggest-activist-investors-2016-6 [https://perma.cc/7SMM-FRQA] (describing various activists' targeted stakes taken in various companies).

7. See Lindsay Fortado, Activist Investors Start Asking for More in Board Battles, Fin. Times (Apr. 26, 2019), https://www.ft.com/content/9edc8dc6-6823-11e9-a79d-04f350474d62 [https://perma.cc/U8P9-VGTP] (noting that many activist investors seek board seats and that "activists still won the largest number of board seats at public companies ever last year"); Jack "Rusty" O'Kelley III, Russell Reynolds Assocs., Activist Investors' Approach to Targeting Boards, Harvard Law Sch. Forum on Corp. Governance (Aug. 21, 2017), https://corpgov.law.harvard.edu/2017/08/21/activist-investors-approaches-to-targeting-boards [https://perma.cc/9QG5-7CPZ] (explaining strategies activist investors use for targeting board seats).

8. Asset managers' AUM is derived from Money Managers, Pensions & Invs. Research Ctr., https://researchcenter.pionline.com/v3/rankings/money-manager/datatable [hereinafter P&I] (data as of Dec. 31, 2018). P&I data are self-reported and may not be comprehensive of all managers everywhere. Total equity market capitalization is based on calculations by BlackRock, based on proprietary methodology using data from World Federation Exchange (data as of Q2 2017), Bank for International Settlement (data as of

In looking more closely at voting and control issues, it is important to note that quite a few large institutional asset owners outsource the management of their assets while choosing to vote proxies for themselves.[9] We estimate that 25% of BlackRock's large separate account mandates are managed for clients who vote their own shares. For example, Washington State Investment Board (WSIB) considers voting a key part of their fiduciary duty to their beneficiaries, as they described in their letter to the Federal Trade Commission (FTC).[10]

And while many academic studies use Form 13F data to measure ownership stakes, these data are not reliable.[11] First, not all investors are required to file Forms 13F. For example, company executives are exempt from filing, as they are individual shareholders, not institutional shareholders.[12] Additionally, asset managers have interpreted aspects of 13F differently. Firms interpret the types of reportable "voting authority" differently, creating discrepancies in how they report.[13] The bottom line is 13F data problems potentially invalidate academic analyses that rely on these data.

As Figure 1 above shows, Vanguard, BlackRock, and State Street Global Advisors currently manage approximately 4%, 4%, and 2% of global equities, respectively. In *The Specter of the Giant Three*, Bebchuk and Hirst assume that these managers will continue to grow at the rate they have for the past few years.[14] While their projections are arithmetically correct, this assumption ignores multiple external variables that can change what products,

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Dec. 31, 2017), Hedge Fund Research (data as of Nov. 2017), Cerulli (data as of Nov. 2017), Simfund (data as of Nov. 2017), iShares Global Business Intelligence (data as of Nov. 2017), Global Heat Map (data as of Dec. 2016), and McKinsey Cube (data as of Dec. 2016). Total equity market capitalization data include institutional and hedge fund figures sourced from McKinsey Cube data as of the previous year due to data availability constraints.

9. The Council of Institutional Investors, for example, recently asserted that large asset owners typically vote their own proxies. See Letter from Council of Institutional Inv'rs to SEC (Oct. 15, 2019), https://corpgov.law.harvard.edu/2019/10/24/cii-letter-to-the-sec-proxy-advisor-regulation [https://perma.cc/ZW5Z-FKKB].

10. Letter from Theresa Whitmarsh, Exec. Dir., Wash. State Inv. Bd. & Gary Bruebaker, Chief Inv. Officer, Wash. State Inv. Bd., to FTC (Dec. 3, 2018), https://www.ftc.gov/system/files/documents/public_comments/2018/12/ftc-2018-0107-d-0002-163005.pdf [https://perma.cc/UR7M-N7E5].

11. See, e.g., Bebchuk & Hirst, Index Funds and the Future, supra note 2, at 2143; Edward Rock & Marcel Kahan, Index Funds and Corporate Governance: Let Shareholders Be Shareholders 13 n.49 (N.Y. Univ. Law & Econ. Research Paper Series, Working Paper No. 18-39, 2019), https://ssrn.com/abstract=3295098 (on file with the *Columbia Law Review*).

12. See Frequently Asked Questions About 13F, SEC (Feb. 24, 2020), https://www.sec.gov/divisions/investment/13ffaq.htm [https://perma.cc/4RKD-DAFW].

13. See R. Franklin Balotti, Jesse A. Finkelstein & Gregory P. Williams, Meetings of Stockholders § 12.3.6.1 (3d ed. Supp. 2020) (describing 13F filing requirements as "somewhat vague" and noting that "[c]ertain institutions claim voting authority for shares actually voted by others" while "some institutions claim no voting authority for shares that they do control and vote").

14. Bebchuk & Hirst, The Specter, supra note 2, at 725.

asset classes, or managers are in or out of favor at a given time, and that translates into changes in growth rates.

Looking back over the past few decades, the list of the top ten asset managers has changed significantly. Who remembers Bankers Trust, Wilmington Trust, and Kemper Financial Services? Each of these firms was a top ten asset manager by total assets under management (AUM) in 1990, when BlackRock was barely on the viewfinder as a two-year-old startup.[15] Likewise, Deutsche Asset Management was a top ten firm by total AUM in 2000, and PIMCO was a top ten firm by total AUM in 2010.[16] However, neither Deutsche nor PIMCO are in the top ten by total AUM today. The point being: This is not a static group. Looking at the asset management industry today, the growth rate over the past five years of Dimensional Fund Advisors' (DFA) equity AUM is 9%, while the growth rate of the equity AUM over the past five years of Bebchuk and Hirst's *Giant Three* ranges from 2% to 12%, suggesting potential changes to the ranks of the largest asset managers in the future.[17]

While we are looking at the data, let's consider the oft-repeated statement: "Index funds are surpassing active funds." While this is factually true, this statement is only part of the story. I call this "the denominator problem." Mutual funds, including open-end funds and exchange-traded funds (ETFs), represent 35% of U.S. equities and 21% of global equities.[18] The remainder of global equity assets are held by pension funds, private funds, foundations and endowments, and individuals. With nearly half of U.S. mutual funds using index strategies, this represents approximately 17% of U.S. equities.[19] BlackRock has done extensive analysis of nonmutual fund assets, and we estimate that even when these assets are included, the percent of U.S. equities managed, whether in-house or externally, using index strategies is under 30%, far from a majority of equity assets.[20]

III. Spectrum of Investment and Engagement Strategies

You may notice that I use the phrase "index strategies" instead of "passive strategies." People often refer to investment strategies as "passive" or "active," as if there is a binary choice. In practice, however, investment strategies fall along a spectrum from pure index to enhanced index, to

15. P&I, supra note 8.

16. Id.

17. Id.

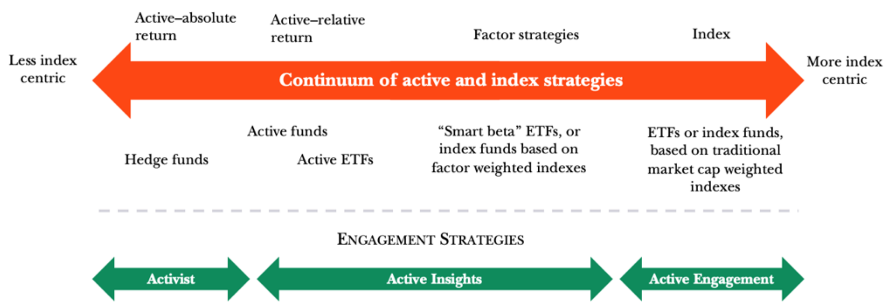
18. Calculations by BlackRock, based on proprietary methodology using data from World Federation Exchange (data as of Dec. 2018), Bank for International Settlement (data as of Q2 2018), Hedge Fund Research (data as of Dec. 2018), Cerulli (data as of Dec. 2018), Simfund (data as of Dec. 2018), iShares Global Business Intelligence (data as of Nov. 2017), Global Heat Map (data as of Dec. 2017), McKinsey Cube (data as of Dec. 2017), and Broadridge Financial Solutions.

19. Id.

20. Id. Estimates for insourced U.S. assets assume 20% of total institutional assets per McKinsey and BlackRock stakeholders.

broadly diversified portfolios, to concentrated portfolios, to long–short strategies, as shown in Figure 3. This is an important distinction because most of these strategies are measured relative to an equity index, and the degree of difference from index strategies to enhanced index strategies, to broadly diversified strategies, may not be as much as one would think.

FIGURE 3: THE SPECTRUM OF INVESTMENT AND ENGAGEMENT STRATEGIES



In looking at flows leaving "active" strategies, many investors are leaving broadly diversified portfolios with high fees and moving to pure index and enhanced index strategies with lower fees, and sometimes better returns, while still providing broad diversification. And now investors can combine various index strategies to create what amounts to an actively managed portfolio.

