HUMANIZING CORPORATE GOVERNANCE

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Abstract

American corporate governance evolved in a different era, for a type of investor who is no longer typical today. Roughly half of Americans own investment funds, but legal and structural impediments prevent these "human investors" from fully participating in corporate democracy.

One response—"so what?"—is based on the assumption that investors are rationally apathetic. Most investors have so little at stake, the argument goes, that it is economically irrational for them to vote in corporate elections. What this argument misses is that investors' rational apathy is not fixed. Instead, it is a function of the costs and benefits of voting. If we increase the impact of voting, while reducing the barriers and complexity, fewer shareholders will be apathetic.

This theoretical intuition is born out empirically. As this Article demonstrates, human investors have strong, surprisingly prosocial views on numerous topics impacting American corporations. If these views were translated into actual votes, the impact would be profound.

This Article proposes a new approach to corporate governance that is explicitly designed to involve human investors. Using hand-collected data, this Article demonstrates that adopting these proposals would change the outcome of numerous significant corporate votes, and it outlines the path to meaningful change by harnessing the voice of human investors.

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INTRODUCTION

It is my thesis that if you assembled a random group of 100 "average" Americans in a room, a substantial majority would be appalled by a number of decisions that have been made by corporate actors in recent years. These grandmothers, soccer coaches, pediatricians, and construction workers would be horrified that Amazon's ruthless march toward maximum efficiency has forced its workers to urinate in bottles.[1] They would bemoan the fact that only 19% of American employees have access to paid parental leave.[2] They would be dismayed that thousands of items for sale on Amazon's website have been declared unsafe by federal agencies or have been banned by regulators.[3] They would be deeply troubled by the fact that 20% of the world's cobalt (a vital input for

1. *Amazon Apologises for Wrongly Denying Drivers Need to Urinate in Bottles*, BBC NEWS (Apr. 4, 2021), https://www.bbc.com/news/world-us-canada-56628745 [https://perma.cc/5V7L-YTKH]; Kari Paul, *Leaked Memo Shows Amazon Knows Delivery Drivers Resort to Urinating in Bottles*, The GUARDIAN (Mar. 25, 2021, 8:37 PM), https://www.theguardian.com/technology/2021/mar/25/amazon-delivery-workers-bathrooms-memo [https://perma.cc/23WY-4GQR].

2. Kelly Anne Smith, *The U.S. Birth Rate Is Down Again–Could This Be The Final Push For Paid Parental Leave?*, FORBES (May 6, 2021, 11:38 AM), https://www.forbes.com/advisor/personal-finance/us-paid-parental-leave-reform/ [https://perma.cc/QXD3-35NW].

3. Alexandra Berzon et al., *Amazon Has Ceded Control of Its Site. The Result: Thousands of Banned, Unsafe or Mislabeled Products*, WALL ST. J. (Aug. 23, 2019, 8:56 AM), https://www.wsj.com/articles/amazon-has-ceded-control-of-its-site-the-result-thousands-of-banned-unsafe-or-mislabeled-products-11566564990 [https://perma.cc/M777-5C68].

mobile phones) is gathered from "informal" miners as young as six years old who spend long hours inhaling lethal mineral dust for just sixty-five cents per day.[4] They would be disturbed that, despite Starbucks's pledge to have "zero tolerance" for child labor, there is evidence of children as young as eight working in grueling conditions for meager pay to harvest Starbucks's coffee beans.[5] More generally, they would express concern about the myriad of ways that American companies contribute to climate change and environmental degradation.[6]

I further contend that if you whittled the group of 100 down to the fifty-eight or so who happen to own stock,[7] the majority of those remaining would *still* oppose corporate practices that step outside the bounds of basic ethics, even if those practices were legal and even if those practices were profitable. Owning some stock does not strip these individuals of their humanity: many of these "human investors" would be willing to make financial sacrifices to ensure that their families, friends, neighbors, and fellow humans can work and live under reasonable conditions.

This Article uses the term "human investors"—borrowed from former Chief Justice of the Delaware Supreme Court Leo E. Strine Jr.—first, to distinguish all flesh-and-blood investors from the various institutions, funds, and foundations that also own equity assets, and, second, with special reference to the investors with the most typical "human" concerns (for example, dependency on labor for their income), broadly defined as all direct and indirect investors in the bottom 99% in terms of wealth.[8] Given that 58% of American families own stock in some form, the majority of this 99% are also investors.[9] They are, in terms of sheer

4. Siddharth Kara, *Is Your Phone Tainted by The Misery of the 35,000 Children in Congo's Mines?*, THE GUARDIAN (Oct. 12, 2018, 4:00 PM), https://www.theguardian.com/global-development/2018/oct/12/phone-misery-children-congo-cobalt-mines-drc [https://perma.cc/Q7P5-NCPB].

5. Jamie Doward, *Children as Young as Eight Picked Coffee Beans on Farms Supplying Starbucks*, THE OBSERVER (Mar. 1, 2020, 2:05 PM), https://www.theguardian.com/business/2020/mar/01/children-work-for-pittance-to-pick-coffee-beans-used-by-starbucks-and-nespresso [https://perma.cc/MD86-CVNT].

6. Megan Brenan, *Water Pollution Remains Top Environmental Concern in U.S.*, GALLUP (Apr. 19, 2021), https://news.gallup.com/poll/347735/water-pollution-remains-top-environmental-concern.aspx [https://perma.cc/4NMQ-S5EG].

7. Lydia Saad & Jeffry M. Jones, *What Percentage of Americans Own Stock*, GALLUP (May 12, 2022), https://news.gallup.com/poll/266807/percentage-americans-owns-stock.aspx [https://perma.cc/RJ85-4XM6] (finding that 58% of Americans own stock).

8. *See* Leo E. Strine, Jr., *Who Bleeds When the Wolves Bite?: A Flesh-and-Blood Perspective on Hedge Fund Activism and Our Strange Corporate Governance System*, 126 YALE L.J. 1870, 1871, 1876 (2017).

9. Saad & Jones, *supra* note 7.

numbers, by far the biggest group of shareholders in the United States. Together, they control 62% of U.S. households' equity ownership.[10]

Of course, even amongst these human investors, stockholdings are unevenly distributed: the bulk of investment-based wealth is concentrated at the top.[11] Still, it makes sense to speak of "human investors" as a coherent entity because they share a number of important commonalities.[12] Even the wealthiest members of the 99% tend to derive most of their income from labor, rather than their investments.[13] In this sense, "human investors" are also America's workers, and they are highly attuned to working conditions and fluctuations in the labor market.[14] Relatedly, given their dependence upon paid labor, human investors largely use their investments to fund long-term financial projects, such as saving for retirement.[15] They can therefore be said to have a long-term interest in the health of the stock market.[16] Finally, they are significantly less likely than their wealthier counterparts to own stock directly.[17] Instead, human investors often purchase stock indirectly through investments in index funds or other mutual funds.[18]

Indeed, mutual funds might be said to be the financial "home" of these human investors. The median mutual fund investor has moderate financial means, with approximately $100,000 in household income and $200,000 in household financial assets.[19] This median mutual fund investor has about $120,000 in mutual funds, representing 65% of their

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10. Robert Gebeloff, *Who Owns Stocks? Explaining the Rise in Inequality During the Pandemic*, N.Y. TIMES (Jan. 26, 2021), https://www.nytimes.com/2021/01/26/upshot/stocks-pandemic-inequality.html [https://perma.cc/5W4P-MXLA].

11. *Id.*

12. *Id.*

13. *See* Strine, *supra* note 8, at 1876–77.

14. *Id.* at 1879 (discussing the concerns of investors who are also workers).

15. *See, e.g.*, Kenneth Corbin, *Investors Focused on Retirement Savings, but Get Little Help from Employers*, FIN. PLAN. (Aug. 31, 2021, 10:15 AM), https://www.financial-planning.com/news/investors-focused-on-retirement-savings-but-get-little-help-from-employers [https://perma.cc/ZU4W-6RRK] (providing data that saving for retirement is most investors' top priority).

16. Leo E. Strine, Jr., Essay, *Can We Do Better by Ordinary Investors? A Pragmatic Reaction to the Dueling Ideological Mythologists of Corporate Law*, 114 COLUM. L. REV. 449, 500 (2014) ("Because most American investors have to entrust their capital to the market for decades to fund college tuitions and retirements, and because most Americans are still more dependent on their ability to get good jobs than on equity returns, their narrower interests as investors and broader economic interests are harmonic in the sense that both are advanced by policies that facilitate durable increases in American wealth, productivity, and job creation, through sustainable, nongimmicky business plans.").

17. Gebeloff, *supra* note 10.

18. *See Frequently Asked Questions About Mutual Fund Shareholders*, INV. CO. INST. (Mar. 15, 2018), https://www.ici.org/faqs/faq/mfs/faqs_mf_shareholders#avg_shareholder [https://perma.cc/4DTY-LKNN].

19. *Id.*

total assets.[20] While that might not be "much" relative to the stock market's big fish, value is relative: the more scant someone's stockholdings, the more precious to that person they are likely to be.[21] In addition, as a collective, mutual funds' holdings are actually quite substantial. Mutual funds and other registered investment companies control at least 30% of U.S. corporate equity.[22] In particular, the "Big Three" index fund managers—Vanguard, BlackRock, and State Street—control a sizable portion of the overall stock market: they manage more than 20.5% of outstanding shares for S&P 500 companies, and they cast more than 25% of the votes at these companies.[23] That figure is expected to grow to 34.3% by 2028 and to 40.8% by 2038.[24]

In sum, human investors are America's workers, and they have a vested interest in the health of the job market as well as the health of the stock market. Although their individual holdings in the market may be relatively small, as a collective and through their financial intermediaries, they control a significant proportion of outstanding stock. In fact, their considerable holdings might appear to cast doubt on this Article's original thesis. If human investors own such a significant portion of outstanding stock, and if they are indeed altruistic, why do they not push American corporations to enhance worker welfare, to minimize human rights abuses, and to prevent environmental degradation? Why do they not make their interests in nonfinancial ends known?

The short answer is that many human investors are trying to do just that. The socially responsible investment movement has exploded in popularity in recent years, with investors actively pursuing environmental, social, and governance (ESG) ends in addition to more traditional corporate aims.[25] ESG investment funds now account for 10% of worldwide fund assets,[26] and these funds are only expected to continue

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20. *Id.*

21. Joshua Greene & Jonathan Baron, *Intuitions About Declining Marginal Utility*, 14 J. BEHAV. DECISION MAKING 243, 243–44 (2001) (discussing declining marginal utility).

22. INV. CO. INST., 2021 INVESTMENT COMPANY FACT BOOK 47 fig. 2.7.

23. Lucian Bebchuk & Scott Hirst, *The Specter of the Giant Three*, 99 B.U. L. REV. 721, 736 (2019).

24. Lucian Bebchuk & Scott Hirst, *The Power of the Big Three and Why it Matters*, 102 B.U. L. REV. 1547, 1560 (2022).

25. U.S. SUSTAINABLE INV. F., 2020 REPORT ON SUSTAINABLE AND IMPACT INVESTING TRENDS, https://www.ussif.org/files/Trends/2020_Trends_Onepager_Alternatives.pdf [https://perma.cc/F5LU-TWBC] (finding that sustainable investments have grown twenty-five-fold since 1995 and increased by 42% in 2020 alone).

26. Ross Kerber & Simon Jessop, *How 2021 Became the Year of ESG Investing*, REUTERS (Dec. 23, 2021, 4:20 PM), https://www.reuters.com/markets/us/how-2021-became-year-esg-investing-2021-12-23/ [https://perma.cc/H8ST-UUQ4].

their explosive growth.[27] Increasingly, investors are seeking out ways to voice their social and environmental concerns,[28] and neuroscientific research suggests that their motivations are often altruistic rather than profit-minded.[29]

The long answer, however, is that these human investors simply do not have a good way to exert much influence over management. ESG funds, for example, typically take a screen-based approach that merely excludes "problematic" companies from an investor's portfolio.[30] By its nature, this approach channels money (and the influence that goes with it) *away* from the most problematic companies, minimizing rather than augmenting investors' ability to promote change through corporate governance mechanisms. Human investors can avoid or "exit" problematic companies, but there is little to no empirical evidence that this approach changes corporate behavior.[31] In addition, ESG grading systems are known to vary wildly, making reliance upon these metrics

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27. Lizzy Gurdus, *ESG Investing to Reach $1 Trillion by 2030, Says Head of iShares Americas as Carbon Transition Funds Launch*, CNBC (May 9, 2021, 10:00 AM), https://www.cnbc.com/2021/05/09/esg-investing-to-reach-1-trillion-by-2030-head-of-ishares-americas.html [https://perma.cc/6AE9-RADT].

28. *See* Sara Bernow et al., *From 'Why' to 'Why not': Sustainable Investing as the New Normal*, MCKINSEY & CO. 1, 10 (Oct. 25, 2017), https://www.mckinsey.com/~/media/McKinsey/Industries/Private%20Equity%20and%20Principal%20Investors/Our%20Insights/From%20why%20to%20why%20not%20Sustainable%20investing%20as%20the%20new%20normal/From-why-to-why-not-Sustainable-investing-as-the-new-normal.ashx [https://perma.cc/4XJ8-CGKB] ("The sustainable investing market has grown significantly as demand for sustainable investment strategies has surged . . . .").

29. Xiaolan Yang et al., *Are People Altruistic When Making Socially Responsible Investments? Evidence From a tDCS Study*, 15 FRONTIERS NEUROSCIENCE 1, 11 (Aug. 18, 2021), https://doi.org/10.3389/fnins.2021.704537 [https://perma.cc/DK3S-Y43T] (finding that brain stimulation of areas associated with altruism increased willingness to make investments in socially responsible investment (SRI) funds, "suggesting that altruism plays an important role in SRI decision-making").

30. Susan N. Gary, *Best Interests in the Long Term: Fiduciary Duties and ESG Integration*, 90 U. COLO. L. REV. 731, 737–38, 740 (2019) (defining negative screens, which exclude companies "that did something the investor found morally or ethically wrong," and positive screens, which use a "best-in-class selection process" to focus investments in only desirable companies).

31. Julian F. Kölbel et al., *Can Sustainable Investing Save the World? Reviewing the Mechanisms of Investor Impact*, 33 ORG. & ENV'T 554, 561 (2020) ("[T]here is no empirical evidence that explicitly links sustainable investors' screening approaches to changes in ESG practices.").

"unreliable,"[32] and numerous funds that espouse prosocial commitments fail to live up to their claims.[33]

More generally, for all the talk of proxy voting and shareholder franchise, the vast majority of these human investors do not even have the right to participate in the proxy voting process, since the law grants such voting rights to the mutual funds themselves.[34] As a result, human investors are largely uninvolved in the corporate democratic process. Additionally, unlike the wealthy and the powerful, human investors do not hold enough sway to meaningfully communicate their interests directly to corporate management through "engagements" or private conversations.[35] Further, these human investors may not meet the ownership and holding requirements necessary to make their own shareholder proposals, and, even if they did, the shareholder proposal process may prove onerous and difficult to navigate for the typical, relatively unsophisticated human investor.[36]

Of course, fund managers could take on these roles on behalf of their clients, and, to a limited extent, they do.[37] For the most part, the "stewardship teams" charged with this function do not seek any input

32. *See The Aggregate Confusion Project*, MIT SLOAN SUSTAINABILITY INITIATIVE, https://mitsloan.mit.edu/sustainability-initiative/aggregate-confusion-project [https://perma.cc/SX6E-NK99].

33. *Climate Funds: Are They Paris Aligned?: An Analysis of ESG and Climate-Themed Equity Funds*, INFLUENCEMAP 2 (Aug. 2021), https://influencemap.org/report/Climate-Funds-Are-They-Paris-Aligned-3eb83347267949847084306dae01c7b0 [https://perma.cc/RDQ2-ZQ5N] ("Of the funds assessed, 421 of them, or 71%, have a negative Portfolio Paris Alignment score, indicating the companies within their portfolios are misaligned from global climate targets.").

34. Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, 68 Fed. Reg. 6564, 6565 (Feb. 7, 2003) (codified at 17 C.F.R. §§ 239, 249, 270, 274) ("Because a mutual fund is the beneficial owner of its portfolio securities, the fund's board of directors, acting on the fund's behalf, has the right and the obligation to vote proxies relating to the fund's portfolio securities.").

35. *See* MATTEO TONELLO & MATTEO GATTI, THE CONFERENCE BD., DN-V10N3, BOARD-SHAREHOLDER ENGAGEMENT PRACTICES: FINDINGS FROM A SURVEY OF SEC-REGISTERED COMPANIES, 1, 5 (Dec. 13 2019), http://www.shareholderforum.com/access/Library/20191200_TCB.pdf [https://perma.cc/8LFL-Q7K5] (finding that most engagements occur between management and large passive asset managers, hedge funds, and public pension funds, rather than individual investors).

