

# MASS CORPORATE GOVERNANCE

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## ABSTRACT

*Democracy is a compliance cost. At least, that is the modern conception of performative corporate governance. Structurally contingent legal and market characteristics mean that shareholder voting is now conducted with an unusual combination of zealous devotion to the voting process and general ambivalence as to substantive outcomes.*

*This dynamic arises because financial and voting rights are routinely decoupled, resulting in a fundamental transformation of the incentives, constraints, and power dynamics through which the world's largest corporations are governed. The ironic result is that the governance actors with the greatest power often have little incentive to use it. Regulators have "solved" this problem by mandating that they do so—that is, the intermediary agents who dominate modern shareholder democracy generally must vote whether they wish to or not. As a consequence of the interplay between a regulatory obligation to vote and weak financial incentives to do so, these agents have developed a privately optimal strategy of high-volume, low-value, non-firm-specific, and compliance-oriented governance activity, which this paper terms "mass corporate governance."*

*While mass corporate governance is privately optimal from the perspective of intermediary agents, it imposes significant costs on investors and society at large. This Article makes a key contribution to the literature by developing a comprehensive strategic framework for assessing limits on intermediary agency costs. It concludes that no extant or proposed policy effectively constrains the governance discretion of intermediaries, and it argues that fighting to constrain discretion is an improper—and ultimately futile—frame of reference. Ultimately, the Article proposes policy solutions that not only benefit investors and the corporate governance system, but also help to limit the concentration of corporate governance power, benefit American labor interests, and mitigate the anticompetitive effects of common ownership.*

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## INTRODUCTION

Conceptualizations of “corporate governance” still conjure classic archetypes of shareholders buying and voting their own shares. However, this archetypal form of corporate governance is rapidly being eclipsed by a new, intermediated form.<sup>1</sup> In practice, today’s financial and voting rights are routinely decoupled,<sup>2</sup> resulting in a fundamental transformation of the

1. Jill Fisch & Jeff Schwartz, *Corporate Democracy and the Intermediary Voting Dilemma*, 102 TEX. L. REV. 1, 13 (2023) (“Today, institutional investors control the voting power with respect to approximately 71% of publicly traded equities.”).

2. Henry T.C. Hu, *Financial Innovation and Governance Mechanisms: The Evolution of Decoupling and Transparency*, 70 BUS. L. 347, 347 (2015) (“‘Decoupling’ undermines classic understandings of the allocation of voting rights among shareholders (via, e.g., ‘empty voting’) . . .”).

incentives, constraints, and power dynamics through which the world's largest corporations are governed.<sup>3</sup>

When a firm grows too large for its owners to manage, the owners hire agents to work on their behalf. This can generate tremendous gains by allowing the firm to grow and labor to specialize. However, it can also generate significant costs: These agents have their own distinct set of incentives, which differ from those of their principals and which they may pursue if not adequately constrained.<sup>4</sup> A focus on these “agency costs” has dominated corporate governance scholarship for much of the last half-century.<sup>5</sup> Now, however, a new set of intermediary agents presents a new set of agency costs.<sup>6</sup> Not only is the day-to-day operationalization of the firm delegated to agents, but the core governance powers of shareholders are delegated to agents as well.<sup>7</sup> As the amount of assets held by intermediaries continues to ascend,<sup>8</sup> addressing these increasingly important governance-related agency costs (which this Article terms “governance costs”) is a crucial task.

In endeavoring to address these governance costs, it is instructive to consider the outer bounds of potential policy responses. These responses can be characterized by two extremes: At one extreme, perhaps allowing intermediaries to exercise governance authority over their clients' equity investments is so poorly incentivized and filled with conflicts of interest that

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3. See Usha Rodrigues, *Corporate Governance in an Age of Separation of Ownership from Ownership*, 95 MINN. L. REV. 1822, 1828 (2011) (“[T]he ownership landscape of American public corporations has shifted dramatically over the past seventy-five years. No longer do we have merely a separation of ownership and control; we now also have a separation of ownership from ownership. Individual long-term capital holders no longer hold shares of corporations directly; the direct holders of shares predominantly are institutional investors.”).