Similarly, engagement strategies fall on a spectrum of their own. Engagement strategies range from activist, which advises on company strategy and seeks board seats, to active engagement, which deals with environmental, social, and corporate governance (ESG) issues, but does not seek board seats or to influence companies. In between are active insights, which attempt to draw perspectives from discussions with management that are more in-depth than in active engagement. At BlackRock, we define engagement as encompassing both interaction with companies and the voting of proxies. Hedge funds often take an "activist approach," which includes advising on company strategy and seeking board seats.[21] On the other hand, index fund managers are, by definition, long-term holders of stocks and stewards on behalf of their clients.[22] As a result, index fund managers tend to take an "active approach" to engagement. To be clear, index fund managers do not take board seats, and their engagement is largely focused on

21. See Martin Lipton, Dealing with Activist Hedge Funds and Other Activist Investors, Harvard Law Sch. Forum on Corp. Governance (Jan. 25, 2019), https://corpgov.law.harvard.edu/2019/01/25/dealing-with-activist-hedge-funds-and-other-activist-investors-2 [https://perma.cc/WW6H-YBQ2].

22. Lucian Bebchuk, Alma Cohen & Scott Hirst, Index Fund Stewardship, Harvard Law Sch. Forum on Corp. Governance (June 12, 2018), https://corpgov.law.harvard.edu/2018/06/12/index-fund-stewardship [https://perma.cc/S6AZ-PYA9].

corporate governance.[23] As I will discuss later, index fund managers are discouraged, by virtue of the regulatory hurdles they would encounter, from telling management what to do and from coordinating stewardship activities with other managers. To complete the picture, active managers have the choice of holding or selling a stock. Active managers may also engage with companies, and many do so effectively; however, theories suggesting that these investors are somehow more engaged than index fund managers or other investors are not apparent in the marketplace.[24]

IV. WHO RUNS THE COMPANIES?

Another key issue in this debate is understanding how public companies are run. Some key questions to consider include: What is the role of management? What is the role of the board of directors? How does the board engage with management and make compensation decisions? How does the board of directors engage with compensation consultants?

Company management makes strategic decisions for companies, ranging from product offerings to pricing, to long-term strategy. Company management is required to act in the best interest of all shareholders.[25] Meanwhile, boards of directors have an oversight role, and are elected as the representatives of all shareholders.[26] Stock exchange listing rules require a majority of directors to be independent, and corporate governance norms have evolved to limit the number of boards that an individual director serves on.[27]

FIGURE 4: QUANTIFYING WHO RUNS U.S. PUBLIC COMPANIES

Over 28,000 individuals oversee public companies in the U.S. alone, including:

- **3,948 CEOs**
- **24,259 board directors**

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23. BlackRock, Policy Spotlight: Shareholders Are Dispersed and Diverse 2 (2019), https://www.blackrock.com/corporate/literature/whitepaper/policy-spotlight-shareholders-are-dispersed-and-diverse-april-2019.pdf [https://perma.cc/92FV-CP74].

24. See Bebchuk & Hirst, Index Funds and the Future, supra note 2, at 2037 n.17 (collecting literature on institutional investor activism).

25. See Arnold v. Soc'y for Sav. Bancorp, 678 A.2d 533, 539 (Del. 1996) ("Fiduciary duties are owed by the directors and officers to the corporation and its stockholders.").

26. See Stone v. Ritter, 911 A.2d 362, 369–70 (Del. 2006) (describing directors' oversight liability); *Arnold*, 678 A.2d at 539.

27. Nasdaq Listing Rule 5605(b)(1) (2009); N.Y. Stock Exch., NYSE Listed Company Manual § 303A.02(a) (2013); Institutional S'holder Servs., United States Proxy Voting Guidelines Benchmark Policy Recommendations 11 (2019), https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf [https://perma.cc/T6CC-G7GX] (providing guidance to vote against a director who sits on more than five boards or for a CEO who sits on the boards of more than two companies).

As shown in Figure 4, there are over 28,000 unique individuals involved in running and setting strategy at U.S. companies alone, including nearly 4,000 CEOs and over 24,000 board directors.[28] And that is before accounting for the diverse investor base I discussed earlier or the influence of proxy advisory firms and compensation consultants.

V. How Does Executive Compensation Work?

While some identify say-on-pay[29] as a potential theoretical mechanism for "control," the nature of say-on-pay votes tells a different story. Say-on-pay votes are retrospective advisory votes, designed to inform boards of directors of shareholder sentiment toward executive compensation for the previous year. For the 2019 N-PX year, more than three-quarters of say-on-pay votes passed with over 90% of the vote, and only 2% were defeated.[30]

Compensation consultants are an often-omitted piece of the puzzle. Approximately 90% of large companies use a compensation consultant to assist them in determining compensation packages for executives, especially for CEOs.[31] Based on a review of company filings, there are more than ten compensation consulting firms that are frequently used.[32]

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28. Ownership Database, FactSet Res. Sys., https://www.factset.com [hereinafter FactSet, Ownership Database] (data as of Mar. 26, 2019). Note that in a few cases, there are CEOs that are the CEO of more than one public company; in these cases, these CEOs have only been counted once. The number of board directors does not include directors that are also CEOs to avoid double counting, nor does the number of board directors double count directors that may serve on more than one board.

29. Dodd–Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 951, 124 Stat. 1376, 1899–1900 (2010) (adding mandatory shareholder voting to approve compensation of executives to § 14A of the Securities Exchange Act of 1934, 15 U.S.C. § 78n–1 (2018)); SEC Office of Inv'r Educ. & Advocacy, Investor Bulletin: Say-on-Pay and Golden Parachute Votes 1 (2011), https://www.sec.gov/files/sayonpay.pdf [https://perma.cc/DWA9-BJEZ].

30. These calculations are based on ownership data from the FactSet Research System Ownership Database using the SEC Form N-PX filings for Russell 3000 companies for the period July 1, 2018 to June 30, 2019. FactSet, Ownership Database, supra note 28 (data as of June 30, 2019).

31. Ryan Chacon, Rachel E. Gordon & Adam S. Yore, Compensation Consultants: Whom Do They Serve? Evidence from Consultant Changes 2 & n.2 (Jan. 11, 2019) (unpublished manuscript), https://ssrn.com/abstract=3281133 (on file with the *Columbia Law Review*).

32. Equilar, Inc., https://www.equilar.com (data as of Mar. 2019). The top ten compensation consultants are: Frederic W. Cook & Co., Meridian Compensation, Pay Governance, Pearl Meyer & Partners, Semler Brossy Consulting Group, Towers Watson, Mercer, Exequity, Compensation Advisory Partners, and Compensia. Id.

FIGURE 5: TOP COMPENSATION CONSULTANTS[33]

Top 10 Compensation Consultants	
Rank	**Consulting Firm**
1	Frederic W. Cook & Co.
2	Meridian Compensation
3	Pay Governance
4	Pearl Meyer & Partners
5	Semler Brossy Consulting Group
6	Towers Watson
7	Mercer
8	Exequity
9	Compensation Advisory Partners
10	Compensia

The ultimate goal of any executive compensation program should be to incentivize senior executives to enhance their respective company's performance relative to prior years and its competitors for the benefit of all shareholders. But it is company boards—not shareholders—that are making these compensation decisions.[34] In setting executive compensation, boards consider a range of factors. For example, they generally start with a peer group comparison provided by a compensation consultant that analyzes executive compensation packages of companies within the same or similar sectors.[35] The processes around setting executive compensation are very transparent, as each company discloses in its proxy statement: (i) the role of the compensation committee; (ii) which compensation consultant, if any, the board of directors retained; (iii) a peer group analysis, including which companies were in the peer group; and (iv) details on salary, performance bonus, long-term incentives, and perquisites.[36]

Another overlooked factor in executive compensation is the role of proxy advisors. Nadya Malenko, Associate Professor of Finance at Boston College, estimates that negative Institutional Shareholder Services (ISS) recommendations drive a 25% decrease in support for say-on-pay proposals.[37] Similarly, Jill Fisch, Professor of Business Law at the University of Pennsylvania Law School, along with colleagues, finds ISS's recommendations

33. See id.

34. Barbara Novick, Executive Compensation: The Role of Public Company Shareholders, Harvard Law Sch. Forum on Corp. Governance (July 31, 2019), https://corpgov.law.harvard.edu/2019/07/31/executive-compensation-the-role-of-public-company-shareholders [https://perma.cc/EGY9-M745] ("[The] process is undertaken by the Board of Directors, often under the advisement of the Board's compensation committee and/or compensation consultant, to determine the amount and composition of executive pay packages.").

35. Id.

36. 15 U.S.C. § 78n–1 (2018); 17 C.F.R. § 229.402 (2019).

37. Nadya Malenko & Yao Shen, The Role of Proxy Advisory Firms: Evidence from a Regression-Discontinuity Design, 29 Rev. Fin. Stud. 3394, 3399 (2016).

are a significant driver of say-on-pay vote results.[38] Unsurprisingly, compensation committees and their consultants often solicit the input of proxy advisors to garner a favorable recommendation on say-on-pay votes.

As a shareholder, BlackRock considers executive compensation an important element in attracting, rewarding, and retaining key talent for the companies in which we invest on behalf of our clients. As we explain in our stewardship commentary, we don't recommend a one-size-fits-all approach.[39] Instead, we look for alignment of interests, albeit with significant flexibility for boards to determine the appropriate executive compensation packages. At BlackRock, we believe that companies should explicitly disclose how incentive plans reflect strategy and incorporate drivers of long-term shareholder value; these disclosures should include the metrics and time frames by which shareholders should assess performance.[40]

To reiterate, while permitting shareholders to express their views on executive compensation after the fact, say-on-pay votes do not dictate how much executives will be paid, nor do they set out the components of executive compensation packages. As compensation packages become better aligned with long-term value creation and shareholders' interests, companies have seen an increase in the affirmation of say-on-pay votes. Ultimately, decisions of executive compensation belong to boards of directors of public companies.