36. *See, e.g.*, *SEC Rule Changes Will Block Most Shareholder's Ability to File Proxy Proposals*, INTERFAITH CTR. ON CORP. RESP. (Sept. 23, 2020), https://www.iccr.org/press-release-sec-rule-changes-will-block-most-shareholders-ability-file-proxy-proposals [https://perma.cc/RQH4-GMLP] (describing how the rules governing shareholder proposals have the effect of "severely restricting shareholders' access to the corporate proxy by limiting the filing of resolutions").

37. *See* Lucian Bebchuk & Scott Hirst, *Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy*, 119 COLUM. L. REV. 2029, 2046–63 (2019) (discussing the promise and disappointing reality of index fund stewardship).

from human investors on their interests and priorities.[38] Even if these stewardship teams have the best of intentions, they could not be said to properly promote investors' best interests because they have no mechanism for discovering what those interests may be.[39] And, as this Article demonstrates, there are substantial discrepancies[40] between fund voting behaviors and human investors' true preferences.[41]

The truth is that the corporate governance system evolved in a different era, for a type of investor who is no longer typical today.[42] Where once just 10% of American households held any stocks,[43] today 58% of households do so.[44] Where once just 8% of Americans held stocks in investment funds, today 47% of households own some type of investment fund.[45] The extant corporate governance system was not built to facilitate the involvement of human investors, nor was it built to serve the needs of indirect investors. This archaic system effectuates the near-total exclusion of human investors from the corporate decisionmaking process. As a normative matter, this is to society's collective detriment. Amongst corporate actors, human investors have the strongest incentives to simultaneously pursue profit, employee welfare, and social welfare, and they are corporate America's best connection to the ethics and values that exist outside the executive suite in broader society.[46]

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38. Caleb N. Griffin, *Environmental & Social Voting at Index Funds*, 44 DEL. J. CORP. L. 167, 178 (2020) (describing how index funds are not required to solicit investor input on voting decisions).

39. *Id.*

40. *See infra* Section III.A.3.

41. Moreover, there is some evidence that the concentration of power at the largest funds may actually be harming the interests of human investors. For example, some commentators argue that concentrated "common ownership" of retail investors' assets by a handful of asset managers has led to price increases and wage stagnation. *See* Eric A. Posner et al., *A Proposal to Limit the Anticompetitive Power of Institutional Investors*, 81 ANTITRUST L.J. 669, 669–70 (2017) (discussing price increase effects); Zohar Goshen & Doron Levit, *Agents of Inequality: Common Ownership and the Decline of the American Worker*, 72 DUKE L.J. 1, 28 (2022) (arguing that common ownership of retail assets has led to decades of wage stagnation).

42. *See* Allison Herren Lee, *Every Vote Counts: The Importance of Fund Voting and Disclosure*, U.S. SEC. EXCH. COMM'N (Mar. 17, 2021), https://www.sec.gov/news/speech/lee-every-vote-counts [https://perma.cc/XH6Y-CGKS] ("I am concerned our regulations have not kept up with this new landscape of institutional investor-driven corporate governance.").

43. *Historical Timeline*, FED. DEPOSIT INS. CORP. (Jan. 2, 2014), https://www.fdic.gov/about/history/timeline/1920s.html [https://perma.cc/JVE8-4WCW] (noting that about 10% of households owned stock in the 1920s).

44. Saad & Jones, *supra* note 7 (finding that 58% of Americans own stock).

45. Lee, *supra* note 42.

46. *See* Leo E. Strine, Jr., *Fiduciary Blind Spot: The Failure of Institutional Investors to Prevent the Illegitimate Use of Working Americans' Savings for Corporate Political Spending*, 97 WASH. U. L. REV. 1007, 1039 (2020) (contrasting the values of human investors with the priorities of corporations).

This Article proposes an approach to corporate governance that is explicitly designed to involve human investors. This project is a response to the reality that human investors are not, as some might suggest,[47] "apathetic" about how corporations are managed.[48] Rather, they are disaffected by a corporate governance and proxy voting system that was designed for a different era, requires excessive resources and expertise to navigate, and produces only very limited personal rewards.[49] They are also limited by legal and structural impediments that severely restrict human investors' involvement.[50]

Although ambitious, this project is attainable, given that it is built upon the existing infrastructure at mutual funds and, in particular, the powerful Big Three index funds, where human investors have already congregated[51] and which already hold substantial influence over modern corporate governance.[52] It seeks to transform these purported representatives of human investors into more faithful agents, attentive to and accountable for the input of these investors.

Part I of this Article explores the issue of human investors' interests. It argues that investors' interests have been conceptualized improperly, and it provides empirical evidence that human investors desire the pursuit of prosocial values, that they are willing to altruistically sacrifice profits to achieve social good, and that such views are surprisingly widespread. Part II examines the state of the current corporate governance system and how that system effectuates the structural ostracization of human investors. Part III provides a roadmap for a new approach to corporate governance, and it sketches the contours of what this approach could look like in practice.

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47. *See, e.g.*, Jeffrey N. Gordon, *The Mandatory Structure of Corporate Law*, 89 COLUM. L. REV. 1549, 1575–76 (1989) (discussing the rationality of shareholder apathy).

48. Evidence of human investors' concern for how corporations are managed can be seen in the rapid growth of ESG investment funds and other forms of socially responsible investment. Increased interest in these types of investment funds suggests that investors wish to influence the behaviors of corporate management, if given a mechanism to do so. *See* Saijel Kishan, *ESG by the Numbers: Sustainable Investing Set Records in 2021*, BLOOMBERG (Feb. 3, 2022, 11:03 AM), https://www.bloomberg.com/news/articles/2022-02-03/esg-by-the-numbers-sustainable-investing-set-records-in-2021 [https://perma.cc/4XXG-CDJN] ("[ESG] assets are set to balloon to $50 trillion by 2025 from about $35 trillion, according to estimates from Bloomberg Intelligence. The growth has been spurred by record-breaking fund inflows amid concerns about climate change and other societal issues.").

49. *See infra* Section II.A.

50. *Id.*

51. Strine, *supra* note 8, at 1965–66.

52. Bebchuk & Hirst, *supra* note 23, at 724 (providing data that the Big Three index funds cast about 25% of the votes at S&P 500 companies as of 2018).

I. WHAT DO HUMAN INVESTORS WANT?

A common concern among political commentators is that various regulators will be captured by "special interests," who will lobby the regulators for favorable treatment that benefits certain individuals or groups but harms others.[53] There is an analogous concern in corporate law: the fear that actors with idiosyncratic or self-interested motives will come to dominate corporate governance.[54] This concern is not limited to obvious self-dealing, such as embezzlement of corporate funds. Rather, any activities or interests other than those that ultimately serve the goal of profit maximization would commonly be considered a "special interest."[55] It is assumed, as a default, that generalized profit maximization is the standard, "non-special" interest of the majority.[56] Is this assumption accurate? This Part examines what human investors want as both a theoretical and empirical matter. It finds evidence that, for the majority of these investors, the relentless and single-minded pursuit of profit is the true special interest.

A. *The (False) Equivalence of Investor Interests and Profit*

Much of corporate law and corporate legal scholarship enshrines the advancement of "shareholder interests" as the primary or even sole purpose of a corporation.[57] In particular, shareholder interests are

53. *See, e.g.*, William M. Landes & Richard A. Posner, *The Independent Judiciary in an Interest-Group Perspective*, 18 J. LAW & ECON. 875, 894 (1975) (advancing a theory of the political process as one in which deals are made by effective interest groups with the legislature and the judiciary enforcing those deals); John M. de Figueiredo & Elizabeth Garrett, *Paying for Politics*, 78 S. CAL. L. REV. 591, 593 (2005) (discussing strategies to curb "quid pro quo corruption . . . by special interests").

54. *See, e.g.*, John H. Matheson & Vilena Nicolet, *Shareholder Democracy and Special Interest Governance*, 103 MINN. L. REV. 1649, 1650 (2019) ("As happens in the political sphere, where power exists, preference is sought. The result in the corporate sphere is the rise of special interest corporate governance.").

55. *See, e.g.*, Henry T.C. Hu, *New Financial Products, the Modern Process of Financial Innovation, and the Puzzle of Shareholder Welfare*, 69 TEX. L. REV. 1273, 1282–83 (1991) ("Most academics now believe that shareholder wealth maximization is the basic pecuniary objective of the modern publicly held corporation.").

56. Joan MacLeod Heminway, *Shareholder Wealth Maximization As A Function of Statutes, Decisional Law, and Organic Documents*, 74 WASH. & LEE L. REV. 939, 943–44 (2017) ("[S]hareholder wealth maximization theory focuses almost exclusively on financial wealth (i.e., pecuniary gain or profit), as opposed to other measures of satisfaction or benefit derived by shareholders from their equity ownership. In addition, decisional law addressing the shareholder wealth maximization norm typically emphasizes the maximization of short-term or long-term profit or financial wealth in connection with an individual decision made by a corporation's board of directors.").

57. *See, e.g.*, Henry Hansman & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L.J. 439, 441 (2001) ("[T]here is today a broad normative consensus that shareholders

routinely juxtaposed to and elevated above the interests of other constituencies, such as employees, the local community, or the environment.[58] This notion of "shareholder primacy" serves as both a positivist theoretical framework facilitating the interpretation of existing law and policy[59] as well as a normative principle guiding corporate law and scholarship toward the advancement of shareholder interests as a socially beneficial outcome.[60]

Shareholder interests, in turn, are almost invariably equated with shareholder wealth and/or share price maximization.[61] Indeed, the terms "shareholder interests" and "shareholder welfare" are routinely used as synonyms for "shareholder wealth" and "shareholder value."[62] In any other context, the notion that a person's interests extend only so far as their pocketbook would be considered an overly simplistic caricature.[63] However, in much of corporate law, the conceptual and linguistic

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alone are the parties to whom corporate managers should be accountable . . . ."); Stephen M. Bainbridge, *In Defense of the Shareholder Wealth Maximization Norm: A Reply to Professor Green*, 50 WASH. & LEE L. REV. 1423, 1424 (1993) ("As it has long done, Delaware law still requires directors to put shareholder interests ahead of those of nonshareholders."); TW Servs., Inc. v. SWT Acquisition Corp., Nos. 10427, 10298, 1989 WL 20290, at *7 (Del. Ch. Mar. 2, 1989) ("[D]irectors may be said to owe a duty to shareholders as a class to manage the corporation within the law, with due care and in a way intended to maximize the long run interests of shareholders."); *see also* Milton Friedman, *A Friedman Doctrine—The Social Responsibility of Business Is to Increase Its Profits*, N.Y. TIMES MAG., Sept. 13, 1970, at 32 ("The whole justification for permitting the corporate executive to be selected by the stockholders is that the executive is an agent serving the interests of his principal.").

58. David Millon, *New Game Plan or Business As Usual? A Critique of the Team Production Model of Corporate Law*, 86 VA. L. REV. 1001, 1010 (2000) ("It is common coin among commentators to speak of corporate law and its fiduciary doctrines as mandating management regard for shareholder interests over those of other corporate constituencies.").

59. Bainbridge, *supra* note 57, at 1424–25 ("At least in Delaware, the shareholder wealth maximization norm thus remains a more accurate description of the state of the law than any of its competitors.").

60. Hansman & Kraakman, *supra* note 57, at 441 ("[T]here is convergence on a consensus that the best means to this end (that is, the pursuit of aggregate social welfare) is to make corporate managers strongly accountable to shareholder interests and, at least in direct terms, only to those interests.'").

61. Heminway, *supra* note 56, at 943.

62. *See, e.g.*, William T. Allen, *Ambiguity in Corporation Law*, 22 DEL. J. CORP. L. 894, 896–97 (1997) (referring to "investors' interests" and "the protection of long-term value of capital committed indefinitely to the firm" interchangeably); FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 124 (1991) (describing "[m]arket [v]alue as a [b]enchmark under the [f]iduciary [p]rinciple"); Katz v. Oak Indus. Inc., 508 A.2d 873, 879 (Del. Ch. 1986) (referring to "the long-run interests of the corporation's stockholders" and the maximization of "shareholder values" as synonyms).

63. *See, e.g.*, Yukako Inoue et al., *People Prefer Joint Outcome Prosocial Resource Distribution Towards Future Others*, 11 SCI. REPORTS (Mar. 8, 2021), https://www.nature.com/articles/s41598-021-84796-4 [https://perma.cc/5DUU-ZKWU] (discussing the complexity of human values and evidence for altruistic motivations).

equivalence of shareholder interests and financial wealth is taken as a given.[64]

Under this "shareholder wealth maximization norm," then, corporate directors are believed to be required to pursue the particular end of shareholder profits, based upon the foundational assumption that "shareholder interests" necessarily and easily translate to financial wealth.[65] Benefits for non-shareholder constituencies are pursued only "incidentally" to the pursuit of shareholder profit.[66]

To be sure, there is a robust literature challenging these foundational assumptions. In particular, numerous scholars have argued for a broadened understanding of corporate purpose that better protects the interests of nonshareholder groups. For example, in 1932, Professor E. Merrick Dodd Jr. advocated that "those who manage our business corporations should concern themselves with the interests of employees, consumers, and the general public, as well as of the stockholders."[67] Likewise, in 1993, Professor Ronald Green argued for "a multi-fiduciary view of managerial responsibilities" that involved treating shareholders as but one of a corporation's many stakeholders.[68] In 1999, Professors Margaret Blair and Lynn Stout advanced a "team production model" of corporate law, under which corporate boards were viewed as being "free to mediate among competing interests" held by the various members of the "corporate team," including shareholders as well as employees, creditors, and the local community.[69] State lawmakers have entered the fray, passing a bevy of nonshareholder constituency statutes that affirmatively permit directors to consider the interests of nonshareholder constituencies when assessing the best interests of the corporate entity as a whole.[70]

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64. *See* Lawrence E. Mitchell, *The Human Corporation: Some Thoughts on Hume, Smith, and Buffett*, 19 CARDOZO L. REV. 341, 358 (1997) (referring to "the current fictionalized model of the stockholder" as a person "with the single goal of maximizing profits").

65. Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 287 (1999) ("[M]ost contemporary corporate scholars tend to assume that directors' proper role is to maximize the economic interests of the corporation's shareholders.").

66. Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919) (referring to the "incidental humanitarian expenditure of corporate funds for the benefit of the employees"); eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, 33 (Del. Ch. 2010) (framing the promotion of "non-stockholder interests" as a route to "promote stockholder value").

67. E. Merrick Dodd Jr., *For Whom Are Corporate Managers Trustees?*, 45 HARV. L. REV. 1145, 1156 (1932).

68. Ronald M. Green, *Shareholders As Stakeholders: Changing Metaphors of Corporate Governance*, 50 WASH. & LEE L. REV. 1409, 1419 (1993).

69. Blair & Stout, *supra* note 65, at 251, 257, 327.

70. *See, e.g.*, MINN. STAT. § 302A.251, subdiv. 5 ("In discharging the duties of the position of director, a director may, in considering the best interests of the corporation, consider the interests of the corporation's employees, customers, suppliers, and creditors, the economy of the

However, even amongst shareholder primacy's strongest detractors, investors' interests are commonly equated with profit. Most historical challenges to shareholder primacy have adopted a "shareholders-versus-stakeholders" or "shareholders-versus-society" posture, which accepts at face value the premise that shareholder interests are properly equated with profit maximization.[71] The grand arc of corporate law can thus be said to presuppose the equivalence of shareholder interests and shareholder profits.[72] The great casualty of this false equivalence is a truly accurate understanding of human investors' nuanced and individualized interests.[73] In the words of former Chief Justice Strine, "the flesh-and-blood human beings our corporate governance system is supposed to serve get lost."[74]

B. *The Lost Shareholders*

A growing amount of literature seeks to give voice to corporate law's lost shareholders. For example, Professor Lynn Stout argues in her 2012 book that notions of "shareholders" as an undifferentiated, profit-obsessed bloc are both descriptively inaccurate and normatively harmful.[75] She convincingly demonstrates that the human beings who own stock have heterogeneous values, ranging from short-term stock price maximization for a single company to long-term economic growth for the economy as a whole to prosocial concerns about how companies operate; she further argues that ignoring shareholders' diverse interests harms shareholders themselves as well as society.[76] Similarly, Professor Daniel J.H. Greenwood problematizes simplistic caricatures of shareholders and argues that our notion of a fictional, wealth-focused shareholder empowers corporations to "take positions of which few, or even none, of their human affiliates would approve."[77] Professor Iman Anabtawi argues that "shareholders have widely divergent interests" and identifies five key schisms that differentiate investors from one another.[78] Likewise, former Chief Justice Strine examines how "the current

state and nation, community and societal considerations, and the long-term as well as short-term interests of the corporation and its shareholders . . . .").

71. *See* LYNN STOUT, THE SHAREHOLDER VALUE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC 7 (2012).