VI. Most Votes Are Not Contentious

From reading media stories, one would think every shareholder vote is hotly contested, with extremely close voting outcomes.[41] However, in reality, very few votes are contentious, with most overwhelmingly voted in one direction, either "FOR" or "AGAINST." To put this in perspective, in the most recent proxy season in the United States, there were approximately

38. Jill Fisch, Darius Palia & Steven Davidoff Solomon, Is Say on Pay All About Pay? The Impact of Firm Performance, 8 Harv. Bus. L. Rev. 101, 113–14 (2018).

39. See BlackRock, BlackRock Investment Stewardship's Approach to Executive Compensation 1–2 (2019), https://www.blackrock.com/corporate/literature/publication/blk-commentary-our-approach-to-executive-compensation.pdf [https://perma.cc/62DL-JK4P].

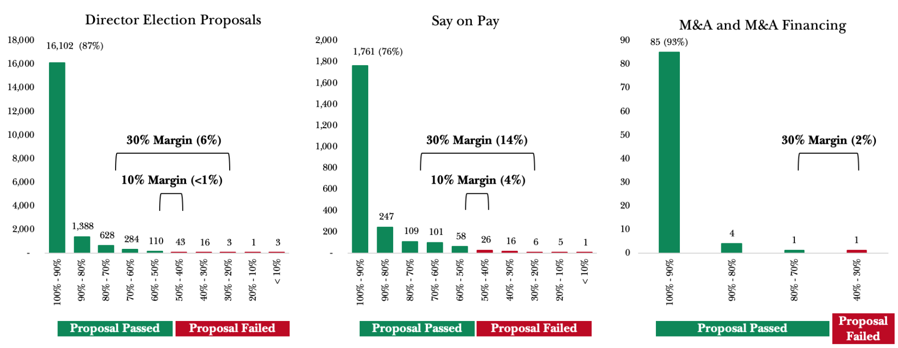
40. See id.

41. See, e.g., Lydia DePillis, Amazon Weathers Contentious Shareholder Meeting, as Investors and Workers Press for Change, CNN (May 22, 2019), https://www.cnn.com/2019/05/22/economy/amazon-shareholder-meeting/index.html [https://perma.cc/M3MD-645U] (last updated May 22, 2019); Campbell Soup and Third Point Urge Shareholders to Vote for Two Different Boards, CNBC (Sept. 17, 2018), https://www.cnbc.com/2018/09/17/campbell-soup-and-third-point-urge-shareholders-to-vote-for-two-different-boards.html [https://perma.cc/5XUR-ZCWB]; Stacy Cowley & Michael Corkery, A Showdown over Wells Fargo's Board of Directors Looms, N.Y. Times: Dealbook (Apr. 24, 2017), https://www.nytimes.com/2017/04/24/business/dealbook/wells-fargo-board-election.html [https://perma.cc/N9GN-5XAQ].

31,500 ballot items, of which 444 were shareholder proposals, and 2,330 were say-on-pay votes.[42]

First, there is overwhelming support for company directors in director election proposals. As shown in Figure 6 below, 94% of director elections were won by a margin greater than 30%, and fewer than 1% of director votes were determined by a margin of less than 10%. Next, 86% of say-on-pay votes were won by a margin greater than 30%, and 96% were won by a margin greater than 10%. Likewise, 98% of M&A-related votes were won by a margin greater than 30%.[43]

FIGURE 6: SUPPORT FOR MANAGEMENT PROPOSALS[44]



The rationale for the use of the 30% and 10% thresholds is that according to several commentators, the three large index fund managers are providing a "swing vote"[45]—or will be soon. However, these charts demonstrate

42. For the estimates of the total U.S. ballot items, see BlackRock, 2019 Investment Stewardship Annual Report 24 (2019), https://www.blackrock.com/corporate/literature/publication/blk-annual-stewardship-report-2019.pdf [https://perma.cc/Q6K3-2LEB] [hereinafter BlackRock, 2019 Investment Stewardship Report]. For estimates of the number of shareholder proposals and say-on-pay votes, see Voting Database, Proxy Insight, https://www.proxyinsight.com [hereinafter Proxy Insight, Voting Database] (data as of June 30, 2019). Calculations are based on voting information from Proxy Insight's voting database based on the SEC Form N-PX filings for Russell 3000 companies for the reporting period of July 1, 2018 through June 30, 2019.

43. These calculations are based on ownership data from the FactSet Research System Ownership Database using the SEC Form N-PX filings for Russell 3000 companies for the period July 1, 2018 to June 30, 2019. FactSet, Ownership Database, supra note 28 (data as of June 30, 2019).

44. Id.

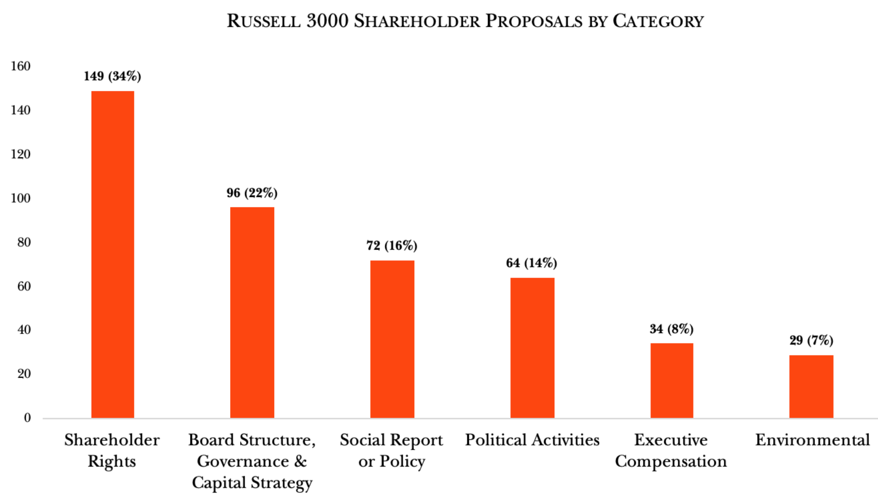
45. See, e.g., Jessica DiNapoli & Saqib Iqbal Adhmed, BlackRock Takes Aim at CEOs Serving on Other Companies' Boards, Reuters (Aug. 27, 2019), https://www.reuters.com/article/us-blackrock-stewardship/blackrock-takes-aim-at-ceos-serving-on-other-companies-boards-idUSKCN1VH16M [https://perma.cc/R34U-VGPM] ("BlackRock is an influential force in how boards of directors operate, and can swing votes in important corporate elections."); Jonathan Litt, Why All Shareholder Voices, Even Passive Ones, Matter, N.Y. Times (July 20, 2017), https://www.nytimes.com/2017/07/20/business/dealbook/why-all-shareholder-voices-even-passive-ones-matter.html [https://perma.cc/S4MB-QA2D] ("[I]ndex funds like

that no individual manager has anything close to a swing-vote type of influence on director elections, say-on-pay, or M&A situations. Even if you assume (i) that these firms grow to each control 10% of the equity votes—which is more than twice their typical voting power today in large cap companies—and (ii) that these firms all vote the same—which their voting records show that they don't—the vast majority of votes would still not be influenced by this theoretical voting bloc.

VII. SHAREHOLDER PROPOSALS ADDRESS "G", "E," AND "S" ISSUES

Shareholder proposals represent just under 2% of the ballot items in the United States, but they are the source of virtually all of the controversy, as evidenced by the proposal topics shown in Figure 7 below. Unlike management proposals, 18% of shareholder proposals are determined by a margin under 10%, and 70% are determined by a margin under 30%.

FIGURE 7: BREAKDOWN OF SHAREHOLDER PROPOSALS[46]



Over 50% of shareholder proposals voted on address governance issues, such as the separation of Chairman and CEO, the desire to modify

State Street, Vanguard and BlackRock now have in so many companies . . . become the swing votes in proxy fights, determining whether an activist's nominees or the company's nominees get elected to the board."); Eli Kasargod-Staub, Climate in the Boardroom, Harvard Law Sch. Forum on Corp. Governance (Oct. 7, 2019), https://corpgov.law.harvard.edu/2019/10/07/climate-in-the-boardroom [https://perma.cc/8RUH-T9ML] (stating that of twenty-eight "critical climate resolutions" in 2019, sixteen would have passed had both BlackRock and Vanguard supported them).

46. Calculations are based on voting information from Proxy Insight's voting database based on the SEC Form N-PX filings for Russell 3000 companies for the reporting period of July 1, 2018 through June 30, 2019. Proxy Insight, Voting Database, supra note 42 (data as of June 30, 2019).

dual-share class structures, or proxy access (i.e., the right of shareholders to nominate directors on the management's slate).[47]

In recognition of the growing influence of proxy advisors in this area, the SEC recently released new guidance related to proxy advisor recommendations and investment managers' use of proxy advisor recommendations in their voting on shareholder proposals.[48] Briefly put, the SEC will be holding proxy advisors to a higher standard than before, indicating the importance of the quality and accuracy of data in proxy advisors' recommendations. Likewise, the SEC expects asset managers to do proper due diligence on the proxy advisors and on the shareholder proposals.[49] We are supportive of this guidance as it largely reflects our current practices.