72. *Id.*

73. *Id.* at 9 ("[I]n directing managers to focus only on share price, shareholder value thinking *ignores the reality that different shareholders have different values.*").

74. Strine, *supra* note 8, at 1871.

75. STOUT, *supra* note 71, at 69.

76. *Id.* at 69, 73.

77. Daniel J.H. Greenwood, *Fictional Shareholders: For Whom Are Corporate Managers Trustees, Revisited*, 69 S. CAL. L. REV. 1021, 1089 (1996).

78. Iman Anabtawi, *Some Skepticism About Increasing Shareholder Power*, 53 UCLA L. REV. 561, 578, 598 (2006).

corporate governance system . . . gives the most voice and the most power to those whose perspectives and incentives are least aligned with that of ordinary American investors."[79] Together, this chorus of voices proclaims a basic, undeniable truth: there is no unified "shareholder class" concerned with profit-making alone. Rather, the majority of U.S. citizens are shareholders in some form or another,[80] and this massive subset of humanity very likely contains all of the variations known to exist therein.[81]

C. *Data on What Human Investors Want*

As evidence of the heterogeneity of investor preferences, and, in particular, the willingness of many human investors to sacrifice profits to support social ends, this Article presents the results of an original survey of 1,611 owners of index funds and/or exchange-traded funds (ETFs). This survey separately examined investors' willingness to sacrifice profits in three different contexts: to benefit employees, to benefit the community and/or society at large, and to benefit the environment.

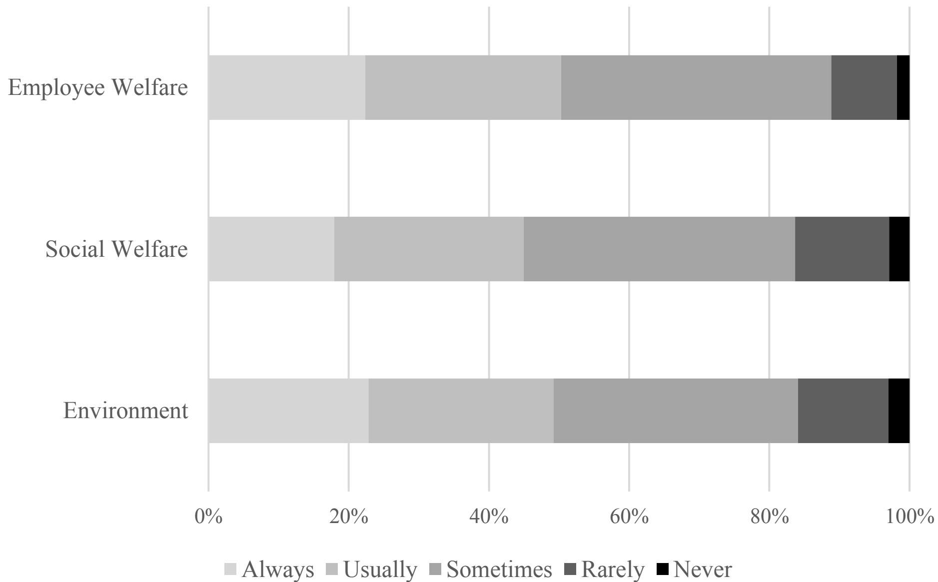
79. Strine, *supra* note 8, at 1970.

80. Saad & Jones, *supra* note 7 (finding that 58% of Americans own stock).

81. *See, e.g.*, Paul Rose, *Common Agency and the Public Corporation*, 63 VAND. L. REV. 1355, 1372–80 (2010) (examining the wide potential for heterogeneous shareholder preferences).

Figure 1: Investors' Willingness to Sacrifice Profits for Social Causes

This chart summarizes the results of a survey of 1,611 index fund and/or ETF owners.[82] The margin of error is +/- 2.491%.



This data has important caveats. First, this portion of the survey is quite general, and it does not cover specific topic areas in detail. It may mask important differences in certain subtopics—for instance, some investors who report concern for the "environment" might care a great deal about, say, carbon emissions, and less about habitat loss for a certain endangered species. Subjectivity may also influence the responses, as what constitutes "societal welfare" may differ considerably between individuals. Moreover, it does not purport to solve the difficult line-drawing problems that would face managers attempting to operationalize these investors' sentiments. Instead, the survey is a tool for checking, at a very broad level, the degree to which the dominant conceptions of what it means to be a shareholder are grounded in reality.

As Figure 1 demonstrates, the overwhelming majority of survey respondents would be willing to sacrifice profits in the pursuit of each of

82. Table 1 provides the results from a survey of 1,611 index fund and ETF owners conducted in June 2021. The study author contracted with Momentive Global Inc. to identify the respondent pool and administer the survey to ensure a random sample representative of the general U.S. population in terms of age and gender. The sample was balanced against the U.S. Census to ensure that respondents represent the broader population in terms of age and gender.

these social ends at least some of the time. Nearly half of respondents would be willing to make such sacrifices "usually" or "always." Intriguingly, only a very small minority (ranging from 1.8% to 2.98%) would *never* be willing to make financial sacrifices for social ends.[83] These data suggest that the dominant theoretical conception of an investor is the exception rather than the rule. Such findings directly contradict traditional understandings of "investor interests" that narrowly focus on profit maximization. Instead of being singularly and unerringly focused on profit, a supermajority of human investors is willing to sacrifice profits to improve employee welfare, societal wellbeing, and the environment.

What explains this "irrational" willingness to make financial sacrifices?[84] One might attempt to dismiss these results on the grounds that they are dominated by less-wealthy Americans who have little invested in the stock market and therefore do not have much to lose.[85] Conversely, one might speculate that those of limited means might be more hesitant to make financial sacrifices.[86] However, the data does not strongly support either view. Although there is slight variation based on income, Figure 2 below reveals that an overwhelming majority of those

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83. Other experimental research has made analogous findings. *See, e.g.*, Jean-François Bonnefon et al., *The Moral Preferences of Investors: Experimental Evidence* 26 (Nat'l Bureau of Econ. Rsch., Working Paper No. 29647, 2022). https://www.nber.org/papers/w29647 [https://perma.cc/ES2G-4F3J] (finding "strong evidence" that investors incorporate firm prosociality into their investment decisions).

84. Markets have been described as "hegemonic" in the sense that they lead people to act in a self-interested, wealth-maximizing manner. *See* Stephen Ellis, *Market Hegemony and Economic Theory*, 38 PHIL. SOC. SCIS. 513, 513 (2008) ("In marketplace transactions people generally act for personal gain; other values are reflected only in what they do with those gains. This is no accident. One of the stylized facts about markets is that they are *hegemonic*: they lead people to act on "bottom line" considerations, that is, to get money, products, services, and so on for themselves."). While it may be the default for many investors, such "hegemony" may also be less static than it initially appears. Rather than reflecting some fundamental fact about human nature, it may instead reflect only the "proper subset" of beliefs and desires on which their attention is focused at a given moment. Which proper subset is motivating investor behavior responds dynamically to associations or "understandings" based on situationally salient factors. Thus, investor attitudes may be substantially altered by a priming or "preprocessing" step that prompts investors to focus on other-regarding factors. *See* Grant M. Hayden & Stephen Ellis, *Law and Economics After Behavioral Economics*, 55 U. KAN. L. REV. 629, 662–65 (2007) ("People act on subsets of their mental states, so they attend to only some of their basic interest rankings and some of their beliefs. In a particular circumstance, the behavior-relevant probability weights will be those that are conditioned on salient beliefs and the action-guiding expected utilities are importance-weighted sums of the (numerical representations of the) rankings of salient desires.").

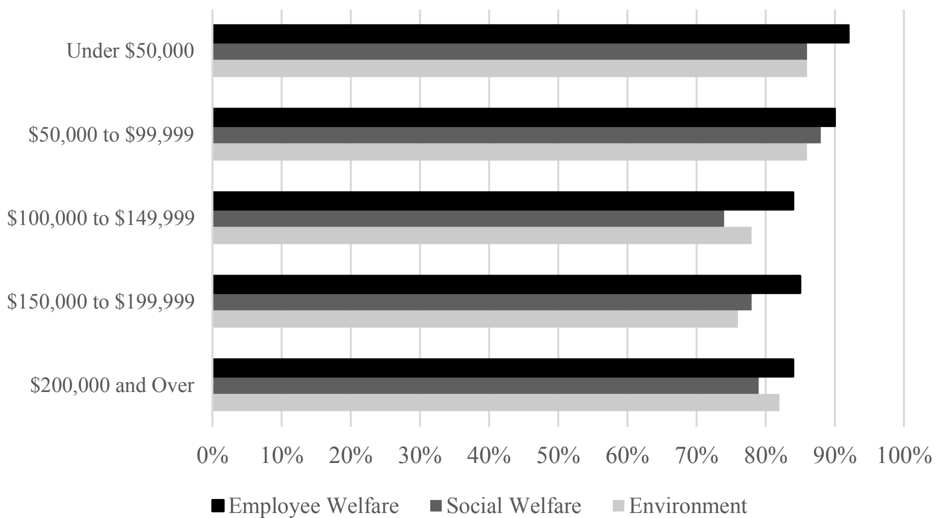
85. Oliver Hart & Luigi Zingales, *The New Corporate Governance*, 1 U. CHI. BUS. L. REV. 195, 209 (2022) (noting that prosociality may be increased where investors have limited stakes in a given company).

86. Oliver Hart & Luigi Zingales, *Companies Should Maximize Shareholder Welfare Not Market Value*, 2 J.L. FIN. & ACCT. 247, 262 (2017) ("Finally, we have ignored the possibility that as shareholders become poorer they may put less weight on ethical concerns, that is, morality is a normal good.").

surveyed supported at least the occasional sacrificing of profits for social outcomes, regardless of income.

Figure 2: Investors' Willingness to Sacrifice Profits by Income

This chart summarizes the results of a survey of 1,611 index fund and/or ETF owners who were asked their views as investors on whether corporations should be free to sacrifice profits in pursuit of various social ends. It categorizes these individuals into groups based upon their self-reported annual income. The margin of error is +/- 2.491%.

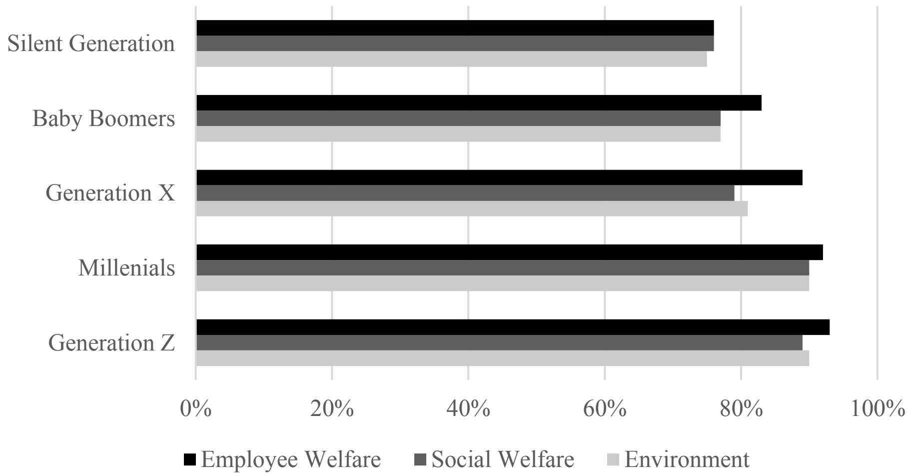


A second justification for these findings might be age. Perhaps these prosocial views are espoused predominantly by the younger generations who have yet to amass any considerable stockholdings and who have yet to discard the supposed financial naïveté of the young.[87] This second potential justification is also not supported by the data. Although there is a slight decrease in support amongst members of older generations, it is not enough to negate the overall proposition that the vast majority of human investors of every generation are willing to sacrifice profits in the pursuit of social causes.

87. *See, e.g.*, Michal Barzuza et al., *The Millennial Corporation: Strong Stakeholders, Weak Managers* 17–22 (Apr. 12, 2022) (unpublished working draft), https://scholarship.law.bu.edu/faculty_scholarship/1172/ [https://perma.cc/ST4N-P4V9] (discussing young investors' prosocial behaviors and whether they may change over time).

Figure 3: Investors' Willingness to Sacrifice Profits by Age

This chart summarizes the results of a survey of 1,611 index fund and/or ETF owners who were asked their views as investors on whether corporations should be free to sacrifice profits in pursuit of various social ends. It categorizes these individuals into groups based upon their self-reported age.



If investors' views cannot be explained by factors such as income or by age, then why would they be willing to make sacrifices for non-financial ends? I believe a more accurate explanation lies in human investors' simultaneous concern for a complex mix of both altruistic and "rationally self-interested" factors, including the health of the stock market, the health of the broader economy, the health of the labor market, and the health of the environment.[88] Human investors do care about stock prices because they have invested the bulk of their savings in the stock market, but this concern is not to the exclusion of their other interests. They *also* care deeply about the interests of workers at American corporations because they and their loved ones are workers at American corporations. They *also* have a concern for social welfare because they and their loved ones make up society. They *also* care about the environment because they hope for the next generation to inherit a clean and sustainable planet. In comparison with other segments of the stockholding population, human investors provide the best representation of broader society's values and interests, and, for this reason, they ought to hold a key position in our corporate governance system.

88. *See* Hart & Zingales, *supra* note 86, at 259–60 (discussing the various factors, including altruistic motives, in investors' utility functions).

II. The Case for a New Approach

Despite the nominal centrality of shareholder interests in corporate law, surprisingly little attention is paid to how real-world investors might perceive or define their own interests. In particular, human investors—the "average" women and men who invest a modest portion of their annual income to fund their retirement or other major expenses—are largely silenced in the current corporate governance regime. The majority of human investors, who own stock indirectly, have no right to vote in firm elections, while the minority of human investors, who own stock directly, have some voting rights but in practice lack an accessible way to express their views on the subjects that matter to them.[89] The ostracism of human investors is troubling given the valuable perspectives that they have to offer. They care deeply about the financial health of their investment portfolio (which is often most or all of their life savings) as well as the impact corporations have on their workers, the environment, and society at large.[90] This Part critiques the failure of the current corporate governance regime to meaningfully incorporate the voices of human investors, and it explains the necessity of a new perspective.

A. *The Contemporary Approach to Corporate Governance*

Human investors currently have three primary mechanisms to exert influence over corporate governance: (1) shareholder franchise, (2) shareholder proposals, and (3) direct communications with firm management. This Section discusses the limited ability of human investors, and particularly indirect human investors, to exert influence through any of the three channels.

1. Shareholder Franchise

In theory, shareholder franchise plays a central role in corporate governance. An oft-quoted case frames shareholder franchise as "the ideological underpinning upon which the legitimacy of directorial power rests."[91] Indeed, voting power is one of the few rights afforded to shareholders, and it is the main mechanism (short of selling their shares) by which shareholders can exert influence over management.[92]

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89. *See infra* Section II.A.1 (discussing the limited role human investors play in corporate governance).

90. Leo E. Strine, Jr. & Nicholas Walter, *Conservative Collision Course?: The Tension Between Conservative Corporate Law Theory and* Citizens United, 100 CORNELL L. REV. 335, 343 (2015) (discussing the nuanced values of human investors).

91. Blasius Indus., Inc. v. Atlas Corp., 564 A.2d 651, 659 (Del. Ch. 1988).

92. Julian Velasco, *The Fundamental Rights of the Shareholder*, 40 U.C. DAVIS L. REV. 407, 419 (2006).

In practice, shareholder voting plays a more moderate role in modern corporate governance. As Professor Stephen Bainbridge notes: "[P]ublic corporations are not participatory democracies, but hierarchies in which decisions are made on a fairly authoritarian basis."[93] Shareholders typically vote on only a few matters, including director elections and whether to approve statutory mergers, charter and bylaw amendments, and sales of substantially all assets.[94] Shareholders do have the right to use a company's annual proxy statement to put forward proposals for other shareholders to vote on at the annual meeting, which significantly expands the universe of issues subject to a shareholder vote.[95] However, a number of procedural and substantive constraints curtail the utility of shareholder proposals,[96] and those constraints have grown even more stringent of late.[97]

What does shareholder franchise look like for a typical human investor? This depends on whether one invests in equity assets directly or indirectly. For the meager fifteen percent of American families that own stock directly,[98] shareholder franchise first involves receiving a copy of the company's definitive proxy statement.[99] This document, written by company management and their lawyers, commonly contains several dozen pages of dense text.[100] Buried therein, the investor will find biographies (that, given their subject matter, could not be expected to give a human investor significant insight into the candidate's values or

93. Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, 97 NW. U. L. REV. 547, 555 (2003).

94. Velasco, *supra* note 92, at 418.

95. 17 C.F.R. § 240.14a-8 (2023).

96. Hart & Zingales, *supra* note 86, at 258 (discussing the limitations imposed by SEC rules on shareholder proposals); Bernard S. Black, *Shareholder Passivity Reexamined*, 89 MICH. L. REV. 520, 541 (1990) (commenting on the limited role shareholder proposals have in corporate governance).

97. In particular, the SEC's 2020 amendments to Rule 14a-8 increased the stock ownership threshold and ownership period, increased procedural requirements governing proposal submission, and increased the level of support needed for resubmission. Press Release, Sec. & Exch. Comm'n, SEC Adopts Amendments to Modernize Shareholder Proposal Rule (Sept. 23, 2020), https://www.sec.gov/news/press-release/2020-220 [https://perma.cc/AJ8A-BWS9]. *But see* Announcement, Sec. Exch. Comm'n, Shareholder Proposals: Staff Legal Bulletin No. 14L (CF), https://www.sec.gov/corpfin/staff-legal-bulletin-14l-shareholder-proposals [https://perma.cc/9Q7M-Q868] (Nov. 3, 2021) (reinterpreting the ordinary business exception, a change which will likely result in the exclusion of fewer shareholder proposals) [hereinafter Announcement].

98. *What Percentage of Americans Own Stock?*, USA FACTS (Mar. 9, 2021, 1:09 PM), https://usafacts.org/articles/what-percentage-of-americans-own-stock/ [https://perma.cc/HYY9-GS4L].

99. 17 C.F.R. § 240.14a-10(a)–(b) (2023).

100. *See, e.g.*, EXXON MOBIL CORP., SCHEDULE 14A, PROXY STATEMENT PURSUANT TO SECTION 14(A) OF THE SECURITIES ECHANGE ACT OF 1934 (May 27, 2020), https://www.sec.gov/Archives/edgar/data/34088/000119312520102226/d869473ddef14a.htm#toc869473_26 [https://perma.cc/S2C3-45RC] (featuring seventy-one pages of dense text).

priorities) of a handful of director nominees, who nearly always go uncontested,[101] as well as the board's voting recommendations for each nominee.[102] In addition, the human investor might be informed of an upcoming vote on more mundane matters, such as the selection of an auditor.[103] There may be a mention of an "advisory vote" on executive compensation, a phrase hardly inspiring much confidence in the purposiveness of the vote.[104] Finally, for the small minority of companies where shareholder proposals will be under consideration,[105] there will be a summary of these shareholder proposals, typically including a strong statement by the board advocating for the rejection of these proposals.[106] Although these proposals might touch upon salient subjects (such as climate change, diversity, or human rights),[107] they frequently use weak language befitting their largely precatory nature.[108] Such language likely does not inspire much confidence in human investors that the proposals' outcomes will be particularly significant.[109]

For those that wish to take the next step to vote their shares, there will be information about how to participate in the meeting and how to vote in advance of the meeting.[110] To participate in the meeting or to submit their votes online, investors will need to find and enter their sixteen-digit control number.[111] If the human investor directly owns stock in more than one company (and, given the risk aversion of most human investors, they probably will be at least somewhat diversified[112]), they will repeat this

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101. Randall S. Thomas & Patrick C. Tricker, *Shareholder Voting in Proxy Contests for Corporate Control, Uncontested Director Elections and Management Proposals: A Review of the Empirical Literature*, 70 OKLA. L. REV. 9, 49 (2017).

102. *See, e.g.*, EXXON MOBIL CORP., *supra* note 100, at 15.

103. *Id.* at 29.

104. *Id.* at 30.

105. Marc Treviño, *2019 Proxy Season Review: Part 1—Rule 14a-8 Shareholder Proposals*, HARV. L. SCH. F. CORP. GOVERNANCE 1 (July 26, 2019) https://corpgov.law.harvard.edu/2019/07/26/2019-proxy-season-review-part-1-rule-14a-8-shareholder-proposals/ [https://perma.cc/4BKW-56ZQ] (indicating that 788 shareholder proposals were submitted in 2018, for the several thousand publicly traded companies in the United States).

106. *See, e.g.*, EXXON MOBIL CORP., *supra* note 100, at 67 (stating in bold text that "The Board recommends you vote AGAINST this proposal for the following reasons. . . .").

107. Glenn Booraem, *What We Do. How We Do It. Why It Matters.*, VANGUARD INV. AUSTL. 12 (Apr. 2019), https://static.vgcontent.info/crp/intl/auw/docs/resources/Investment_Stewardship_ISCOMMP.pdf [https://perma.cc/Y6XL-LC99] (indicating that just .1% of all ballot items in annual elections involve social or environmental shareholder proposals).

108. *See* 17 C.F.R. § 240.14a-8 (2023).

109. *Id.*

110. *See, e.g.*, EXXON MOBIL CORP., *supra* note 100, at 4–5.

111. *Id.*

112. *See* Ronald J. Gilson & Jeffrey N. Gordon, *The Agency Costs of Agency Capitalism: Activist Investors and the Revaluation of Governance Rights*, 113 COLUM. L. REV. 863, 884–86 (2013) (discussing increasing rates of diversification for investors).

process for all of the companies in their portfolio.[113] These proxy statements will all come at different times scattered throughout the year, and the human investor will need to make individualized votes specific to each company.[114]

Given the onerous nature of the proxy voting process and the numerous impediments to human investors' meaningful participation, it is unsurprising that the vast majority of retail investors are "rationally apathetic" toward shareholder voting.[115] Retail investors cast votes for just 32% of their shares, in contrast to 80% for the entire shareholder population.[116] Absenteeism is more common in less wealthy zip codes, where the median human investor is more likely to reside.[117]

If direct human investors are characterized by their quietness in the shareholder voting arena, their indirect counterparts are similarly largely characterized by their silence.[118] Unlike their brethren, who at least retain the right to advocate for their individual interests by voting in corporate elections, indirect investors (who make up the vast majority of American families with any stock ownership[119]) have been almost completely ostracized from the corporate governance system. They lack the legal right to vote in annual and special elections for portfolio companies

113. *See, e.g.*, *Scorecard 2021*, PROXY MONITOR, https://www.proxymonitor.org/ScoreCard2021.aspx [https://perma.cc/Z7JW-5S8W] (providing links to the 2021 proxy statements for dozens of different companies).

114. *Id.* (listing the widely varying annual meeting dates for Fortune 250 companies in the United States for 2021).

115. Alon Brav et al., *Retail Shareholder Participation in the Proxy Process: Monitoring, Engagement, and Voting* 11–12 (Eur. Corp. Governance Inst. Working Paper No. 637/2019, 2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3387659 [https://perma.cc/6R8P-EK5G].

116. *Id.* at 16–17.

117. *Cf.* Kobi Kastiel & Yaron Nili, *In Search of the "Absent" Shareholders: A New Solution to Retail Investors' Apathy*, 41 DEL. J. CORP. L. 55, 59 (2016) (discussing the high cost of voting shares, and how it is rational for investors to not participate).

118. There is, however, one small index fund that has begun permitting investors to vote on shareholder proposals. *See* Leslie P. Norton, *Own This Index Fund, and You Can Still Vote on Shareholder Resolutions*, BARRON'S (Mar. 18, 2021, 11:15 AM), https://www.barrons.com/articles/own-this-index-fund-and-you-can-still-vote-on-shareholder-resolutions-51616080556 [https://perma.cc/72W7-YLZN] ("Typically, once you've invested in a fund, you've surrendered your voting decision to the fund's manager, who hasn't asked for your input. But this year, Index Funds S&P 500 Equal Weight No Load Shares (ticker: INDEX) is allowing investors in the fund a say on how to vote on shareholder proposals at each of the S&P 500's companies."). Additionally, Vanguard and BlackRock are trialing methods to enhance investor involvement, although the ability of human investors to participate is still, at present, effectively nonexistent. *See infra* note 177.

119. *What Percentage of Americans Own Stock?*, *supra* note 98.

because the law grants that right to mutual fund management.[120] In addition, they have a severely constrained ability to influence management by "voting with their feet" due to numerous structural and financial constraints.[121] As a result, most indirect investors have little ability to advocate for, or even to meaningfully express, their own interests.

2. Shareholder Proposals

In addition to voting, shareholders also have the right to engage with management on topics of concern through shareholder proposals.[122] Under Rule 14a-8, qualifying shareholders have the right to propose a resolution advocating (typically on a precatory basis) that the company take a particular course of action.[123] Such proposals are considered and voted upon by shareholders at the annual meeting, unless the corporation successfully excludes the proposal.[124] Among other grounds, a corporation is permitted to exclude proposals from consideration if they seek to "micro-manage" a director's exercise of control over ordinary business matters.[125] However, certain "matters which have significant policy, economic or other implications inherent in them" do not fall under this exception.[126] As a result, shareholders can and do bring proposals addressing the types of economic, social, and environmental concerns that would be of significant interest to human investors.[127]

Despite the potential value of this route to redressing concerns with management, a typical human investor faces significant barriers that prevent many such individuals from submitting their own proposals. The first and most significant is that indirect investors do not meet the necessary qualifications to bring a shareholder proposal because they do not legally "hold" the shares purchased with their money.[128] Thus, for the

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120. Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, 68 Fed. Reg. 6564, 6565 (Feb. 7, 2003) (codified at 17 C.F.R. §§ 239, 249, 270, 274) ("Because a mutual fund is the beneficial owner of its portfolio securities, the fund's board of directors, acting on the fund's behalf, has the right and the obligation to vote proxies relating to the fund's portfolio securities.").

121. *See* John Morley & Quinn Curtis, *Taking Exit Rights Seriously: Why Governance and Fee Litigation Don't Work in Mutual Fund*s, 120 YALE L.J. 84, 112–13 (2010) (explaining, among other factors, the limitations imposed by the "net asset value" structure and redemption mechanics of mutual funds).

122. 17 C.F.R. § 240.14a-8 (2023).

123. *Id.*

124. *Id.*

125. *Id. But see* Announcement, *supra* note 97 (reinterpreting the ordinary business exception in a way that is likely to result in the exclusion of fewer shareholder proposals).

126. Austin v. Consol. Edison Co., 788 F. Supp. 192, 194 (S.D.N.Y. 1992).

127. Stephen M. Bainbridge, *Revitalizing SEC Rule 14a-8's Ordinary Business Exclusion: Preventing Shareholder Micromanagement by Proposal*, 85 FORDHAM L. REV. 705, 709 (2016).

128. *See* 17 C.F.R. § 240.14a-8(b)(1).

bulk of human investors who only own stock indirectly, this channel of involvement is unavailable.[129]

Second, many direct human investors may be unaware that such an input mechanism exists. Corporate governance concepts are rarely included in even university curricula, and common knowledge of the somewhat arcane rules and exclusions governing shareholder proposals is unlikely for the typical human investor.[130] Relatedly, success in the shareholder proposal submission process requires a substantial commitment of time and energy, obstacles that deter or prevent the typical, relatively unsophisticated human investors with many commitments from taking advantage of this tool.[131]

Finally, recent changes to 14a-8 have increased ownership thresholds, with the effect of pricing out many less-wealthy investors.[132] These changes further prohibit shareholders from aggregating shares to meet ownership thresholds, which again disadvantages the less wealthy.[133]

3. Direct Communications with Management

In addition to voting and shareholder proposals, shareholders can theoretically express their concerns and values directly to management through private communications. Powerful individuals, hedge funds, and large asset managers regularly leverage their holdings in this manner.[134] Through these private discussions, powerful market actors exert pressure

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129. *What Percentage of Americans Own Stock?*, *supra* note 98.

130. *See* JUDY T. LIN ET AL., FINRA INV. EDUC. FOUND., THE STATE OF U.S. FINANCIAL CAPABILITY: THE 2018 NATIONAL FINANCIAL CAPABILITY STUDY, 33 (June 2019), https://finrafoundation.org/sites/finrafoundation/files/NFCS-2018-Report-Natl-Findings.pdf [https://perma.cc/WV66-NNR7] (showing relatively low levels of financial literacy among Americans with a clear trend of declining financial literacy from 2009 to 2018).

131. *See, e.g.*, *Shedding Light on the Influence of Shareholder Proposals on Corporations*, PROXY MONITOR, https://www.proxymonitor.org/Default.aspx [https://perma.cc/EX46-JNYT] (providing data on Fortune 250 shareholders proposals) [hereinafter *Shedding Light*]; *see also* James R. Copland, *Frequent Filers: Shareholder Activitsm by Corporate Gadflies*, PROXY MONITOR, https://www.proxy monitor.org/forms/2014Finding5.aspx [https://perma.cc/45VY-U9VB] (describing how the majority of shareholder proposals were brought by organizations and, of those proposals brought by individuals, the majority of those were brought by the same few repeat players, known as "corporate gadflies").

132. *See* Yaron Nili, *It is Not Just Small Investors Who Will Be Silenced Thanks to SEC's New Rule*s, PROMARKET (Nov. 4, 2020), https://promarket.org/2020/11/04/small-investors-silenced-sec-new-rules-threshold/ [https://perma.cc/KMC9-Z9TL].

133. *See id.*

134. *See generally* Amy Freedman et al., *The Director-Shareholder Engagement Guidebook*, HARV. L. SCH. F. CORP. GOVERNANCE (Mar. 2, 2019), https://corpgov.law.harvard.edu/2019/03/02/the-director-shareholder-engagement-guidebook/ [https://perma.cc/WEC3-Q998] ("Institutional investors have become increasingly clear . . . that they expect access to independent directors and a clear process for regular interaction.").

on management to act in a particular manner, often circumventing the voting process entirely.[135]

Human investors, who individually have relatively meager holdings in any given company and who often hold those shares indirectly, are not afforded this highly valuable opportunity to discuss topics of concern with management.[136] Their shareholdings are simply too small for them to merit management's attention.[137] Unlike the wealthy and the powerful, human investors cannot simply call up management to discuss their concerns, nor can they realistically expect to write a letter that will ever be read by management, let alone acted upon.[138]

Under the status quo, then, management regularly entertains the wishes and whims of powerful market actors and often acts on those concerns in less-than-transparent ways without the input of the firm's shareholders as a whole. They effectively do not hear from human investors. There is thus a profound imbalance that favors the wealthy and the powerful and disfavors human investors.

4. The Status of Human Investors

At present, we have a corporate governance system that has profoundly underemphasized the diversity of shareholder interests and values.[139] We fail to meaningfully engage with human investors' true preferences.[140] We have presupposed that all investors behave like profit-obsessed automatons,[141] and we have neglected the true nature of the human investors who serve as the best advocates for long-term economic health, the labor market, sustainability, and morality in the shareholder population.[142] We genuflect toward the vitality of shareholder franchise,

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135. *See, e.g.*, Matheson & Nicolet, *supra* note 54, at 1682–83 (discussing how activist investors come to private agreements with the board without approval of the majority of shareholders).

136. *See, e.g.*, David A. Bell et al., *Public Company Guide—Planning for Shareholder Engagement*, HARV. L. SCH. F. CORP. GOVERNANCE (Aug. 10, 2021), https://corpgov.law.harvard .edu/2021/08/10/public-company-guide-planning-for-shareholder-engagement/ [https://perma.cc /S55Z-8CT5] (proposing that public companies should actively solicit private conversations with their largest twenty-five shareholders).

137. *See id.* (describing how "most companies will want to focus their engagement efforts on institutional shareholders" because of their significant ownership percentages and higher likelihood of voting).

138. *See id.* (explaining how companies can derive goodwill through annual shareholder outreach, but actual meetings with non-institutional investors is not management's priority).

139. *See* Gregory Scott Crespi, *Maximizing the Wealth of Fictional Shareholders: Which Fiction Should Directors Embrace?*, 32 J. CORP. L. 381, 426 (2007) (discussing the unrealistic nature of conceptions of shareholders).

140. *See supra* Sections II.A.1–3 (discussing the limited role human investors play in modern corporate governance).

141. *See supra* Section I.A (assuming that all investors are trying to act in their best interests).

142. *See* Strine, *supra* note 8, at 1884–85.

when in practice human investors are kept quiet—most of them silent—by the structural barriers of the present proxy voting system.[143] While a few powerful market actors have the ear of management, human investors are largely ignored.

If we desire to reform this system—to restore some meaning to shareholder franchise and to make a system that serves human investors, rather than the other way around—we would likely wish for a few key items. First, we might wish for some entity that was duty-bound to promote the "best interests" of its human investors. Second, we might wish that such an entity possessed a universal cross-section of investors that was representative of human investors more broadly. Third, we might wish that such an entity in turn owned a universal cross-section of stocks, so it might have a market-wide impact. Fourth, we might wish that such an entity was powerful enough to easily and meaningfully influence the companies in which it held shares. If these wishes were granted, we would have an agent with the means to remake corporate governance into a useful vehicle for human investors.