On the other hand, both issuers and investors have expressed concern with the recent SEC guidance on Rule 14a-8 no-action requests.[50] The SEC has indicated that in certain circumstances staff will decline to provide no-action letters on the inclusion of shareholder proposals in proxy statements.[51] Unless ISS and Glass Lewis modify their policies, this may lead to unintended consequences, as both ISS and Glass Lewis automatically recommend voting against directors if a company excludes a proposal without SEC staff response or a court order. On November 4, 2019, Glass Lewis announced that it would not be changing this policy.[52]

And in November 2019, the SEC voted on a proposed rule which would require proxy advisors to allow issuers to correct incorrect information in their recommendations.[53] In addition, the Commission proposed changes to rules around shareholder proposal eligibility requirements, proposing to raise the submission and resubmission thresholds for a given shareholder proposal.[54] In 2018, we participated in the SEC roundtable on

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47. Id.

48. See Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, 84 Fed. Reg. 47,420 (Sept. 10, 2019).

49. See id. at 47,422–26.

50. See Announcement Regarding Rule 14a-8 No-Action Requests, SEC, https://www.sec.gov/corpfin/announcement/announcement-rule-14a-8-no-action-requests [https://perma.cc/GCX6-DDKM] (last modified Sept. 6, 2019) (explaining that "the staff may respond orally instead of in writing" and that "[i]f the staff declines to state a view on any particular request, the interested parties should not interpret that position as indicating that the proposal must be included").

51. Id.

52. See 2020 Policy Guideline Updates—U.S., U.K., Canada, Europe, China, and More, Glass Lewis (Nov. 4, 2019), https://www.glasslewis.com/2020-policy-guideline-updates-u-s-u-k-canada-europe-china-and-more [https://perma.cc/G72V-SHW8].

53. See Press Release, SEC, SEC Proposes Rule Amendments to Improve Accuracy and Transparency of Proxy Voting Advice (Nov. 5, 2019), https://www.sec.gov/news/press-release/2019-231 [https://perma.cc/S36B-X5AM].

54. See Press Release, SEC, SEC Proposes Amendments to Modernize Shareholder Proposal Rule (Nov. 5, 2019), https://www.sec.gov/news/press-release/2019-232 [https://perma.cc/H5L3-X6JT].

the proxy process and submitted a comment letter.[55] In our letter, we identified four key principles: (i) transparency, (ii) accurate data, (iii) shareholder rights, and (iv) the use of technology.[56] We look forward to reviewing the proposed rule, using these principles as our guide.

VIII. VOTING VARIES SIGNIFICANTLY ACROSS MANAGERS

Historically, dissecting manager voting records had been complicated. However, new services like Proxy Insight, MSCI, and other data analysis tools have become available in the past few years to make this easier. Plus, many managers voluntarily disclose summary voting statistics on their respective websites, which are available for free and provide significant insights.

BlackRock's approach to shareholder proposals is to assess the company's current disclosures and how the company is managing the issue that a given proposal raises. As just discussed, some shareholder proposals address environmental and social (E&S) issues. Often, it is the case that management is already addressing a particular issue or that an issue may not be material to the company's long-term sustainable performance. At BlackRock, we use engagement as part of our process to make informed votes.

While it's easy to count votes in support of shareholder proposals and rank firms based on such data, doing so definitely does not provide the whole story. For example, in the past year, BlackRock engaged globally with over 1,400 individual companies on a wide range of ESG issues.[57] By comparison, there were 165 shareholder proposals in the United States on E&S issues in the past proxy season, which represents less than 1% of all ballot items.[58] And 37% of E&S proposals addressed political activities disclosure, where much of the information being sought is already publicly available on government websites.[59]

Importantly, in many cases, we have seen companies improve on ESG issues through engagements over time. In 2018, BlackRock updated its proxy voting guidelines on board diversity and sent letters sharing our position on this topic to about 30% of the Russell 1000. We used the lack of at least two women on their respective boards as a flag to have a deeper

55. See generally Letter from Barbara Novick, Vice Chairman, BlackRock & Ray Cameron, Managing Dir., BlackRock, to Brent J. Fields, Sec'y, SEC (Nov. 16, 2018), https://www.blackrock.com/corporate/literature/publication/sec-roundtable-proxy-process-111618.pdf [https://perma.cc/JD8L-TZNX] (offering recommendations for restructuring the proxy process).

56. Id. at 2–5.

57. BlackRock, 2019 Investment Stewardship Report, supra note 42, at 4.

58. Id. at 24 (noting a total of 31,570 proposals voted on in the United States during the 2019 proxy season); Proxy Insight, Voting Database, supra note 42 (using the SEC Form N-PX filings for Russell 3000 companies for the reporting period of July 1, 2018 through June 30, 2019).

59. Proxy Insight, Voting Database, supra note 42 (using the SEC Form N-PX filings for Russell 3000 companies for the reporting period of July 1, 2018 through June 30, 2019).

discussion on their approach to board diversity. We have been pleased to see that over 120 companies added a female board member just in 2019.[60] Likewise, BlackRock engaged with over 200 companies on climate risk, and we have seen just over a 60% increase in organizations embracing the Task Force on Climate-Related Financial Disclosures (TCFD) reporting framework.[61] Of course, these results reflect the collective voices of multiple shareholders.

Once again, shareholder proposal support is an area where simple statistics can be misleading. In Figure 8, we observe a correlation between size of manager by equity AUM and voting patterns. Asset managers with stewardship responsibility for larger amounts of equity assets are clearly expressing views that are independent of ISS's proxy advisor recommendations and of each other. Some managers voted "FOR" shareholder proposals more than 75% of the time, which exceeded even ISS's recommendations.

The subset of just E&S votes shows a similar pattern, with these smaller managers by equity AUM voting "FOR" on more than 83% of the proposals, exceeding ISS's recommendations in favor of 81% on E&S proposals.[62]

FIGURE 8: SHAREHOLDER PROPOSAL SUPPORT[63]

Support for Russell 3000 Shareholder Proposals (2019 N-PX Year)

Name	Equity AUM ($ M)	Total Votes	Votes 'FOR'	% 'FOR'	ISS Match Count	% ISS Match
BNP Paribas Asset Management	$86,237.97	233	196	84%	158	**68%**
Pacific Investment Management Co. (PIMCO)	$38,306.79	330	267	81%	299	**91%**
UBS Global Asset Management	$335,865.26	420	331	79%	329	**78%**
AXA Investment Managers	$75,085.92	355	275	77%	298	**84%**
Legal & General Investment Management	$310,394.40	344	264	77%	272	**79%**
Prudential Global Investment Management	$327,790.02	75	56	75%	73	**97%**
ISS	N/A	444	332	75%	444	**100%**
Nuveen Asset Management LLC	$306,122.99	315	216	69%	307	**97%**
Invesco Advisers, Inc.	$439,660.98	403	220	55%	273	**68%**
Glass Lewis	N/A	341	159	47%	226	**66%**
Franklin Templeton Investments	$266,441.78	360	155	43%	196	**54%**
Natixis Global Asset Management	$221,869.90	166	71	43%	89	**54%**
BNY Mellon	$396,060.00	432	177	41%	283	**66%**
Goldman Sachs Asset Management LP	$300,690.00	437	149	34%	253	**58%**
SSgA Funds Management, Inc. (State Street)	$1,607,230.08	444	129	29%	218	**49%**
Northern Trust Investments	$478,047.96	444	124	28%	226	**51%**
T. Rowe Price Associates, Inc.	$720,762.70	444	115	26%	195	**44%**
JPMorgan Investment Management, Inc.	$489,504.71	429	88	21%	195	**45%**
Fidelity Management & Research Co. (FMR)	$1,357,830.32	406	68	17%	163	**40%**
Vanguard Group, Inc.	$3,338,495.15	441	76	17%	187	**42%**
BlackRock	$2,993,884.82	444	67	15%	171	**39%**

60. BlackRock, 2019 Investment Stewardship Report, supra note 42, at 12.

61. Id. at 16, 18.

62. Proxy Insight, Voting Database, supra note 42 (using the SEC Form N-PX filings for Russell 3000 companies for the reporting period of July 1, 2018 through June 30, 2019).

63. AUM derived from P&I, supra note 8 (data as of Dec. 31, 2018). Voting records are based on voting information from Proxy Insight's voting database based on the SEC Form N-PX filings for the reporting period of July 1, 2018 through June 30, 2019. Proxy Insight, Voting Database, supra note 42 (data as of June 30, 2019). For Natixis Global Asset Management AUM, see Natixis, Registration Document and Annual Financial Report 227 (2018), https://www.natixis.com/natixis/upload/docs/application/pdf/2019-03/natixis_registration_document_2018.pdf [https://perma.cc/X9DQ-3ALM]. The total universe includes 444 shareholder proposals. Glass Lewis' Total Votes is underrepresented due to its data redistribution

We encourage academics to study these data to explain the disparity in voting. Some questions to consider include how much respective managers rely on proxy advisors' recommendations, whether some managers do additional research leading them to either support or oppose shareholder proposals, or whether there are other factors driving managers' voting.

Regardless of the rationale for these voting outcomes, one of the most important takeaways is to recognize that different asset managers vote differently, and rarely are the large asset managers capable of being a swing vote.

IX. Factoring in Dual-share Class Structures

The subject of proxy voting has a touchpoint with another important corporate governance issue: capital formation. Some commentators have cited the burdens of being a public company—including the proliferation of shareholder proposals and the fear of activist investors, among others—as a deterrent to going public.[64]

SEC Chairman Jay Clayton and others have pointed out that the number of public companies is shrinking.[65] In 2018, there were 4,025 public companies, down from over 5,100 in 2007 and over 8,000 in 1996.[66] Further, the number of initial public offerings (IPOs) is less than the high-water mark, albeit that number may have been artificially high.[67] One concern expressed is that companies are going public later, precluding

constraint. Per Proxy Insight, Prudential Global Investment Management's Total Votes may be low since it outsources management of equities. Proxy Insight, Voting Database, supra note 42.