B. *The Promise & the Reality of Index Fund Managers*

In fact, we have such an agent, or three such agents to be precise: Vanguard, BlackRock, and State Street—known as the Big Three index fund managers. Despite indirect investors' functional powerlessness, their collective assets convey enormous power to index and mutual fund managers. In particular, stewardship teams at the Big Three index funds have come to wield an unprecedented degree of influence over corporate management. Stewardship teams at the Big Three cast 25.4% of votes at S&P 500 companies,[144] and they have the power to unilaterally decide the fate of a substantial proportion of the hundreds of shareholder proposals at issue in corporate elections at America's largest companies.[145]

Asset managers have long been regarded as holding considerable "promise" as representatives of investors' interests.[146] Due to their scale and index-based model, the Big Three own a considerable stake in all of America's largest public companies, and one of this trio (usually Vanguard) serves as the single largest investor in the majority of such

143. *See supra* Section II.A.1 (discussing the limited role human investors play in modern corporate governance due to the complicated nature of the shareholder voting process).

144. Bebchuk & Hirst, *supra* note 23, at 736.

145. *See* Caleb N. Griffin, *Margins: Estimating the Influence of the Big Three on Shareholder Proposals*, 73 SMU L. REV. 409, 438 (2020) ("[T]he Big Three may already be in a position to determine the outcome of the majority of shareholder proposals.").

146. *See, e.g.*, Bernard S. Black, *Agents Watching Agents: The Promise of Institutional Investor Voice*, 39 UCLA L. REV. 811, 879–81 (1992) (describing the incentives of asset managers to perform well on behalf of their clients).

companies.[147] The Big Three are duty-bound to act in their investors' best interests,[148] and they have the resources to afford expert support from proxy advisors[149] and to access or create digital tools that streamline the proxy voting process.[150]

In practice, however, index fund stewardship teams use their enormous voting power and considerable voting resources with little apparent regard for human investors. Despite a fiduciary obligation to act in investors' "best interests," index fund management has no obligation to identify their investors' preferences, values, or even their basic demographic characteristics.[151] This nebulous notion of investors' best interests thus translates into near-total discretion for stewardship teams, as to date no vote or abstention has been deemed to conflict with investors' "best interests."[152]

The Big Three have the right to bring shareholder proposals on their investors' behalf, and they have ample resources to do so effectively.[153] Unfortunately, the Big Three do not take advantage of that right.[154] In fact, in the five years from 2014 to 2018, the Big Three did not submit a single shareholder proposal on any subject.[155] This trend has continued up until the present, as an analysis of shareholder proposal data conducted for this Article demonstrates that the Big Three did not bring a single shareholder proposal at any Fortune 250 company from 2018 to 2022.[156] Ultimately, this inaction on shareholder proposals places the Big Three in a reactive role rather than a proactive one.

Despite the availability of the far more public and participatory shareholder proposal and shareholder voting mechanisms, index funds

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147. Griffin, *supra* note 145, at 411.

148. *See* Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, 68 Fed. Reg. 6564, 6565 (Feb. 7, 2003) (codified at 17 C.F.R. pts. 239, 249, 270, 274) ("An investment adviser voting proxies on behalf of a fund . . . must do so in a manner consistent with the best interests of the fund and its shareholders.").

149. *See* Booream, *supra* note 107, at 12 (describing how Vanguard's stewardship team uses data from proxy advisors).

150. Jill E. Fisch, *Standing Voting Instructions: Empowering the Excluded Retail Investor*, 102 MINN. L. REV. 11, 39 (2017).

151. *See* Disclosure of Proxy Voting Policies, 68 Fed. Reg. 6564, 6565 (requiring investment advisers to vote "in a manner consistent with the best interests of the fund and its shareholders" without any obligation to ascertain what the investors' interests are).

152. Griffin, *supra* note 38, at 178.

153. *See* Bainbridge, *supra* note 127, at 709–10.

154. Bebchuk & Hirst, *supra* note 37, at 2104.

155. *Id.* at 2103–04.

156. *See Shedding Light*, *supra* note 131 (filter by dates "2018-2022" and the terms "Fortune 250" and "Vanguard, BlackRock, State Street") (providing data showing that none of the shareholder proposals brought from 2018–-2022 at Fortune 250 companies were proposed by the Big Three).

wield much of their considerable power in secret, in the form of direct communications with company management (known as "engagements").[157] Even though the Big Three's power derives from indirect investors and their hard-earned capital, these investors are not privy to the contents of these discussions beyond the information contained in the scant, post hoc "stewardship reports" promulgated by stewardship teams.[158] Stewardship reports generally feature only self-selected engagement "case studies" and "overviews" that reduce these powerful, standard-setting discussions to a single phrase such as "board composition" or "shareholder rights."[159] With apparent pride, index fund managers often proclaim that these engagements are their favored method of stewardship, with the far more transparent proxy voting process deemed a last resort after several years of failed engagements.[160]

Even assuming these agents are well-intentioned, stewardship teams' pursuit of investors' best interests is severely hampered by their general lack of information about their own investors. They are hugely susceptible to their own biases about what their investors *might* want, and index fund investors have essentially no way to hold stewardship teams accountable to any particular outcome. At worst, index fund companies are in a position to use their enormous latitude to advance their own interests under the guise of investment stewardship.

C. *The Need for a New Approach*

Commentators often lament that small-time human investors "suffer from their own rational apathy" at the ballot box.[161] This "shareholder apathy," as demonstrated by low voting rates amongst retail investors, is taken as evidence that (minor) shareholders want little to do with the management of America's corporations.[162] Indeed, it is true that human investors can be rightly characterized as either quiet or silent in their

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157. *See* John C. Coates, *The Future of Corporate Governance Part I: The Problem of Twelve* 16 (Sept. 20, 2018) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3247337 [https://perma.cc/QJ3H-EHHT] ("A second channel of influence is through what institutional shareholders call 'engagements.' Their staffs 'meet'–sometimes in person, more often by phone, sometimes just by email–with representatives of their portfolio companies.").

158. *See, e.g.*, VANGUARD GRP., INVESTMENT STEWARDSHIP 2020 ANNUAL REPORT 52, https://about.vanguard.com/investment-stewardship/perspectives-and-commentary/2020_investment_stewardship_annual_report.pdf. [https://perma.cc/5AKB-HDNX].

159. *See id.*

160. *See, e.g.*, Eric Rosenbaum, *Activists Thought BlackRock, Vanguard Found Religion on Climate Change. Not Anymore.*, CNBC (Oct. 16, 2019, 8:50 AM), https://www.cnbc.com/2019/10/13/blackrock-vanguard-found-religion-on-climate-doubts-are-growing.html [https://perma.cc/Q493-PA56] ("[BlackRock and Vanguard] favor multi-year, direct dialogue with management, and only when that fails turning to a vote.").

161. *See, e.g.*, STOUT, *supra* note 71, at 70.

162. *Id.*

current approach to engaging with management.[163] For many, this low level of involvement is quite rational, given the difficulty a typical investor would have in exercising their rights as shareholders at even a handful of portfolio companies.[164]

However, it would be wrong to infer from their current level of involvement that human investors do not care about how corporations are managed. These are the very people who work at America's companies, who spend a good portion of their incomes on the goods and services offered by these companies, who depend upon the financial health of these companies and the overall economy to be able to retire, and who hope that these companies will operate in such a way that their children can inherit a better world than they themselves knew.

Nor is it fair to argue that small-time investors are unwilling to vote because their holdings are too small to make a difference. As we routinely observe in political elections, millions of people willingly vote, even in relatively one-sided elections, despite the fact that just one vote is rarely determinative.[165] The seismic growth of the sustainable investing movement stands as a testament to human investors' concerns about how corporations are managed,[166] and the recent "meme-stock" movement shows how involved individual investors can be if given an opportunity to have a meaningful impact.[167] More generally, as the millions of product reviews on Amazon and other websites testify, individuals value the ability to have their voice heard. If millions of people willingly provide their input on the relatively inconsequential and mundane,[168] it

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163. *See supra* Section II.A.4.

164. *See supra* Section II.A.1.

165. *See, e.g.*, Drew DeSilver, *Turnout Soared in 2020 as Nearly Two-Thirds of Eligible U.S. Voters Cast Ballots for President*, PEW RSCH. CTR. (Jan. 28, 2021), https://www.pewresearch.org/fact-tank/2021/01/28/turnout-soared-in-2020-as-nearly-two-thirds-of-eligible-u-s-voters-cast-ballots-for-president/ [https://perma.cc/UCJ8-FSZ9].

166. *See, e.g.*, Daniel C. Esty & Quentin Karpilow, *Harnessing Investor Interest in Sustainability: The Next Frontier in Environmental Information Regulation*, 36 YALE J. ON REG. 625, 638–39 (2019) (referring to the "recent groundswell of interest in sustainability among mainstream investors" and discussing the structural obstacles to harnessing investors' interest in sustainability).

167. *See* Sergio Alberto Gramitto Ricci & Christina M. Sautter, *Corporate Governance Gaming: The Collective Power of Retail Investors*, 22 NEV. L.J. 51, 52–53 (2021) (discussing how the meme-stock phenomenon "laid the foundation . . . for an amplified retail shareholder voice by way of engaging with corporate governance").

168. *See, e.g.*, Shalee Fries, *Worst Toaster Ever*, AMAZON (Oct. 1, 2014), https://www.amazon.com/review/RXWU44AY16YWY [https://perma.cc/NJ26-6TGN] (amazon customer review). The reviewer detailed the following:

> [This is the] [w]orst toaster ever. I bought this [be]cause I liked how it looked but I can't ignore how poorly it works just [be]cause it's cute. It's very cheaply

stands to reason that if asked in a simple and straightforwardly structured manner, individuals would willingly provide input on some of society's most salient social, environmental, and economic questions.[169]

Thus, the problem with shareholder franchise is that it is poorly structured. Rather than enabling human investors to provide input quickly and easily, we have assembled a confusing, difficult to navigate, and overly burdensome system that is open only to the small minority of human investors who own stock directly. Although we have tools and resources to simplify and streamline proxy voting, we often fail to make them available to human investors.[170] Although we have mechanisms to bring concerns to management through shareholder proposals, we have kept those tools out of reach for the typical human investor.[171] Although human investors have collectively amassed an impressive ownership stake through a handful of index funds, these investors do not have any significant say in how that power is used.[172] It is clear that these systems were designed without a thought to how the average human investor's input might be solicited and utilized.

III. REIMAGINING SHAREHOLDER FRANCHISE

With a bit of reimagining, corporate governance could be restructured so as to give voice to human investors, simultaneously mitigating the problems of investors' perceived rational apathy and funds' ignorance of investors' true interests.[173] This reimagined version of shareholder

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> made. I also had to turn my bread over and toast it again to get it even. Then it'd be burned on one side and splotchy on the other side.

Id.

169. As a proof of concept, one index fund, simply referred to as INDEX, offers its shareholders the ability to complete a poll regarding their views on shareholder proposals and votes shares accordingly. *See The Original Index Fund. Reimagined.*, INDEX FUNDS, https://index.fund/ [https://perma.cc/T987-KWFB].

170. *See, e.g.*, *Proxy Exchange*, INST. S'HOLDER SERVS., https://www.issgovernance.com/solutions/proxy-voting-services/proxy-exchange [https://perma.cc/JB9K-RJLZ] (providing a service that "simplifies the proxy voting process" for institutional investors and enables "exception-based processing to automate the routine tasks, enabling your team to spend more time on the decisions and analyses that have bigger impact").

171. *See supra* Section II.A.2 (discussing limitations on human investors utilizing shareholder proposal process).

172. *See supra* Section II.A.1 (discussing how indirect human investors have been silenced in the proxy voting process).

173. Increased attention to proxy voting at investment funds can be seen in political action on the topic. For example, in 2021, Senator Tammy Baldwin and Congresswoman Pramila Jayapal introduced a bill designed to "allow workers to elect representative trustees who would manage their ERISA plan jointly with the employer's trustees and set voting guidelines that investment managers would be required to follow." Press Release, *Senator Baldwin, Congresswoman Jayapal Introduce Bicameral Legislation to Reverse Trump Administration*

franchise would intentionally focus on human investors as its starting point. This frame can be justified both by human investors' relatively low level of sophistication and by the fact that their interests very likely provide the best reflection of the interests of society as a whole. Rather than ignoring or silencing these valuable potential inputs into the corporate decision-making process, this approach would intentionally seek out these broad-based voices and perspectives.

This Part outlines what facilitating human investors' participation in corporate governance would look like in practice. It focuses on the Big Three index funds, as well as other mutual funds, given their role as the financial home of human investors[174] and their increasingly dominant role in the corporate governance ecosystem.[175] Any project to amplify human investors' voice in corporate governance must begin by identifying the contexts in which they have been ignored or silenced. These include (A) proxy voting, (B) engagements, (C) shareholder proposals, and (D) stewardship team representation. This Part explores how corporate governance could be reimagined to empower human investors in each of these four contexts.

A. *Proxy Voting*

1. Current Approach to the Best Interests Standard

The approach the Big Three and other similar fund managers currently take to proxy voting unnecessarily ignores the perspectives of the human investors on whose behalf these entities allegedly act. The law grants fund managers (and not the human investors whose money they invest) the right to vote at shareholder meetings, subject only to the limitations that they disclose certain information about their voting and that they vote in their investors' "best interests."[176] Despite this "best interests" requirement, the Big Three are not required to and, overwhelmingly, do not voluntarily undertake any effort to ascertain their investors'

Move to Silence Workers in Corporate America, TAMMY BALDWIN U.S. SENATOR FOR WISCONSIN (May 18, 2021), https://www.baldwin.senate.gov/news/press-releases/empowers-act-2021 [https://perma.cc/K2E9-4BS6] (discussing how change is needed to have human investors' voices heard). In addition, a group of senators brought a bill in 2022 seeking pass-through voting for essentially all passive funds above a certain size threshold, including those in ERISA plans. *See* INDEX Act, S. 4241, 117th Cong. (2022).

174. *See supra* notes 19–24 and accompanying text (discussing mutual funds as the "home" of human investors).

175. *See supra* Section II.B (discussing the increasing influence the Big Three and other mutual funds have over corporate governance).

176. Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, 68 Fed. Reg. 6564, 6565–67 (Feb. 7, 2003) (codified at 17 C.F.R. pts. 239, 249, 270, 274).

preferences and priorities.[177] How, then, do the Big Three and other fund managers divine their investors' best interests? There are three main possibilities, which this Article terms "absolute return," "bad faith," and "good faith guessing."

First, under the "absolute return" theory, funds have no need to learn their investors' preferences and priorities because funds assume that there is only one all-consuming interest: risk-adjusted financial returns. As the data presented in Section I.C suggest, this assumption may simply be untrue as an empirical matter for many investors. Human beings do not shed their humanity when they invest; rather, they balance the value of financial returns against important non-financial values.[178] Shareholder wealth maximization purists might respond that even if empirical evidence demonstrates that the majority of investors favor certain non-financial interests, it is normatively worse to pursue them.[179] Under this view, if given the opportunity to costlessly bargain, investors would agree only to pursue profit.[180] Thus, profit serves as a sort of least common denominator that unites all investors, making it the most desirable goal.[181] However, as a general proposition, a rule prohibiting prosocial behavior to protect the least prosocial is normatively undesirable. If investors want to use their money for prosocial purposes, there is a strong normative argument that corporate law should encourage rather than discourage

177. *See* Griffin, *supra* note 38, at 178; Caleb N. Griffin, *We Three Kings: Disintermediating Voting at the Index Fund Giants*, 79 MD. L. REV. 954, 975, 988, 1002 (2020). BlackRock recently announced that it is "working with a digital investor communications platform in the UK to enable investors in select mutual funds to exercise choice in how their portion of eligible shareholder votes are cast." Larry Fink, *The Transformative Power of Choice in Proxy Voting*, BLACKROCK, https://www.blackrock.com/corporate/about-us/investment-stewardship/blackrock-voting-choice/proxy-voting-power-of-choice [https://perma.cc/NJY8-HQT4]. It has pledged to allow some level of individual investor input more broadly at an unspecified point in the future, although it is unclear exactly what that level of involvement will be. *See id.* Additionally, Vanguard plans to begin "a trial to give retail clients more say over how their shares are voted at corporate meetings" in early 2023. Silla Brush, *Vanguard to Test Giving Retail Investors More Voting Power*, BLOOMBERG (Nov. 2, 2022, 7:30 AM), https://www.bloomberg.com/news/articles/2022-11-02/vanguard-to-test-giving-retail-investors-more-voting-power [https://perma.cc/9DQR-QUNH]. The exact nature of investors' involvement is uncertain, although it appears Vanguard plans to test multiple approaches to soliciting investor input. *See id.*

178. *See, e.g.*, Virginia Harper Ho, *"Enlightened Shareholder Value": Corporate Governance Beyond the Shareholder-Stakeholder Divide*, 36 J. CORP. L. 59, 80–85 (2010) (discussing shareholders' non-financial values).

179. *See* Michael C. Schouten, *The Mechanisms of Voting Efficiency*, 2010 COLUM. BUS. L. REV. 763, 773 ("When shareholders have heterogeneous preferences and some vote with a view to maximizing their private interests rather than their pro-rata share of the firm's future cash flows, the probability that a majority of the shares is voted for the correct option decreases dramatically.").

180. Bainbridge, *supra* note 93, at 578–79 (discussing the optimal default rule in the context of corporate governance).

181. *See id.*

such behavior.[182] Moreover, as is true in virtually every aspect of modern corporate law, unanimous support should not be a prerequisite to a popular course of action.[183]

Under the "bad faith" theory, the Big Three do not even attempt to mirror their investors' interests or preferences in their proxy voting behavior. They simply vote in whatever manner maximizes their own welfare. A standard agency cost model suggests that such conduct occurs to one degree or another.[184] Without any accountability mechanism, some percentage of agents will take self-interested actions that impose costs on their principals.[185] For instance, the Big Three derive substantial revenue from managing the retirement plans of many of the corporations at which they also vote as shareholders (e.g., say-on-pay votes on the compensation of the managers who hire them), and they may vote in ways that favor incumbent management so as not to jeopardize this income stream.[186] Because the financial impact of many governance issues is difficult to measure, and because the Big Three do not publish any data on their investors' preferences and priorities, it is effectively impossible to hold the Big Three accountable for votes that do not align with their investors' interests.[187] In point of fact, rarely, if ever, has a fund been found to have violated the "best interests" standard due to its proxy voting behavior.[188]

Finally, there is the more charitable, "good faith guessing" theory, which holds that the Big Three try diligently to infer or guess their investors' interests and attempt to pursue those interests with their voting behavior. Problematically, however, there is precious little for the Big Three to go on with these "guesses," and, as such, their guesses are highly

182. *See, e.g.*, Hart & Zingales, *supra* note 85, at 201–03 (discussing the separability problem, or the fact that prosociality cannot be neatly separated from profit without significant inefficiencies).

183. *See, e.g.*, Lisa M. Fairfax, Essay, *Just Say Yes? The Fiduciary Duty Implications of Directorial Acquiescence*, 106 IOWA L. REV. 1315, 1326–27 (2021) (discussing different voting standards applicable in corporate law, such as majority and supermajority voting standards).

184. *See* Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 308–10 (1976) (defining the concepts of an agency relationship and agency costs).

185. *Id.* at 308.

186. For example, a Proxy Disclosure states that:

> Moreover, in some situations the interests of a mutual fund's shareholders may conflict with those of its investment adviser with respect to proxy voting. This may occur, for example, when a fund's adviser also manages or seeks to manage the retirement plan assets of a company whose securities are held by the fund.

Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, 68 Fed. Reg. 6564, 6565 (Feb. 7, 2003).

187. *See* Griffin, *supra* note 38, at 178.

188. *See id.*

vulnerable to error, prejudice, and motivated reasoning.[189] In addition, evidence from the Big Three's voting behaviors for their ESG funds suggests that the good faith guessing theory is unlikely.[190] Despite the strong statement of their personal values that investors make by selecting ESG funds, Vanguard and State Street have voted their ESG funds and traditional funds identically, and all three of the Big Three vote both ESG funds and traditional funds in ways that are less supportive of ESG than several of their competitor index funds.[191] One would expect that fund representatives would easily be able to infer that, relative to traditional investors, ESG investors would prefer voting that more strongly advanced ESG outcomes—but that is often not born out in practice.[192]

Ultimately, each of these scenarios presents its own conundrums. The absolute return theory espouses an artificially narrow and, in some cases, empirically flawed view of investors' interests that actively prohibits investors from pursuing nonfinancial but prosocial goals. As to the bad faith theory, there are obvious negative social consequences generated by agents acting with subjective bad faith. Finally, perhaps there is a genuine attempt by the Big Three to guess at investors' preferences, but it is likely to be a highly uninformed guess given very limited investor input.

This uninformed and potentially self-interested approach to "stewardship" makes sense when examining the incentives currently facing the Big Three: if discerning true investor preferences is even a bit costly for funds, if they sell essentially commoditized index offerings that compete largely on price, and if they face effectively zero risk of negative consequences, if they fail to discern investors' actual preferences, then ignoring investors' preferences may optimize their private welfare.[193] However, this produces suboptimal effects at the level of society as a whole. When investors are willing but unable to vote their investments in prosocial ways, society may be worse off than it would be if investors were unconstrained.[194] There is, effectively, an artificial cap on investor altruism. Like price ceilings, this cap may also generate deadweight loss. Whatever efficiency gains a singular focus on profit may generate,

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189. *See, e.g.*, Ulrike Malmendier & Geoffrey Tate, *Behavioral CEOs: The Role of Managerial Overconfidence*, 29 J. ECON. PERSPS. 37, 40–58 (2015) (analyzing decision-making in the field of corporate management and finding that cognitive biases lead to poorer outcomes).

190. *See* Griffin, *supra* note 38, at 204–05.

191. *Id.*

192. *See id.*

193. *See Trends in the Expenses and Fees of Funds, 2020*, 27 ICI RSCH. PERSP. at 1, 1–2 (Mar. 2021), https://www.ici.org/doc-server/pdf%3Aper27-03.pdf [https://perma.cc/RB7Z-JUBX] (finding evidence of downward pressure on mutual fund fees in recent years).

194. *See generally* Ernst Fehr & Urs Fischbacher, *The Nature of Human Altruism*, 425 NATURE 785 (2003) (discussing the significance of human altruism and noting that even "a minority of altruists can force a majority of selfish individuals to cooperate or, conversely, a few egoists can induce a large number of altruists to defect").

policymakers should carefully weigh such gains against the costs of placing an artificial ceiling on altruism.

The data in Section I.C suggest the potentially significant extent to which investors desire to vote in prosocial ways. However, large asset managers appear to have little interest in the views of their human investors. Cynically, learning what their investors actually want would reduce index funds' discretion, power, and autonomy—the funds would be constrained to do what their investors had expressed. Why would the large asset managers, particularly the Big Three, voluntarily give up their enormous power over corporate governance at virtually every publicly traded company? Moreover, why would they incur unnecessary costs that go beyond what the law requires? As long as the current, toothless interpretation of the "best interests" standard remains unchanged, they probably never will.

2. The Best Interests Standard, Reinterpreted

This Article proposes that the SEC reinterpret the best interests standard.[195] Under this proposal, discerning the best interests of investors would require seeking investors' input. Specifically, the SEC should adopt a rule providing as follows:

> Voting proxies in the best interests of fund shareholders requires that registered management investment companies make a good-faith effort to (a) seek investors' input on important issues related to how their investment is voted, (b) publish such input in a form that facilitates comparison with the firm's proxy voting record, and (c) vote in reasonable accord with such input. In the event that a fund shareholder opts not to provide input, the shares representing their economic interest should be voted proportionately in the shares for which input was received.[196]

195. In the alternative, pass-through voting could also be mandated through Congressional action. Ideally, such legislation would mandate that mutual funds adopt "vote outsourcing" (discussed below) or semi-specific, issue-based (i.e., "categorical") pass-through voting, which would enable human investors to provide input on broad categories of highly salient topics. Investors' input would then be applied to firm-level votes each time the relevant topic was at issue. For example, an investor would have the ability to indicate their support or opposition to all climate disclosure proposals, and the mutual fund would vote the shares indirectly owned by that investor accordingly. An analogous proposal, the INDEX (Investor Democracy Is Expected) Act, is currently under consideration by Congress. *See* INDEX Act, S. 4241, 117th Cong. § 2 (2022). Although the INDEX Act clearly mandates pass-through voting, it does not require categorical pass-through voting. *See id.* However, the language appears broad enough to permit such voting, given the breadth of the term "voting instructions" left undefined in the bill. *See id.*

196. Other types of mirror voting are possible. *See, e.g.*, Jill E. Fisch, *Mutual Fund Stewardship and the Empty Voting Problem*, 16 BROOK. J. CORP. FIN. & COM. L. 71, 94 (2021)

Despite its profound implications, this is in many ways a modest proposal. It does not attempt to mandate how a fund might seek investor input; there are myriad ways to collect and communicate information, and the exact mechanisms should be left indeterminate to allow for experimentation and to facilitate private ordering. Nor does it mandate the frequency or content of such communications or solicitations. Additionally, although "investors' input" is required, input from all investors is not. Investors have no specific input rights, and techniques such as representative sampling are fully acceptable. Further, the proposal does not attempt to define "important issues;" different issues will be more or less relevant for different funds based on heterogeneous holdings and investor bases. Overall, the "good faith" language is key—funds, as agents, should make good faith, reasonable efforts to identify their investors' interests and to responsibly act on that information.

There are three basic ways that funds could "seek investor input," per the language of this proposal: "pure" pass-through voting, semi-specific pass-through voting, and vote outsourcing. First, in "pure" pass-through voting, fund managers would seek granular investor input on every ballot item at every election for every company in every fund.[197] This approach would be unduly burdensome for most investors. An investor in an S&P 500 index fund would have to cast several thousand votes each year, and those with larger indexed holdings would face an even greater burden.[198]

Semi-specific or "categorical" pass-through voting represents a better option. This method does not require input on the many thousands of ballot items under consideration; rather, it permits semi-specific investor input on broad categories of salient issues, such as board diversity,

(discussing mirror voting in which institutional investors would "vote their shares in the same proportion as direct retail investors"). Although, as with the rules requiring N-PX publication, no exemption for smaller entities is present in this proposal, one could be included. However, much of the Commission's reasoning for not including an exemption in the N-PX context is also applicable here. *See* Disclosure of Proxy Voting Policies, *supra* note 34, at 6580. The Commission explained that:

> Different disclosure requirements for small entities, such as reducing the level of proxy voting disclosure that small entities would have to provide shareholders, may create the risk that those shareholders would not receive sufficient information to make an informed evaluation as to whether the fund's board and its investment adviser are complying with their fiduciary duties to vote proxies of portfolio securities in the best interest of fund shareholders.

Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, 68 Fed. Reg. 6564, 6565 (Feb. 7, 2003).

197. *See Considering the Index Fund Voting Process: Hearing Before the S. Comm. on Banking, Hous., and Urb. Affs.*, 117th Cong. 12 (2022) (testimony of John C. Coates IV & John F. Cogan, Jr.), https://www.banking.senate.gov/imo/media/doc/Coates%20Testimony%206-14-22.pdf [https://perma.cc/KKK3-6Y2U].

198. *See id.*

political spending, or climate disclosures. Stewardship teams will then take this semi-specific input (e.g., "vote yes on all climate disclosure proposals") and apply it to specific, firm-level votes. Such semi-specific, categorical input greatly reduces the time and effort human investors would need to expend to meaningfully impact voting outcomes. This approach also preserves an element of discretion for fund managers in interpreting how to apply issue-based preferences to specific ballot items or director elections.

Finally, perhaps the simplest way fund managers could both comply with the proposal and solve the problem of efficiently aggregating investors' preferences is through "vote outsourcing." Rather than retaining proxy voting authority for themselves, fund managers would allow investors to delegate voting authority to a third party. This approach would enable investors to reap the benefits of third-party research on ballot items while retaining the agency to select a representative that aligns with their values. Additionally, adoption of "vote outsourcing" by large asset managers could prompt a wider range of entities to provide proxy voting recommendations, as many nonprofit groups are already actively involved in the proxy voting process.[199]

Relatedly, input from investors should also guide decisions regarding whether funds recall their shares for votes.[200] Where an annual meeting only addresses mundane matters or topics without a clear consensus amongst the fund's investors, the benefits of a recall may be outweighed by the revenue available from continuing to loan out those shares. In contrast, where investors strongly desire a particular course of action on a given ballot item, the benefits of a recall may be more likely to outweigh the revenue from loaning out shares.

The proposal also requires that funds publish the information gleaned from investors in some form to increase transparency and to empower investors to hold funds accountable for their stewardship activities. Publication of investor input in summary form should be acceptable and encouraged; the goal is to provide a high-level way to judge fund performance—do the fund's actions broadly reflect investors' input? A user-friendly way to fulfill this requirement would be to display summary data on investors' preferences based on the results of a survey or other

199. For example, the nonprofit As You Sow already provides a proxy advisory service, called As You Vote, wherein shareholders can subscribe and automatically have their votes cast according to recommendations curated by the nonprofit. *As You Vote — A New Proxy Voting Service from As You Sow*, AS YOU SOW (Mar. 17, 2021), https://www.asyousow.org/press-releases/2021/3/17/as-you-vote-a-new-proxy-voting-service-as-you-sow [https://perma.cc/T2HG-RK9G].

200. *See* Edwin Hu et al., *The Index-Fund Dilemma: An Empirical Study of the Lending-Voting Tradeoff* 11–12 (Columbia Univ. L. Sch. Ctr. for L. and Econ. Studs., Working Paper No. 647, 2020), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3673531 [https://perma.cc/5792-R8T4].

sampling effort in broad categories[201] (such as "political contribution transparency" or "climate change disclosures") alongside summary statistics for the funds' voting record on these same categories.[202] For example, such disclosures might show that seventy-five percent of respondents supported political contribution transparency, which would be published alongside data showing that the fund voted in favor of twenty-five out of thirty political contribution transparency proposals in the most recent proxy year. Funds could also provide an explanation where votes seemingly contradict investor input, such as a brief statement outlining the fund's reasoning for voting against a particular proposal. Funds could update the data in real time or in a reasonable period after the vote.[203]

In addition, the SEC should monitor and enforce compliance with this revised best interest standard using the published data on investors' input and funds' voting records. Liability should attach only in extreme cases. A loose analogy to the Delaware judiciary's *Caremark* jurisprudence is instructive.[204] *Caremark* held that only a "sustained or systematic failure of the board to exercise oversight—such as an utter failure to attempt to assure a reasonable information and reporting system exists—will establish the lack of good faith that is a necessary condition to liability."[205] Similarly, under this proposal, funds must "attempt to assure [that] a reasonable information and reporting system exists." In this context, the reporting system will be focused on investor input rather than corporate misconduct. However, only a "sustained or systematic failure" to implement and act upon appropriate investor input mechanisms will result in liability. One example of such a failure would be a significant, sustained, and unjustified divergence between investor input and fund voting behavior. Ultimately, this proposal is not designed to provide individual investors with granular control over their investments; rather,

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201. The SEC has recently created a categorization framework for reporting the matters on which funds have voted. These categories could be useful starting points for funds, but funds should be permitted to create their own categories that are more responsive to their investors' interests. *See* Enhanced Reporting of Proxy Votes by Registered Management Investment Companies; Reporting of Executive Compensation Votes by Institutional Investment Managers, 86 Fed. Reg. 57478, 57486 (proposed Oct. 15, 2021) (to be codified at 17 C.F.R. pts. 232, 240, 249, 270, 274).

202. Some nonprofits already organize and display voting information in this category-based fashion. *See, e.g.*, *Shedding Light*, *supra* note 131.

203. *See generally* James McRitchie, Rulemaking Petition for Real-Time Disclosure of Proxy Votes (Mar. 15, 2019) (unpublished manuscript), https://ssrn.com/abstract=3353456 [https://perma.cc/3END-XBBZ] (arguing that real-time disclosure of proxy votes will "revolutionize how such information is shared, allowing much wider participation in the development of corporate strategies and practice").

204. *See* In re Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 971 (Del. Ch. 1996).

205. *Id.*

it is designed to aggregate the preferences of human investors to grant them a meaningful voice in the corporate world.

3. Proxy Voting Reimagined: A Practical Example

What would it look like in practice if the Big Three[206] sought investor input[207] on proxy voting decisions? This Article provides some illustrative examples for shareholder proposals in the following five categories: (1) political contribution transparency, (2) lobbying transparency, (3) gender pay gap disclosures, (4) climate change reporting, and (5) human rights reporting. These types of proposals are relatively common. S&P 500 companies considered seventy-seven such proposals in the 2019–2020 proxy season,[208] sixty-one in the 2020–2021 proxy season,[209] and ninety in the 2021–2022 proxy season.[210] These proposals are largely unsuccessful: 87% of these proposals in the 2019–2020 proxy season, 90.1% in the 2020–2021 proxy season, and 87% in the 2021–2022 proxy season failed to receive majority support.[211]

The Big Three infrequently support proposals in any of these categories. As Figures 4–6 below reveal, Vanguard supported less than 25% of proposals in all categories, except climate change reporting in two proxy seasons. Similarly, BlackRock generally supported less than a quarter of all proposals and always supported less than half of all proposals. State Street was more consistently supportive of these proposals, but overall supported the minority of such proposals with the exception of political contribution transparency proposals in only the

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206. This Article's proposals focus on voting and other reforms at mutual funds generally. However, because the Big Three (Vanguard, BlackRock, and State Street) are noted for their large and often determinative impact on voting behaviors at large public companies, this section highlights the impact that the proposed reforms would have on voting at these three asset managers. *See, e.g.*, Bebchuk & Hirst, *supra* note 23.