64. See Adena Friedman, Opinion, Nasdaq's Blueprint for a New Era of Trading, Wall St. J. (May 3, 2017), https://www.wsj.com/articles/nasdaqs-blueprint-for-a-new-era-of-trading-1493852688 (on file with the *Columbia Law Review*) (noting that "a small group of agitators . . . flood public companies with agenda-driven proposals"); Jay Clayton, Chairman, SEC, Remarks at the Economic Club of New York (July 12, 2017), https://www.sec.gov/news/speech/remarks-economic-club-new-york [https://perma.cc/E7GW-EHQY] ("[I]ncreased disclosure and other burdens may render alternatives for raising capital, such as the private markets, increasingly attractive to companies that only a decade ago would have been all but certain candidates for the public markets."). But see Jonas Kron, Shareholder Resolutions and IPOs, Harvard Law Sch. Forum on Corp. Governance (Jan. 5, 2019), https://corpgov.law.harvard.edu/2019/01/05/shareholder-resolutions-and-ipos [https://perma.cc/5MKK-MJ6C] ("[T]here is no evidence to think shareholder proposals have any impact on companies' decisions to launch an IPO.").

65. See Clayton, supra note 64.

66. Id. at n.7; Opinion, Where Have All the Public Companies Gone?, Bloomberg (Apr. 9, 2018), https://www.bloomberg.com/opinion/articles/2018-04-09/where-have-all-the-u-s-public-companies-gone [https://perma.cc/7PGG-CARF].

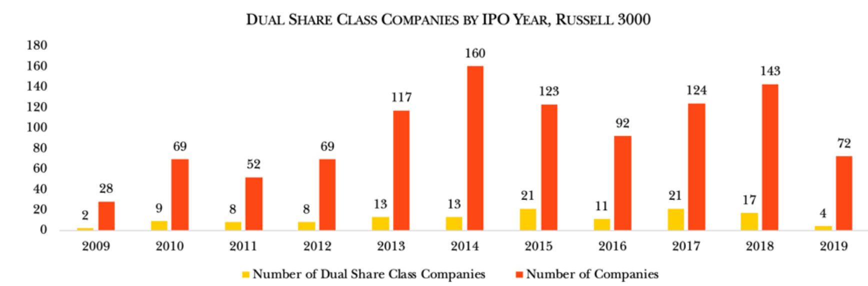
67. See Jay R. Ritter, Initial Public Offerings: Updated Statistics 40 tbl.15 (2017), https://site.warrington.ufl.edu/ritter/files/2017/08/IPOs2016Statistics.pdf [https://perma.cc/DLX4-2JAL].

retail investors from participating in earlier stages of growth.[68] And, of course, the abundance of private capital allows companies to stay private longer, making the public–private tradeoff more challenging.

As a response to deterrents against going public, some companies have come to market with dual-share class structures. These cases range from situations where a founder has weighted voting rights while public shareholders have less, to the extreme case of Snap Inc., where public shareholders have no voting rights.[69] This increase in dual-share class structures raises a new set of issues.

FIGURE 9: QUANTIFYING DUAL-SHARE CLASS COMPANIES[70]

Outstanding Dual-Share Class Companies		
Exchange	**Number of Dual-Share Class Companies**	**Number with Sunset Provisions**
NASDAQ	135 out of 1,516	8 have sunset provisions
NYSE	176 out of 1,419	9 have sunset provisions



The Council of Institutional Investors (CII) and the International Corporate Governance Network (ICGN) have each weighed in, expressing concerns about the implications for corporate governance and shareholder rights that dual-share class structures may have.[71] They cite the potential for weak corporate governance and diminished accountability to

68. See Ajay Chopra, With So Much Late-Stage Money Available, Why Are Tech Companies Going Public Now?, TechCrunch (July 12, 2019), https://techcrunch.com/2019/07/12/with-so-much-late-stage-money-available-why-are-tech-companies-going-public-now [https://perma.cc/75L4-RFW6].

69. See Dual-Class Stock, Council of Institutional Inv'rs, https://www.cii.org/dualclass_stock [https://perma.cc/GXY3-3DK9] (last visited Jan. 30, 2020).

70. Council of Institutional Inv'rs, Dual Class Companies List (2019), https://www.cii.org/files/FINAL%20format%20Dual%20Class%20List%209-27-19.pdf (on file with the *Columbia Law Review*); Bloomberg LP, https://www.bloomberg.com/professional (data as of Sept. 27, 2019). These calculations are based on ownership data from the FactSet Research Systems Ownership Database. FactSet, Ownership Database, supra note 28 (data as of Sept. 27, 2019).

71. See Int'l Corp. Governance Network, ICGN Viewpoint: Differential Share Ownership Structures: Mitigating Private Benefits of Control at the Expense of Minority Shareholders 2–3 (2017), https://www.icgn.org/sites/default/files/2.%20ICGN%20Viewpoint%20differential%20share%20ownership_1.pdf [https://perma.cc/487E-EUXD]; Dual-Class Stock, supra note 69.

shareholders and ask the stock exchanges to modify their listing standards to create a negative incentive against these governance structures.[72]

In February 2018, the SEC's Investment Advisory Committee recommended that the SEC strengthen disclosures of the risks associated with dual-share class companies.[73] Rick Fleming, the SEC's Investor Advocate, recently gave a speech at the ICGN conference, where he noted concerns with self-dealing, "insular group-think," and poor controls, among a list of issues he associated with "unchecked corporate control" with dual-share class companies.[74]

BlackRock has written on the topic of dual-share class structures several times, starting from the perspective of finding a solution that balances the needs of issuers and the rights of investors.[75] BlackRock recognizes that when companies are establishing themselves in the public markets, unequal voting rights may allow founders to focus on long-term strategy and performance without exposure to outside pressures.[76] Yet benefits dissipate over time, and dual-share class structures challenge investor rights. We believe the benefits do not outweigh the loss of investor protections, over extended periods of time.

One possible solution is to require a sunset provision for dual-share class structures. The listing exchange of such a company could require they automatically revert to one-share-one-vote five to seven years after going public. Alternatively, the respective listing exchanges could require the company put the future of its dual-share class structure to a shareholder vote—between years five and seven of being public—where all minority shareholders would be given an equal vote to decide whether or not to extend the structure.

BlackRock recommends additional safeguards be included. These include specifying "trigger events"—such as a founder retiring, passing away, or leaving for another reason—where the shares would automatically

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72. See Int'l Corp. Governance Network, supra note 71; Dual-Class Stock, supra note 69.

73. Inv. Advisory Comm., SEC, Recommendation of the Investor as Owner Subcommittee: Dual Class and Other Entrenching Governance Structures in Public Companies 6–7 (2018), https://www.sec.gov/spotlight/investor-advisory-committee-2012/iac030818-investor-as-owner-subcommittee-recommendation.pdf [https://perma.cc/5AL6-AQHF].

74. Rick Fleming, Inv'r Advocate, SEC, Speech at ICGN Miami Conference: Dual-Class Shares: A Recipe for Disaster (Oct. 15, 2019), https://www.sec.gov/news/speech/fleming-dual-class-shares-recipe-disaster [https://perma.cc/L8TF-9478].

75. See, e.g., BlackRock, Key Considerations in the Debate on Differentiated Voting Rights 3, https://www.blackrock.com/corporate/literature/whitepaper/blackrock-the-debate-on-differentiated-voting-rights.pdf [https://perma.cc/P696-M9NY] (last visited Jan. 31, 2020) (proposing recommendations that would "reinforce long-termism by corporate governance actors, without creating an uneven playing field between shareholders").

76. See id.; Letter from Barbara Novick, Vice Chairman, BlackRock, to Baer Pettit, President, MSCI, Inc. (Apr. 19, 2018), https://www.blackrock.com/corporate/literature/publication/open-letter-treatment-of-unequal-voting-structures-msci-equity-indexes-041918.pdf [https://perma.cc/Y6CX-MV3R].

revert to one-share-one-vote. Likewise, the transfer of ownership to a person or entity that is not actively involved in running the company should trigger one-share-one-vote.

As academics, regulators, and practitioners alike contemplate corporate governance and investment stewardship today, they need to consider this growing phenomenon of dual-share class companies.

X. THE COMMON OWNERSHIP THEORY IS FLAWED

Given the number of academic forums and papers that have focused on the theory of common ownership and the impact the proposed remedies would have on corporate governance, I would be remiss not to address some of the flaws in this theory in these remarks.

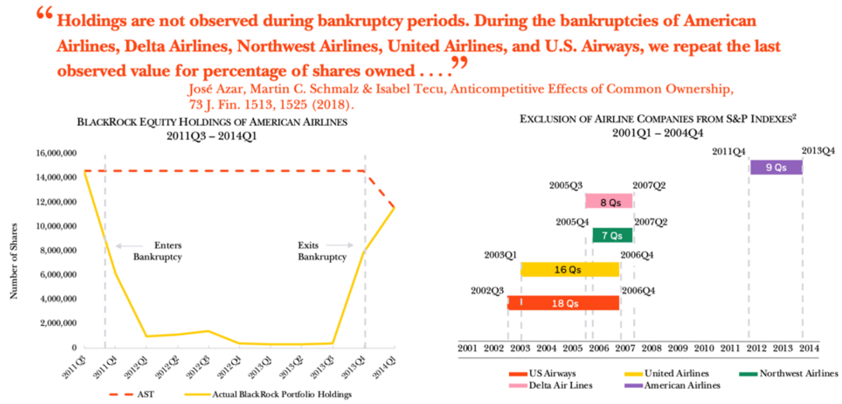
At the most basic level, it is disturbing to note that the data used in the seminal common ownership paper—generally referred to as "the Airlines Paper"—are incorrect. The authors of the paper observed that the dataset of asset managers' holdings had "zeros" during periods of bankruptcy.[77] Not understanding why, they chose to override these zeros by repeating the last observed value of the respective asset managers' holdings prior to the bankruptcy periods.[78] However, when a company enters bankruptcy, its stock is delisted from the exchanges. Subsequently, when a company is delisted, index providers remove the stock from their indexes, prompting index fund managers to sell the stock from their portfolios. Hence, the zeros found in the Airlines Paper's dataset were correct.[79]

77. See José Azar, Martin C. Schmalz & Isabel Tecu, Anticompetitive Effects of Common Ownership, 73 J. Fin. 1513, 1525 (2018) ("During the bankruptcies of American Airlines, Delta Airlines, Northwest Airlines, United Airlines, and U.S. Airways, we repeat the last observed value for percentage of shares owned . . . .").

78. Id.

79. See BlackRock, Policy Spotlight: Common Ownership Data Is Incorrect 2 (2019), https://www.blackrock.com/corporate/literature/whitepaper/policy-spotlight-common-ownership-data-is-incorrect-january-2019.pdf [https://perma.cc/2RDS-AMCP].

FIGURE 10: COMMON OWNERSHIP DATA ARE INCORRECT[80]



In the example shown, the discrepancy is in the order of millions of shares, reflecting the difference between an actual ownership of less than 0.1% versus the authors' assumption of 4.25%. Since five out of seven of the airlines in the study went through bankruptcies—which is an interesting point in itself—this is a significant data error that affected twenty-eight out of fifty-six quarters in the study period, grossly misrepresenting the ownership of each of the large index fund managers.

In addition to the data being incorrect, a host of academic papers now challenge key aspects of the theory, including its treatment of the "control" in bankruptcy, its conflation of financial incentives of asset owners and asset managers, and the appropriateness of its use of the modified Herfindahl Hirschmann Index (MHHI) as a measure of common ownership.[81]

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80. See Common Ownership, BlackRock, https://www.blackrock.com/corporate/literature/publication/data-package-replicating-sensitivities-ast-011419.zip (on file with the *Columbia Law Review*) (last visited Mar. 26, 2020) (providing the data used to replicate the Airlines Paper). Additional data based on calculations by BlackRock, based on Thomson Reuters Spectrum, SEC filings, and S&P announcements. The "Airlines Paper" line is sourced from Thomson Reuters Spectrum and José Azar, Martin C. Schmalz, and Isabel Tecu's manually collected SEC Form 13F filings. Share counts are aggregated across separate BlackRock entities. Shares from Q3 2011 are "forward-filled" for the bankruptcy period. The "Actual BlackRock Portfolio Holdings" line for Q4 2011–Q4 2013 is sourced from BlackRock's internal data systems and includes shares in American Airlines that would be reported in SEC Form 13F by any of BlackRock's entities. For quarters outside of the bankruptcy period, the values of the "Actual BlackRock Portfolio Holdings" line are the same as the "Airlines Paper" line.

81. Pablo Florian & Anne Gron, AlixPartners, A Simple Index of Common Ownership Is Not So Simple 1–2 (2019), https://www.alixpartners.com/media/12590/ap_a_simple_index_of_common_ownership_may_2019.pdf [https://perma.cc/QR5W-AECX] (cautioning against the use of MHHI as a measure of common ownership); Erik Gilje, Todd A. Gormley & Doron Levit, Who's Paying Attention? Measuring Common Ownership and Its Impact on Managerial Incentives, J. Fin. Econ. (forthcoming) (manuscript at 3–6), https://ssrn.com/abstract=3165574 (on file with the *Columbia Law Review*) (analyzing the impact of common ownership on managerial incentives, and countering scholarship that fails to account for

Given numerous issues with the underlying research, it is quite surprising to see anyone suggest pursuing policy measures, especially measures that would be harmful to investors and disruptive to the functioning of the real economy. As with dual-share class structures, the corporate governance and investment stewardship implications of this debate must be considered.

XI. UNDERSTANDING THE REGULATORY LANDSCAPE

I would like to bring this discussion back to the practitioner's perspective on investment stewardship—what it is and what it is not—and how this is informed by the regulatory environment at present. While many people have ideas of what they would like investment stewardship to be, it is useful to start with an understanding of the relevant rules, which have been established by the SEC, Department of Labor (DoL), and FTC.

Both the SEC and the DoL have weighed in on issuing voting guidance. In 2003, the SEC issued its proxy voting rule under the Advisers Act, outlining that investment advisers are required to adopt and implement policies to ensure they vote proxies according to their clients' best interest.[82] Then in 2014, SEC Staff Legal Bulletin 20 clarified these duties.[83] In the recent guidance I mentioned earlier, the SEC clarified how managers can fulfill their duty to vote in their clients' best interest, and how the scope of voting authority can be shaped (including the use of proxy advisors or not voting) through disclosure and informed consent.[84]

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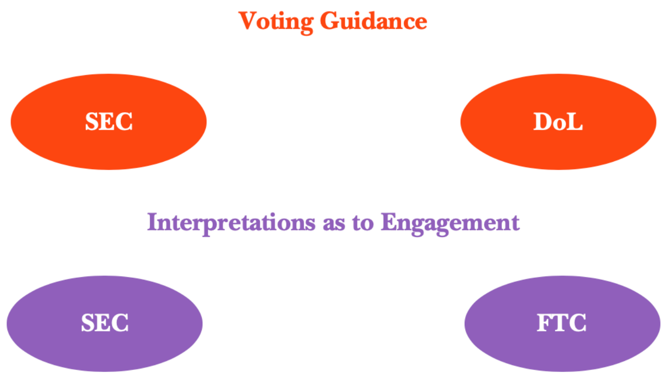
investor inattention); Barbara Novick, Vice Chairman, Blackrock, Revised and Extended Remarks at Federal Trade Commission Hearing #8: Competition and Consumer Protection in the 21st Century 3 (Dec. 6, 2018), https://www.blackrock.com/corporate/literature/publication/remarks-barbara-novick-ftc-hearing-8-competition-consumer-protection-21st-century-120618.pdf [https://perma.cc/WF9D-9EKB] ("The often-cited paper *Anti-Competitive Effects of Common Ownership* assumes that managers continue to hold airlines during periods of bankruptcy. The reality is quite different.").

82. See Proxy Voting by Investment Advisers, 68 Fed. Reg. 6,585 (Feb. 7, 2003), https://www.govinfo.gov/content/pkg/FR-2003-02-07/pdf/03-2952.pdf [https://perma.cc/PM29-PLZL].

83. See SEC Staff Legal Bulletin No. 20, Proxy Voting: Proxy Voting Responsibilities of Investment Advisers and Availability of Exemptions from the Proxy Rules for Proxy Advisory Firms (June 30, 2014), https://www.sec.gov/interps/legal/cfslb20.htm [https://perma.cc/ZFH2-MPMY].

84. See Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, 84 Fed. Reg. 47,420 (Sept. 10, 2019).

FIGURE 11: THE STEWARDSHIP REGULATORY LANDSCAPE



While the SEC has oversight of mutual funds, the DoL has oversight of ERISA assets. In 1988, the DoL first indicated in the Avon Letter that voting is a plan asset, meaning that asset managers should generally vote shares as part of their fiduciary duty.[85] This letter was followed with a series of interpretive guidance in 1994, 2008, 2016, and 2018, largely reaffirming this position.[86]

Next, both the SEC and FTC have offered interpretations concerning engagement with companies. The SEC requires Schedule 13D filings when a shareholder reaches a 5% threshold of beneficial ownership in a company and has the intent to change or influence control of the company.[87] Recognizing that this is intended for activist situations, the SEC allows investors to instead file Schedule 13G when the shareholder is holding with passive intent.[88] 13G filings permit a beneficial owner to engage with management on governance, social, and public interest topics as part of the investor's broad efforts to promote good practices across its portfolio investments. Eligibility to file Schedule 13G is a key reason why index fund managers do not coordinate voting of proxies, as doing so would require they file Schedule 13D instead.

The FTC (together with the Department of Justice) has jurisdiction over implementation of the Hart–Scott–Rodino (HSR) Act, which sets notification

85. See Letter from Alan D. Lebowitz, Deputy Assistant Sec'y, U.S. Dep't of Labor, to Helmuth Fandl, Chairman, Ret. Bd., Avon Prods., Inc. (Feb. 23, 1988), 1988 ERISA LEXIS 19.

86. See Interpretive Bulletins Relating to the Employee Retirement Income Security Act of 1974, 59 Fed. Reg. 38,863 (July 29, 1994) (codified at 29 C.F.R. § 2509 (2019)); Interpretive Bulletin Relating to Exercise of Shareholder Rights, 73 Fed. Reg. 61,731 (Oct. 17, 2008) (codified at 29 C.F.R. § 2509.2016-01 (2019)); Interpretive Bulletin Relating to the Exercise of Shareholder Rights, 81 Fed. Reg. 95,879 (Dec. 29, 2016) (codified at 29 C.F.R. § 2509.2016-01 (2019)); Field Assistance Bulletin No. 2018-01, U.S. Dep't of Labor (Apr. 23, 2018), https://www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/field-assistance-bulletins/2018-01 [https://perma.cc/SPH4-9BS4].