207. BlackRock has already begun to institute a form of pass-through voting. *See Working to Expand Proxy Voting Choice for Our Clients*, BLACKROCK (Oct. 31, 2021), https://www.blackrock.com/corporate/about-us/investment-stewardship/2021-blackrock-voting-choice [https://perma.cc/VZG2-767L]. To date, this input mechanism is only available to its institutional clients, rather than individual human investors. *See id.* Nevertheless, its existence provides evidence regarding the feasibility of pass-through voting at large index funds.

208. *See* iShares Trust, Annual Report of Proxy Voting Record of Registered Management Investment Company (Form N-PX) (Aug. 17, 2020), https://www.sec.gov/Archives/edgar/data/1100663/000119312520232632/d30829dnpx.txt [https://perma.cc/2XTH-XGQ2].

209. *See* iShares Trust, Annual Report of Proxy Voting Record of Registered Management Investment Company (Form N-PX) (Aug. 27, 2021), https://www.sec.gov/Archives/edgar/data/1100663/000119312521258978/d176642dnpx.txt [https://perma.cc/Y4BM-S2T3].

210. *See* iShares Trust, Annual Report of Proxy Voting Record of Registered Management Investment Company (Form N-PX) (Aug. 15, 2022), https://www.sec.gov/Archives/edgar/data/1100663/000119312522229742/d385092dnpx.txt [https://perma.cc/NJ7E-AR24].

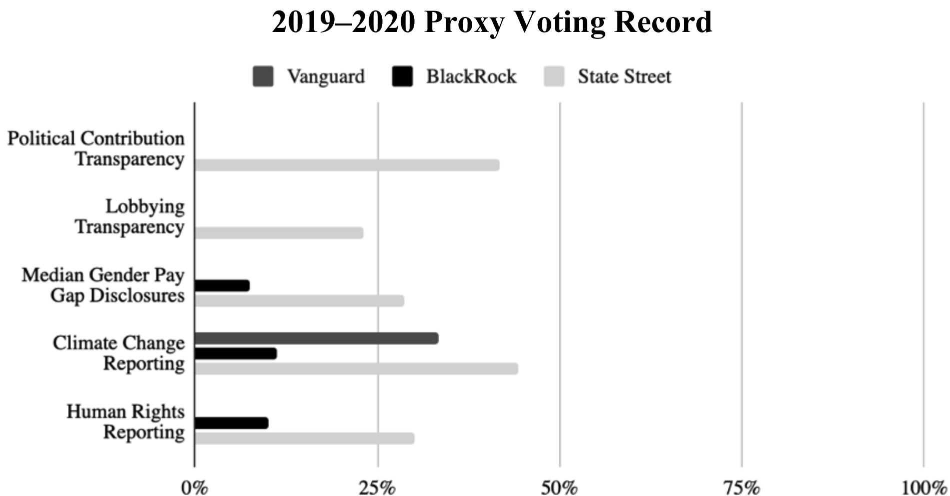
211. Calculations and data on file with the author.

2020–2021 proxy season. As detailed below, this voting behavior appears to diverge from investors' self-reported best interests.

Figures 4–6: Big Three Support of Shareholder Proposals by Topic

These figures summarize the voting records of the S&P 500 index funds at Vanguard,[212] *BlackRock,*[213] *and State Street*[214] *on five common categories of shareholder proposal topics at issue during the 2019–2020, 2020–2021, and 2021–2022 proxy seasons.*

2019–2020 Proxy Voting Record

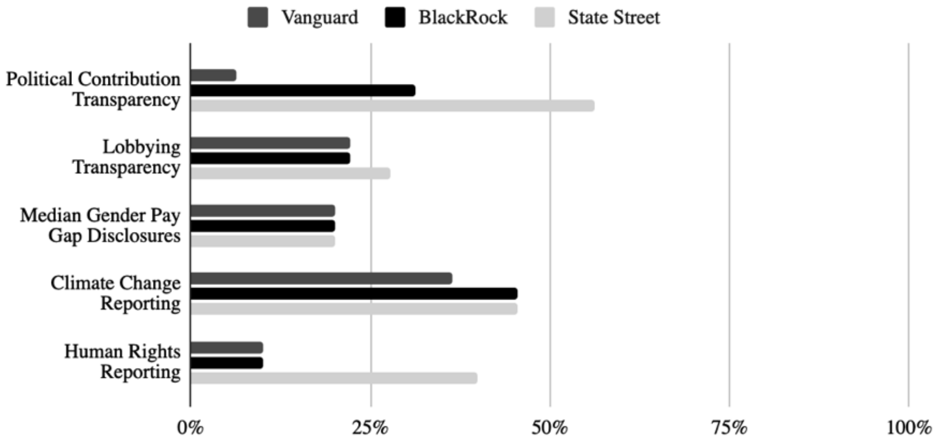


212. Vanguard Index Funds, Annual Report of Proxy Voting Record of Registered Management Investment Company (Form N-PX) (Aug. 27, 2020), https://www.sec.gov/Archives/edgar/data/36405/000110465920099318/tm2026413-11_npx.txt [https://perma.cc/7C FS-ZL8X] (for data form the 2019 to 2020 proxy season); Vanguard Index Funds, Annual Report of Proxy Voting Record of Registered Management Investment Company (Form N-PX) (Aug. 27, 2021), https://www.sec.gov/Archives/edgar/data/36405/000110465921110299/tm2121856d3_npx.txt [https://perma.cc/4567-MK7M].(for data from the 2020 to 2021 proxy season); Vanguard Index Funds, Annual Report of Proxy Voting Record of Registered Management Investment Company (Form N-PX) (Aug. 26, 2022), https://www.sec.gov/Archives/edgar/data/36405/0001104659 22094602/tm2221142d1_npx.txt [https://perma.cc/UPQ3-2MNW] (for data from the 2021–2022 proxy season).

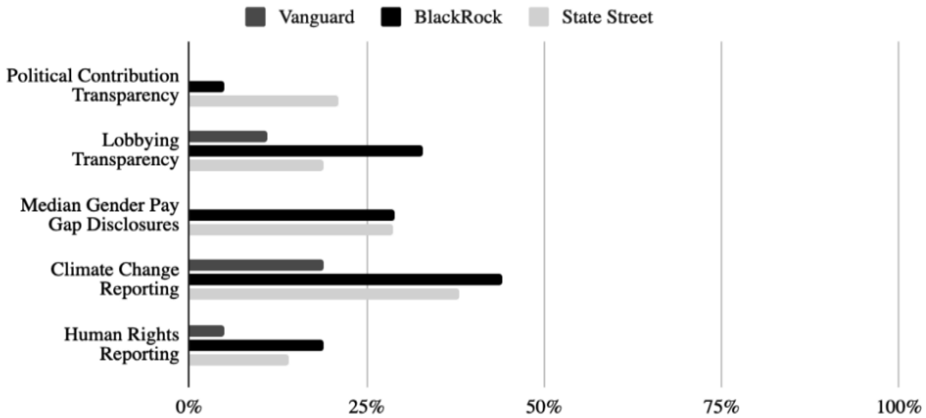
213. iShares Trust, *supra* notes 208 (for the 2019–2020 proxy season), 209 (for the 2020–2021 proxy season), and 210 (for the 2021–2022 proxy season).

214. SSGA FUNDS, ANNUAL REPORT OF PROXY VOTING RECORD OF REGISTERED MANAGEMENT INVESTMENT COMPANY (FORM N-PX) (Aug. 17, 2020), https://www.sec.gov/Archives/edgar/data/826686/000119312520233195/d26548dnpx.txt [https://perma.cc/LFB7-UQ D3] (for data from the 2019–2020 proxy season); SSGA FUNDS, ANNUAL REPORT OF PROXY VOTING RECORD OF REGISTERED MANAGEMENT INVESTMENT COMPANY (FORM N-PX) (Aug. 27, 2021), https://www.sec.gov/Archives/edgar/data/0000826686/000119312521258991/d161999 dnpx.htm [https://perma.cc/PK4Z-WLLE] (for data from the 2020–2021 proxy season); SSGA Funds, Annual Report of Proxy Voting Record of Registered Management Investment Company (Form N-PX) (Aug. 25, 2022), https://www.sec.gov/Archives/edgar/data/826686/00011931 2522230056/d319918dnpx.htm (for data from the 2021–2022 proxy season).

2020–2021 Proxy Voting Record



2021–2022 Proxy Voting Record

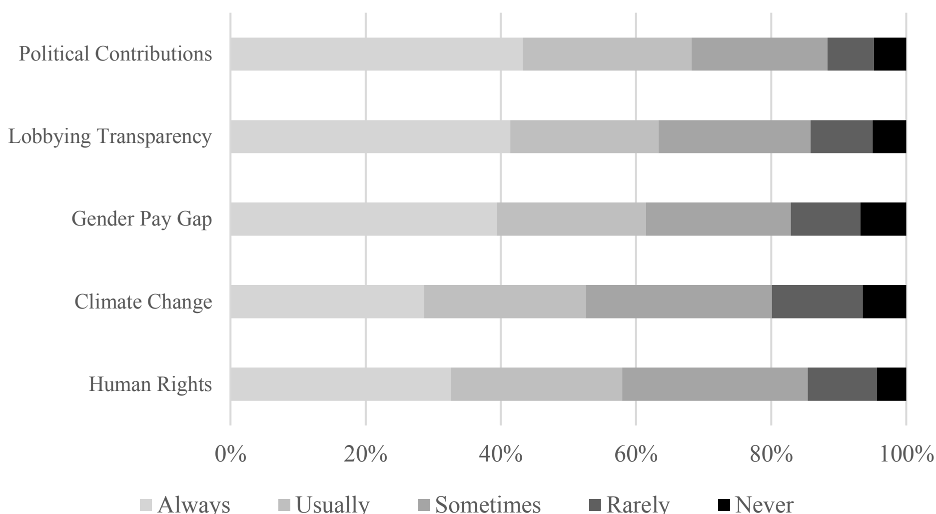


Under the revised corporate governance model described above, funds would be required to seek input from investors before voting on these types of shareholder proposals. One route funds could take to gain insight into investors' views on these issues would be to directly seek their input through a survey. As an example of what this would look like, this Article presents original survey data on mutual funds owners' support for initiatives related to political contribution transparency, lobbying transparency, median gender pay gap disclosures, climate change reporting, and human rights reporting. As Figure 7 below reveals,

investors are highly supportive of these five initiatives. The majority of respondents would "always" or "usually" support proposals in all five categories.

Figure 7: Investor Support of Shareholder Proposals by Topic

This chart summarizes the results of a survey of 1,611 index fund and/or ETF owners who were asked to provide their views on common shareholder proposal topics. The margin of error is +/- 2.491%.



Investors' preferences on these topics diverge significantly from the voting behaviors of their representatives. For example, while nearly two-thirds of respondents would *always* or *usually* support political contribution transparency proposals, these proposals were rarely supported (generally less than 25% of the time) in the proxy seasons studied. Likewise, despite investors' strong support for median pay gap reporting proposals, funds supported such proposals only in limited circumstances (ranging from 0% to 28.6% in all three proxy seasons studied). Surprisingly, although the most popular proposals for investors were political contribution transparency, lobbying transparency, and gender pay gap disclosures, the Big Three were relatively less supportive of these categories of proposals. In contrast, index fund providers were most supportive of climate change reporting proposals, which received the lowest level of support amongst investors. These data suggest that a disconnect exists between the relative desirability of a given proposal amongst investors and index fund voting as currently practiced.

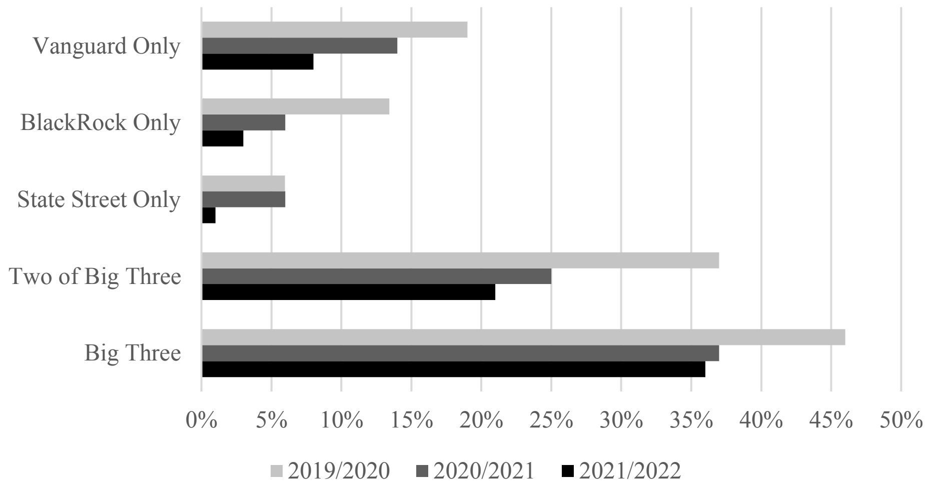
What would happen if the Big Three were held accountable to investors' views? First, the Big Three might undertake a survey similar to the one conducted above, and they would publish the results from that study. The results would provide useful information that would help guide voting behaviors, and rates of support for the five proposals studied would likely increase substantially. Additionally, because the aggregate survey data would be made public, investors would be better able to hold their representatives accountable. For instances of extreme deviations from investors' input, the SEC would have the authority to investigate and bring enforcement actions based on these discrepancies.

This approach would clearly increase the alignment between investor preferences and Big Three voting behaviors. However, would it make any practical difference? As Figure 8 below demonstrates, increased support by the Big Three would have made a significant and determinative impact on the fate of many of the proposals discussed above. Vanguard alone caused 19% of proposals in the studied categories to fail in 2019–2020, 14% to fail in 2020–2021, and 8% to fail in 2021–2022. If two of the Big Three had better aligned their votes with investors' views, more than one-in-three failing proposals would have achieved majority support in 2019–2020, more than one-in-four failing proposals would have passed in 2020–2021, and more than one-in-five failing proposals would have passed in 2021–2022. If all of the Big Three voted in alignment with investor preferences, more than four-in-ten failing proposals would have received majority support in 2019–2020 and more than one-third would have received majority support in 2020–2021 and 2021–2022. Given that strong minority support often leads a firm to proactively implement the proposal under consideration, these rates likely understate the impact of this Article's proposals on the outcome of common ballot items.[215]

215. *See* Virginia Harper Ho, *Nonfinancial Risk Disclosure and the Costs of Private Ordering*, 55 AM. BUS. L.J. 407, 420 (2018).

Figure 8: Estimated Impact of Big Three Opposition

This table provides an estimate[216] *of the portion of shareholder proposals related to political contribution transparency, lobbying transparency, gender pay gap disclosure, climate change disclosure, and human rights reporting proposals that would have achieved majority support but for the opposition of one or more of the Big Three.*



216. Data on the negative impact of the Big Three's votes on the outcomes of unsuccessful political contribution transparency proposals were calculated by taking the overall rates of support for the unsuccessful shareholder proposals (those receiving less than majority support) and adding (for proposals that were opposed) or ignoring (for proposals that were supported) the percentage ownership for each of the Big Three in the company where the proposal was under consideration. The overall rates of support for shareholder proposals were calculated as reported by Proxy Monitor (for firms within the Fortune 250) or as reported by the firm in the relevant 8-K document (for firms outside the Fortune 250). The ownership data was gathered based upon the outstanding share ownership data reported by Morningstar as of June 18, 2021 (for proxy seasons 2019–2020 and 2020–2021) and CNN Money as of October 1, 2022 (for the 2021–2022 proxy season). The accuracy of these calculations depends upon two assumptions. First, this approach depends on the assumption that the votes casted by the S&P 500 index fund for each of the Big Three accurately represent the votes casted by all of the funds controlled by the fund family as a whole. Prior research suggests that the funds controlled by the Big Three exhibit very high internal agreement, making this a well-founded assumption. *See, e.g.*, Jan Fichtner et al., *Hidden Power of the Big Three? Passive Index Funds, Re-Concentration of Corporate Ownership, and New Financial Risk*, 19 BUS. & POL. 298, 316–17 (2017). Second, these figures assume that a proposal failed if it received half or less than half of votes casted and succeeded if it received more than half of votes casted. While a reasonable assumption, there are exceptions where companies have different voting thresholds, such as supermajority requirements. *See, e.g.*, Tim Higgins, *Tesla Board Fails to Pass Supermajority Measure It Proposed Amid Call for More Oversight*, WALL ST. J. (June 12, 2019, 2:27 PM), https://www.wsj.com/articles/tesla-shareholders-rejectmeasure-to-eliminate-super-majority-vote-requirement-11560290775 [https://perma.cc/JWZ4-2J8E] (discussing Tesla's requirement that proposals receive "two-thirds approval from all shares outstanding").