87. See 17 C.F.R. § 240.13d-1(a) (2019).

88. Id. § 240.13d-1(b)(1).

requirements—including filing and a mandatory thirty-day waiting period—for mergers, as well as the acquisition of voting shares of a company above a certain threshold of ownership.[89] Similar to the SEC rules, HSR has an "investment only exemption" to these requirements, in cases where shares are acquired for investment purposes only.[90]

XII. BLACKROCK INVESTMENT STEWARDSHIP

At BlackRock, Investment Stewardship is part of our investment function, applying to both active and passive funds. Fifty percent of the assets we manage are equity assets, and of these, 92% are index and 8% active.[91] The index assets closely track market indexes created by others, which means whether we like a company or not—including its management, its strategy, and its products—we will still hold it in these portfolios. This is quite different than actively managed portfolios that can express displeasure by voting with their feet and selling the stock. Given this long-term perspective, our investment stewardship activities are focused on maximizing long-term shareholder value.

BlackRock engages directly with companies to better understand their position and strategy on material corporate governance matters. BlackRock Investment Stewardship is now forty-five persons strong—the largest and most global team in the industry—which reflects our commitment to deeper, more meaningful, and more productive engagements. These individuals are strategically located in the United States, Europe, Hong Kong, Tokyo, Singapore, and Sydney to be closer to the markets and the companies we cover.

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89. Joseph J. Simons, FTC & Makan Delrahim, DOJ, Hart–Scott–Rodino Annual Report, FTC 1, 4–5 (2018), https://www.ftc.gov/system/files/documents/reports/federal-trade-commission-bureau-competition-department-justice-antitrust-division-hart-scott-rodino/fy18hsrreport.pdf [https://perma.cc/73F2-EWZX].

90. See Debbie Feinstein, Ken Libby & Jennifer Lee, "Investment-Only" Means Just That, FTC (Aug. 24, 2015), https://www.ftc.gov/news-events/blogs/competition-matters/2015/08/investment-only-means-just [https://perma.cc/CK9G-BXRV].

91. See BlackRock, BlackRock Reports Third Quarter 2019 Diluted EPS of $7.15, at 5 (2019), https://ir.blackrock.com/files/doc_news/archive/4a1e3da1-e31d-4295-a0e8-96eed78aeef2.pdf [https://perma.cc/Q9V7-DFRB].

FIGURE 12: QUANTIFYING BLACKROCK'S 2019 STEWARDSHIP ACTIVITIES

1,458 total global companies engaged

2,050 total global engagements

155,131 total global ballot items

16,124 total global meetings voted

Voted "FOR" a dissident candidate in **40%** of U.S. proxy contests

Supported **28%** of dissident candidates at U.S. proxy contests

In the 2018–2019 N-PX year, BlackRock Investment Stewardship held 2,050 engagements with 1,458 companies based in forty-two markets, and we voted on 155,131 global ballot items over 16,124 global meetings.[92]

While some people think index fund managers "always support" one side, the data shows sometimes we support dissidents and sometimes we don't. For example, during this same period, we voted "FOR" a dissident candidate in 40% of U.S. proxy contests (i.e., four out of ten proxy contests), and we supported 28% of dissident candidates (i.e., eight out of twenty-nine seats).[93] Think of this as "the law of small numbers," given the small sample size.

Simply put, by engaging directly with companies and other interested parties, we develop a better understanding of the companies and make more informed voting decisions.

XIII. COMMITMENT TO TRANSPARENCY

In September 2019, when I participated in the Harvard–PIFS roundtable, "The Rise of Passive Investing: Corporate Governance, Systemic Risk and Index Construction,"[94] Lucian Bebchuk asserted that index fund managers are not sufficiently vocal on policy issues, and John Coates suggested that asset managers work too secretively. I took exception with both statements then, and I will take the opportunity today to elaborate.

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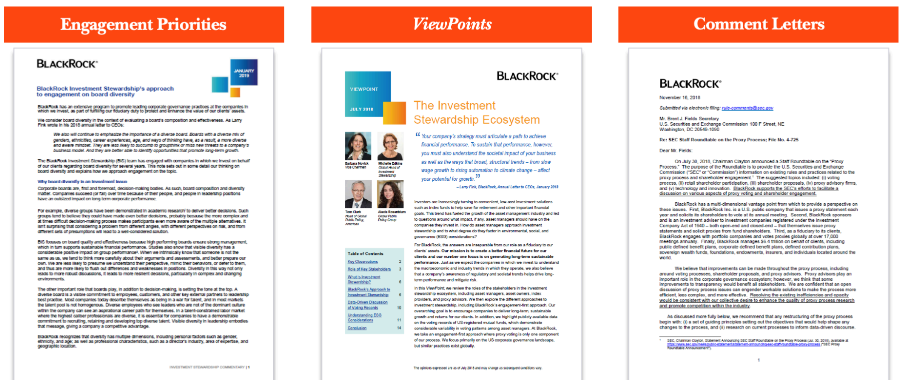
92. BlackRock, 2019 Investment Stewardship Report, supra note 42, at 5.

93. Id. at 23–24.

94. The conference occurred on September 27, 2019. The Rise of Passive Investing: Corporate Governance, Systemic Risk and Index Construction, Program on Int'l Fin. Sys., https://www.pifsinternational.org/special-events/past-special-events/the-rise-of-passive-investing-corporate-governance-systemic-risk-and-index-construction [https://perma.cc/RL7U-2JEN] (last visited February 21, 2020).

BlackRock is committed to providing a high level of transparency around our investment stewardship activities. On the BlackRock Investment Stewardship site, we have posted approximately seventy documents, including engagement priorities, voting guidelines for multiple markets, commentaries on special topics, quarterly and annual reports, voting data, whitepapers, and comment letters.[95] And that is before counting market structure, investment products, or other topics that we address on our Global Public Policy site.[96]

FIGURE 13: BLACKROCK STEWARDSHIP PUBLICATIONS



For companies and clients, this means they can easily see the issues we are focused on. To put this in perspective, here are the engagement priorities for 2019:[97]

1. Governance—board quality and effectiveness
2. Corporate strategy and capital allocation
3. Compensation that promotes long-termism
4. Environmental risks and opportunities
5. Human capital management

95. Investment Stewardship, BlackRock, https://www.blackrock.com/corporate/about-us/investment-stewardship [https://perma.cc/P9EJ-97GT] (last visited Jan. 31, 2020).

96. See Public Policy, BlackRock, https://www.blackrock.com/corporate/insights/public-policy (on file with the *Columbia Law Review*) (last visited Jan. 31, 2020); see also, e.g., BlackRock Inv. Inst., Getting Physical: Scenario Analysis for Assessing Climate-Related Risks 2 (2019), https://www.blackrock.com/corporate/literature/whitepaper/bii-physical-climate-risks-april-2019.pdf [https://perma.cc/ARN5-U32Y]; Barbara Novick, Kate Fulton, Martin Parkes, Rachel Barry, Joanna Cound, Stephen Fisher, Samantha DeZur & Anahide Pilibossian, The Decade of Financial Regulatory Reform: 2009 to 2019, at 1 (2020), https://www.blackrock.com/corporate/literature/whitepaper/viewpoint-decade-of-financial-regulatory-reform-2009-to-2019.pdf [https://perma.cc/57D5-HF9T].

97. BlackRock, BlackRock Investment Stewardship Engagement Priorities for 2019, at 2 (2019), https://www.blackrock.com/corporate/literature/publication/blk-stewardship-priorities-final.pdf [https://perma.cc/8WEK-TZQ4] [hereinafter, Blackrock, Investment Stewardship Engagement Priorities].

Each of our engagement priorities is explained in more detail on our site, including, in many cases, examples of our engagement questions. Likewise, the quarterly and annual reports we publish provide insights into our engagements with companies and our voting statistics.[98] Our clients—the end investors—find these reports useful in understanding and monitoring our investment stewardship activities. In recognition of our efforts, in 2018, BlackRock won ICGN's Global Stewardship Disclosure Award for asset managers, and that was before we enhanced our website.[99]

I encourage you to look at our materials as well as those you can find on Vanguard, State Street, TIAA, and J.P. Morgan Asset Management's respective websites.[100] There is a wealth of information available if you want to learn more about investment stewardship.

XIV. PROFITS AND PURPOSE ARE INEXTRICABLY LINKED

BlackRock's stewardship activities play a critical part in delivering what we see as our corporate purpose: delivering financial well-being to our clients. Sometimes we get into discussions about "Friedman" versus "Fink." However, at BlackRock, we see profit and purpose as inextricably linked.[101]

FIGURE 14: PROFIT AND PURPOSE

"Profits are in no way inconsistent with purpose . . . ."

Larry Fink, 2019 CEO Letter

Factoring in stakeholders such as employees and clients makes good business sense. In a world of low unemployment, companies that treat

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98. See, e.g., BlackRock, 2019 Annual Engagement and Voting Statistics 2 (2019), https://www.blackrock.com/corporate/literature/publication/blk-voting-and-engagment-statistics-annual-report-2019.pdf [https://perma.cc/3229-REXG] (providing summary statistics of how BlackRock voted and engaged with management in 2019).