As it currently stands, the Big Three may not adequately represent their investors' views on political contribution transparency, lobbying transparency, median gender pay gap disclosures, climate change disclosures, and human rights reporting proposals. However, if they were to monitor their investors' views and align voting behaviors with those views, the Big Three's voting record would change substantially. Such a change would ensure that dozens more shareholder proposals on important topics would pass each proxy season. Given the influence of the Big Three over virtually all of the world's largest public companies, the social, economic, and environmental impact of such a change would be significant.

B. *Shareholder Proposals*

1. Shareholder Proposals Reimagined

Human investors are also underrepresented in the submission of shareholder proposals. Under the status quo, indirect investors do not have the right to bring shareholder proposals on their own behalf, and the Big Three neglect to bring such proposals on behalf of their investors.[217] A reformed approach to shareholder proposals would empower human investors to voice their concerns to management. In practice, this approach would be facilitated by the Big Three and other institutional investors.

First, the Big Three and other similarly positioned institutional investors would actively solicit investor input on potential shareholder proposal topics. Unlike the more onerous process for formal shareholder proposals, this input could be shared in a more casual, user-friendly manner. Although, as discussed above, no particular form of input should be mandated to allow for experimentation and innovation, funds might choose to seek input on shareholder proposals as part of a broader survey, in the form of a very brief one- or two-question, issue-specific survey, or in an unstructured format in the form of a brief message submitted through a chat box. For instance, in the case of the chat box, an investor could identify their concerns regarding a particular company, industry, or issue related to their portfolio (as simple as "plastic bag use at Walmart" or "palm oil use in consumer goods"). The goal is not for investors to craft formal shareholder proposals, but rather to put issues they view as important on the radar of the stewardship team.

Investor stewardship team members would be charged with reviewing and assessing investors' input, and they would have an element of discretion to identify the handful of issues that were particularly meritorious, significant, and reflective of their investors' values.

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217. *See* Bebchuk & Hirst, *supra* note 37, at 2104.

Stewardship teams would then be charged with researching and drafting formal shareholder proposals on the selected issues. In addition, they would also research the relevant companies where they could submit such a proposal—while some proposals will be firm-specific, others may have a market-wide impact. Stewardship teams would be able to consult with outside resources and agents, such as proxy advisors, to facilitate this research process.

Although this streamlined route would be open only to indirect investors, the barriers to access for investment in, e.g., an index fund are far lower than for submission of a traditional shareholder proposal.[218] Indeed, there may even be a market advantage for early adopters of this shareholder proposal submission process, with socially conscious individuals gravitating towards funds offering this input mechanism, much as they have gravitated towards ESG funds more broadly.

2. A Practical Example: Paid Parental Leave

This Section provides an example of what a modernized approach to shareholder proposals could look like, focusing on the issue of paid parental leave. Americans widely support paid parental leave following the birth or adoption of a child.[219] Despite this support, federal law does not mandate that employers provide paid parental leave.[220] As a result, six-in-ten public companies in the United States do not provide paid leave to parents,[221] and the negative effects of the lack of parental leave are well documented.[222] One route to increasing paid leave for parents is, of course the political process. However, as is often the case, politicians have been slow to act on this issue.[223] Meanwhile, babies are still being

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218. *See supra* notes 133–34 and accompanying text for a discussion of increased barriers to the submission of shareholder proposals.

219. Juliana Menasce Horowitz et al., *Americans Widely Support Paid Family and Medical Leave, but Differ Over Specific Policies*, PEW RSCH. CTR. (Mar. 23, 2017), https://www.pewresearch.org/social-trends/2017/03/23/americans-widely-support-paid-family-and-medical-leave-but-differ-over-specific-policies/ [https://perma.cc/3AYR-JCFM].

220. The federal Family and Medical Leave Act (FMLA) requires eligible employers to offer unpaid family leave. *See* 29 U.S.C. § 2654 (explaining that the Secretary of Labor is responsible for making regulations in line with the FMLA); 29 U.S.C. § 2612 (outlining the requirements for unpaid family leave).

221. Emily Ferreira & Rich Fuerstenberg, *The Pressure Is on to Modernize Time-Off Benefits: 6 Survey Findings*, MERCER (Jan. 16, 2019), https://www.mercer.us/our-thinking/healthcare/the-pressure-is-on-to-modernize-time-off-benefits-6-survey-findings.html [https://perma.cc/9K45-A52G].

222. *See* Claire Cain Miller, *Stressed, Tired, Rushed: A Portrait of the Modern Family*, N.Y. TIMES (Nov. 4, 2015), https://www.nytimes.com/2015/11/05/upshot/stressed-tired-rushed-a-portrait-of-the-modern-family.html [https://perma.cc/8R76-JDLH].

223. *See* Tamara Keith, *Paid Parental Leave: How Republicans Learned to Love A Democratic Priority*, NPR (Dec. 13, 2019, 5:00 AM), https://www.npr.org/2019/12/13/787631

born, and parents at six-in-ten companies continue to suffer financially, physically, and psychologically from the lack of support.

What would it look like if we had a robust shareholder franchise system designed to solicit investors' input on critical issues such as parental leave? To start, imagine, as is extraordinarily likely, that some of the investors who have entrusted their savings to Vanguard care passionately about this topic. One or more of them might use Vanguard's shareholder proposal solicitation feature to submit their concerns to Vanguard's stewardship team by filling out an online form or typing a sentence or two in a chat box. Such an activity would take just a few minutes, as all that would be involved would be writing a one- or two-sentence description of the potential proposal topic.

Vanguard's stewardship team would then review this and other submissions, and, as part of their good-faith effort to act on investor input, the team might select parental leave as an important topic for stewardship activities in the coming years. The stewardship team would use its resources to research parental leave policies and would be responsible for fleshing out the details of a draft shareholder proposal on the subject. Perhaps they might propose a shareholder resolution requesting that companies prepare a report evaluating the potential negative impact that the lack of paid family leave has on employee wellbeing, retention, and equity.[224] The stewardship team could submit such a proposal to all U.S. companies in the S&P 500 lacking an existing paid parental leave policy. The stewardship team would use their resources and expertise to submit this proposal in the proper manner and at the proper time for all applicable companies. In addition, they would engage with companies about the issue of paid parental leave, and they would disclose these communications to their investors in the interest of transparency. Vanguard would vote its shares in accordance with investors' views on paid parental leave.

It may turn out that this proposal is successful only at a handful of relevant companies in its first incarnation, but Vanguard would be able to resubmit the proposal in subsequent years. Eventually, many of the world's largest companies might come to adopt paid parental leave policies, either pre-emptively because of pressure from Vanguard during engagements or after a formal shareholder proposal achieved majority

029/paid-parental-leave-how-republicans-learned-to-love-a-democratic-priority [https://perma.cc/7Y55-QBVQ] (describing how one politician had been working on the issue of parental leave for two decades).

224. For an example of a shareholder proposal that addresses paid family leave, see STARBUCKS CORP., 2018 PROXY STATEMENT PURSUANT TO SECTION 14(A) OF THE SECURITIES EXCHANGE ACT OF 1934 53 (2018), https://www.sec.gov/Archives/edgar/data/829224/000119312518021792/d440699ddef14a.htm#toc440699_65 [https://perma.cc/3E9R-AES6].

support. With a small investment of time, human investors could achieve real change, succeeding where the political process has failed.

C. *Engagements*

In addition to proxy voting and shareholder proposals, major players in corporate governance promote their own interests through private conversations with company management. Under the status quo, index fund managers (in particular the Big Three), wealthy private individuals, hedge funds, and other large asset managers regularly engage in such communications.[225] In contrast, human investors do not have the opportunity to discuss their concerns directly with management because their holdings are simply too scant to merit any attention.

This imbalance is itself a subject of concern. It stands to reason that if human investors cannot voice their concerns to management, but their more powerful counterparts can, management will have a greater understanding of powerful corporate and financial actors' interests, concerns, and preferences relative to those of human investors.

In addition, the fact that these communications happen at all is potentially problematic. Engagements occur because of the implicit threat that a major player will use their funds in a way that will cause problems for management—whether that be through opposition to one or more director candidates, via the shareholder proposal process, or by withdrawing some or all of their investment. This threat exists not because these major players control a majority of shares, as invariably they do not, but because they control enough shares to cause trouble for management. To the extent that major players can privately pressure corporations to act without majority shareholder support, these major players are in a position to extract idiosyncratic benefits—or rents—from the corporation.[226]

More troubling is the fact that funds conduct these types of communications in secret. Such communications come in the form of emails, letters, telephone calls, and sit-down meetings, and the contents of these communications are known only to those parties who are directly involved. At their own election, the Big Three publish extremely limited, post hoc summaries of engagements, but these contain few specifics, except for a handful of self-selected "case studies."[227]

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225. Freedman et al., *supra* note 134.

226. In some ways, this phenomenon is analogous to strike suits. *See Strike Suit*, MERRIAM-WEBSTER DICTIONARY (2023), https://www.merriam-webster.com/legal/strike%20suit [https://perma.cc/A378-73J6]. Just as there exists a mix of meritorious suits and nuisance suits, there is also likely to be a mix of beneficial advocacy and engagements designed to extract private gains.

227. *See, e.g.*, VANGUARD, INVESTMENT STEWARDSHIP 2021 ANNUAL REPORT 9–15 (2021), https://corporate.vanguard.com/content/dam/corp/advocate/investment-stewardship/pdf/policies-and-reports/inv_stew_2021_annual_report.pdf [http://perma.cc/7A62-HHZH].

How can we level the playing field for human investors? The first step is for the SEC to mandate that all communications between mutual funds and portfolio company management be recorded and transcribed (for oral communications) or copied and stored (for written and digital communications) and then made available to investors within a reasonable time period (perhaps ten days) after the engagement.[228]

The only defensible reason why index fund management should be able to withhold the substance of their conversations with corporate officers from the very clients on whose behalf they purportedly act is if their investors desire them to withhold this information. However, the data suggests that investors strongly support increased transparency for engagements. As Figure 9 below reveals, 78% of index fund and ETF investors favor disclosing the contents of engagements. Over half (56%) believe that engagement transcripts should be disclosed to investors, while a further 22% believe that transcripts from engagements should also be made available to the public.

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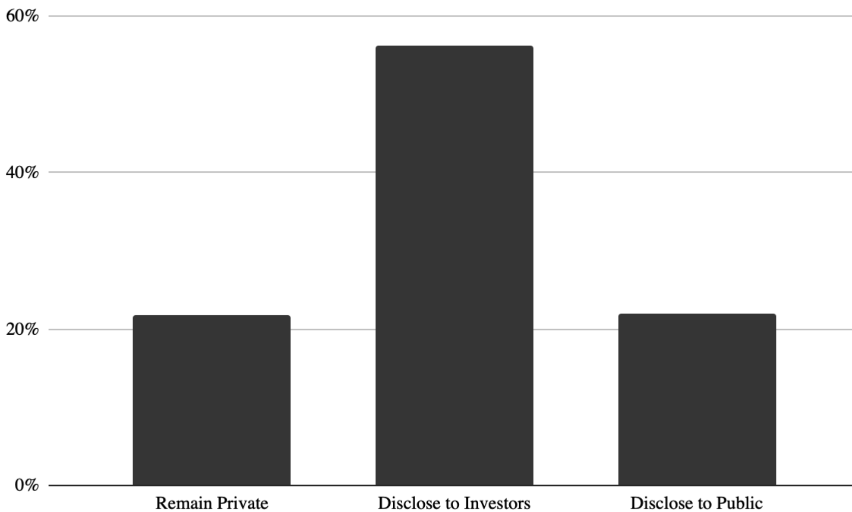
228. Professor John Coates has made a similar proposal. *See* Coates, *supra* note 157, at 23. Coates explained that:

> Another dimension of such regulation would be to enhance disclosure of how index funds engage with public companies – treating them as if they were subject to the equivalent of a 'Freedom of Information Act' request or, going further, requiring public disclosure of what index funds are saying to corporate representatives, similar to the 'Sunshine Laws' used to accomplish something similar for regulatory agencies.

Id.

Figure 9: Investors' Views on Engagement Transparency

This chart summarizes the results of a survey of 1,611 index fund and/or ETF owners who were asked their views as investors on whether communications with management should be disclosed or should remain private. The margin of error is +/- 2.491%.



Disclosure of transcripts from engagements would facilitate far greater transparency in the engagement process. This disclosure requirement would enable investors and/or outside monitors to identify instances where stewardship team representatives acted to advance personal interests or the interests of the fund provider rather than fulfilling their fiduciary duty to investors. Alternatively, the threat of exposure might deter self-dealing in the first instance. In combination, engagement disclosures and investor input disclosures would allow human investors to hold fund managers accountable in the exercise of their fiduciary duties.

D. *Stewardship Team Representation*

Human investors currently lack representation on stewardship teams at the Big Three and other mutual funds. Presently, stewardship teams at the Big Three are composed of a few dozen individuals who are hired by the fund and who have no direct connection to their investors other than their employment status.[229] Although the backgrounds of these

229. *See* BLACKROCK, BLACKROCK INVESTMENT STEWARDSHIP ENGAGEMENT PRIORITIES 8 (2022), https://www.blackrock.com/corporate/literature/publication/blk-stewardship-priorities-final.pdf [https://perma.cc/7NC5-YENM].

employees are not publicly available, this group likely does not fully represent the diverse characteristics of the investor base as a whole. These individuals have considerable power, as they conduct all stewardship activities including proxy voting and engagements for the world's largest asset managers.

Under a revised approach to corporate governance, investors would be represented on the stewardship team at the Big Three and its competitors. Investor representation would be roughly modeled after the German codetermination system, wherein employees sit alongside management on a work council.[230] In the context of the Big Three, all investors would be eligible to apply for an advisory role on the stewardship team by submitting their name for consideration. Each of the Big Three would randomly select individuals from the pool of all applicants to serve in this representative capacity for a term of a few years.[231] The fund would invite these individuals to review periodic reports and attend an annual virtual meeting, during which the stewardship team would report on its stewardship activities and investor representatives could voice any concerns directly to management. In these meetings, the stewardship team would justify stewardship activities undertaken on behalf of investors based on the investor input mechanisms outlined above. To the extent that representatives thought a particular course of action deviated from investors' best interests, they could flag that topic for review by management.

E. *Overall Impact*

Overall, this four-pronged approach would recalibrate corporate governance mechanisms to better serve the interests of human investors and not merely the wealthy, powerful, and well-connected. These proposals would reform the Big Three index funds and their competitors so that stewardship activities truly advance the "best interests" of investors. The result would be a more balanced approach to corporate governance and greater alignment between corporate America's actions and human investors' values.

CONCLUSION

Various attempts have been made to humanize corporate governance. Benefit corporations explicitly allow conscience-based activities,[232] but

230. Mitbestimmungsgesetz, May 4, 1976, BGBl. I § 7.

231. In the German system, the number of representatives is generally equal to the number of board members. *Id.* In the index fund context, the number of representatives might be equal to the number of stewardship team members.

232. Kevin V. Tu, *Socially Conscious Corporations and Shareholder Profit*, 84 GEO. WASH. L. REV. 121, 142 (2016) (explaining that benefit corporations "have a corporate purpose of creating a general public benefit").

so little economic activity is funneled through benefit corporations that they are largely a curiosity.[233] Similarly, stakeholder theorists have attempted to articulate a meaningful alternative to the shareholder wealth maximization norm,[234] but experts have criticized such theories as unworkable due to the pragmatic difficulties inherent in being accountable to everyone.[235] Finally, although the ESG movement has recently experienced tremendous growth,[236] it still suffers from the fatal limitation that, for most funds, the pursuit of ESG goals largely depends on evidence that such goals also happen to increase risk-adjusted financial returns.[237] Such evidence is increasingly mixed,[238] threatening to upend much of the progress of the ESG movement. Ultimately, efforts to humanize corporate governance have been met with only limited success.

As this Article has demonstrated, human investors have a deeply held interest in nonfinancial ends, such as environmental sustainability and societal welfare,[239] in addition to their interest in financial returns. Given their extant concentration in index funds, particularly the Big Three, human investors are uniquely poised to voice these concerns—if only their purported representatives would listen. This Article therefore sets forth a framework that would empower human investors and make mutual fund managers more accountable.

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233. Jackson C. Esker, Note, *Corporate Social Responsibility: Can a Corporation Be Responsible If Its Only Responsibility Is to the Shareholders?*, 106 IOWA L. REV. 1961, 1981 (2021) (noting that only .023% of American businesses are benefit corporations).

234. *See supra* notes 65–68 and accompanying discussion.

235. *See supra* notes 85–90 and accompanying discussion.

236. *See supra* notes 27–31 and accompanying discussion.

237. *See supra* notes 25–38 and accompanying discussion.

238. *See, e.g.*, Giovanni Bruno et al., "*Honey, I Shrunk the ESG Alpha": Risk-Adjusting ESG Portfolio Returns*, 31 J. INVESTING 45 (Apr. 2022) ("In this paper, we show that there is no solid evidence supporting recent claims that ESG strategies generate outperformance.").

239. *See supra* Section I.C.