99. See ICGN 2018 Global Stewardship Awards, Int'l Corp. Governance Network, https://www.icgn.org/winners [https://perma.cc/8A92-8J3W] (last visited Jan. 31, 2020).

100. See Governance, J.P. Morgan Asset Mgmt., https://am.jpmorgan.com/us/institutional/governance (on file with the *Columbia Law Review*) (last visited Jan. 31, 2020); Asset Stewardship, State Street Global Advisors, https://www.ssga.com/eu/gb/institutional-investor/en/about-us/asset-stewardship.html [https://perma.cc/E9QP-JSCE] (last visited Jan. 31, 2020); Engagement, TIAA, https://www.tiaa.org/public/about-tiaa/corporate-social-responsibility/stewardship-corporate-governance [https://perma.cc/9CY7-NRWM] (last visited Jan. 31, 2020); Investment Stewardship, Vanguard, https://about.vanguard.com/investment-stewardship/ [https://perma.cc/EWQ5-FD9C] (last visited Jan. 31, 2020).

101. Larry Fink, Larry Fink's 2019 Letter to CEOs: Purpose & Profit, BlackRock, https://www.blackrock.com/corporate/investor-relations/2019-larry-fink-ceo-letter [https://perma.cc/SR5N-EMLU] (last visited Jan. 31, 2020) ("Profits are in no way inconsistent with purpose . . . .").

their employees well will likely experience lower turnover and lower costs associated with recruiting and training. Likewise, having long-term customers who make repeat purchases and recommend you to others is a strong positive for the bottom line. And, if you are wondering about communities as a key stakeholder, the Vale mine tragedy in Brazil[102] should be a wake-up call to the importance of being allowed to operate based in part by how you treat the communities in which you work. I doubt Milton Friedman would disagree. In August 2019, the Business Roundtable released its statement on the purpose of a corporation, reflecting the need for companies to consider multiple stakeholders, and signed by 181 CEOs.[103]

Investment stewardship is about encouraging companies to focus on the long-term implications of their decisions with a goal of creating sustainable returns for shareholders. It is not about making social decisions. Our engagement emphasizes issues that we believe have a material impact on a specific company and its ability to deliver long-term shareholder value. For two years now, in our stewardship activities we have been speaking to companies about corporate purpose and how it aligns with corporate strategy, seeking to understand how a company's purpose informs its strategy, not to tell a company what its purpose ought to be. We see this as an extension of our fiduciary duty, and not a means for imposing social values.

XV. Engaging on Environmental and Social Issues

Given the increasing attention on E&S issues, I would like to touch on BlackRock's investment stewardship approach in this area. First, BlackRock has identified "Environmental Risks and Opportunities" as one of our five engagement priorities.[104]

As with all of our engagements, BlackRock is focused on issues that could have a material impact on the companies we invest in on behalf of our clients. While E&S is language that can imply something separated or siloed from how a business is run, BlackRock looks at these issues as core to business operations and as areas presenting new opportunities. We find that sound practices in relation to material E&S factors can signal operational excellence and management quality. We also find that factors with long-term financial relevance tend to have impact over time and be industry-specific.

While there are numerous frameworks, surveys, and ratings, we have embraced the Sustainability Accounting Standards Board's (SASB) approach,

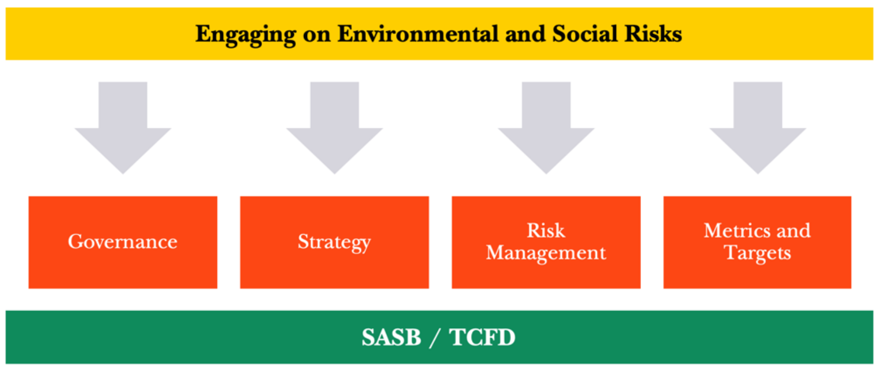
102. See In re Vale S.A. Sec. Litig., No. 1:15-cv-9539, 2017 WL 1102666, at *1 (S.D.N.Y. Mar. 23, 2017).

103. Business Roundtable, Statement on the Purpose of a Corporation 1 (2019), https://opportunity.businessroundtable.org/wp-content/uploads/2019/09/BRT-Statement-on-the-Purpose-of-a-Corporation-with-Signatures-1.pdf [https://perma.cc/Y395-ECR3].

104. BlackRock, Investment Stewardship Engagement Priorities, supra note 97, at 2.

which is industry-specific.[105] BlackRock's engagement on material E&S factors has four main components: (i) governance, (ii) strategy, (iii) risk management, and (iv) metrics and targets. These four pillars are also the conceptual framework underpinning the recommendations of the Financial Stability Board's TCFD, which we participated in developing.[106]

FIGURE 15: FRAMEWORK FOR ENVIRONMENTAL AND SOCIAL ENGAGEMENT



When a sector or a company faces a specific risk or development, BlackRock will engage the companies concerned to better understand how their board and management are addressing the situation and what governance and business practices are in place to mitigate the risks involved. Depending on what we learn, we may continue to engage and give the company time to address these issues, we may vote against one or more directors, or we may vote in favor of a shareholder proposal. Each situation is different and requires careful analysis.

CONCLUSION

Corporate governance and investment stewardship are important pillars of our economy and our capital markets. This is recognized globally, as evidenced by two decades of encouraging managers to be active stewards. Today, there are more than twenty stewardship codes across various jurisdictions.[107]

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105. See Standards Overview, Sustainability Accounting Standards Bd., https://www.sasb.org/standards-overview [https://perma.cc/DNU9-CBZ5] (last visited Jan. 31, 2020).

106. See Publications, Task Force on Climate-Related Fin. Disclosures, https://www.fsb-tcfd.org/publications [https://perma.cc/EWX4-T4LZ] (last visited Jan. 31, 2020).

107. See, e.g., Australian Council of Superannuation Inv'rs, Australian Asset Owner Stewardship Code 5 (2018) https://www.acsi.org.au/images/stories/ACSIDocuments/Stewardship_code/AAOSC_-_Final.pdf [https://perma.cc/4TRK-P3ZQ]; Canadian Coalition for Good Governance, Stewardship Principles 1 (2017), https://admin.yourwebdepartment.com/site/ccgg/assets/pdf/stewardship_principles_public.pdf [https://perma.cc/C264-NJQZ]; Council of Experts on the Stewardship Code, Principles for Responsible Institutional Investors: Japan's

FIGURE 16: GLOBAL STEWARDSHIP CODES

Representative Stewardship Codes	
Australia	Australian Asset Owner Stewardship Code
Canada	Canadian Coalition for Good Governance Stewardship Principles
Japan	Japan's Stewardship Code
The Netherlands	Eumedion Dutch Stewardship Code
OECD	G20/OECD Principles of Corporate Governance
South Africa	South Africa Code on Responsible Investing
United Kingdom	The Financial Reporting Council's UK Stewardship Code

The increased focus on stewardship has led to more transparency and, in turn, has spawned new research asking critical questions: Do asset managers do *enough*? Do they do *too much*? Or, are they doing *just the right amount*? Let's call this the Goldilocks Dilemma.

To answer these questions, one must recognize that asset managers represent a minority interest in any given company, and they engage and vote independently of each other to promote the economic interests of their clients, the asset owners. Key to these questions is also an understanding of the roles of company management and boards of directors, and their responsibility to *all* shareholders. Plus, the stewardship regulatory environment, specific to each country, adds another layer of complexity in answering these questions.

As I have discussed, these debates need to be grounded in good data. Given the importance of compensation consultants and proxy advisors, their roles and influence also need to be factored into any future research.

We welcome what I'm sure will be a spirited and thought-provoking discussion on these issues.

Stewardship Code 3 (2017), https://www.fsa.go.jp/en/refer/councils/stewardship/20170529/01.pdf [https://perma.cc/HL7D-M26N]; Eumedion, Dutch Stewardship Code 1–2 (2018), https://www.eumedion.nl/en/public/knowledgenetwork/best-practices/2018-07-dutch-stewardship-code-final-version.pdf [https://perma.cc/4L52-FGVQ]; Fin. Reporting Council, The UK Stewardship Code 4 (2020), https://www.frc.org.uk/getattachment/5aae591d-d9d3-4cf4-814a-d14e156a1d87/Stewardship-Code_Dec-19-Final-Corrected.pdf [https://perma.cc/HG62-9BYB]; Inst. of Dirs. in S. Afr., Code for Responsible Investing in South Africa 3 (2011), https://cdn.ymaws.com/www.iodsa.co.za/resource/resmgr/crisa/crisa_19_july_2011.pdf [https://perma.cc/FTT4-CN8H]; Org. for Econ. Cooperation & Dev., G20/OECD Principles of Corporate Governance 7 (2015), https://www.oecd-ilibrary.org/docserver/9789264236882-en.pdf [https://perma.cc/E2X4-LY89].