4. For a robust discussion of agency costs at the firm level, see Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305 (1976).

5. See Dorothy S. Lund & Elizabeth Pollman, Essay, *The Corporate Governance Machine*, 121 COLUM. L. REV. 2563, 2574 (2021) (“[B]y the early 1980s, louder voices had started to prevail in focusing the term’s meaning on reducing agency costs to serve shareholder interests. Corporate governance underwent a ‘revolution’ toward the ‘monitoring model.’”).

6. 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 (2013) (“Equity ownership in the United States no longer reflects the dispersed share ownership of the canonical Berle-Means firm. Instead, we observe the reconcentration of ownership in the hands of institutional investment intermediaries, which gives rise to ‘the agency costs of agency capitalism.’”).

7. See Sean J. Griffith & Dorothy S. Lund, *Conflicted Mutual Fund Voting in Corporate Law*, 99 B.U. L. REV. 1151, 1157 (2019) (discussing the conflicts that arise “when mutual fund intermediaries control corporate voting rights”).

8. Lucian Bebchuk & Scott Hirst, *The Specter of the Giant Three*, 99 B.U. L. REV. 721, 725–26 (2019) (“Over the last fifty years, institutional investors have come to hold a majority of the equity of U.S. public companies. From 1950 to 2017, the institutional ownership of corporate equity increased tenfold, from 6.1% to 65%. As a result, institutional investors now control a large majority of the shares of public companies and have a dominant impact on vote outcomes at those companies.”).

we should ban it outright. Under this view, it should be *illegal* for an intermediary to choose how to vote their investors' equity assets. At the opposite extreme, perhaps intermediary voting is so important and valuable that we should legally require *every intermediary* to vote *every share* in *every corporate election*. Under the most extreme version of this logic, we should characterize choosing how to vote your investors' assets as a core part of your fiduciary duty.

These extremes are not merely hypothetical. In an interesting twist, policymakers have in fact incorporated both extremes into the law governing intermediary voting. The exercise of proxy voting power by intermediaries today is, somewhat humorously, either a core part of an intermediary's fiduciary duty or effectively prohibited, depending on with which intermediary one invests.

As disparate as these treatments are, they both represent attempts to control agency costs. In a series of actions from the mid 2000s and early 2010s, the Securities and Exchange Commission (SEC) approved rule changes to the New York Stock Exchange's (NYSE) listing requirements which effectively banned discretionary broker voting on most matters, evidently under the belief that discretionary voting imposed agency costs on investors.<sup>9</sup> However, shortly before this series of changes began, the SEC effectively *mandated* discretionary voting in the mutual fund context, because it thought, apparently, that *not* engaging in such voting imposed agency costs on investors.<sup>10</sup>

Thus, under the current status quo, if one invests in a basket of stocks through an intermediary that provides mutual funds and exchange-traded funds (ETFs) (e.g., BlackRock), it is a part of such intermediary's fiduciary duty to engage in discretionary voting on the beneficial owner's behalf, and the law effectively mandates that they do so in most circumstances.<sup>11</sup> However, if one engages in economically identical behavior—investing in the same basket of stocks, this time through a different intermediary (e.g.,

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9. See Order Approving Proposed Rule Change, Exchange Act Release No. 60215 (July 1, 2009), <https://www.sec.gov/files/rules/sro/nyse/2009/34-60215.pdf> [<https://perma.cc/9MED-PB9U>] (stressing “accountability” of corporate agents and arguing that eliminating discretionary broker voting on non-routine matters would lead to “better corporate governance”).

10. Dorothy Lund, *The Case Against Passive Shareholder Voting*, 43 J. CORP. L. 493, 526 (2018) (“On January 23, 2003, the SEC solidified this position by adopting a rule mandating that investment fund advisors disclose their votes, as well as their policies and procedures for voting, in corporate elections. In the adopting release to the rule, the SEC explained, ‘the investment adviser to a mutual fund is a fiduciary that owes the fund a duty of . . . good faith. This fiduciary duty extends to . . . the voting of proxies relating to the fund’s portfolio securities.’” (alteration in original) (quoting Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, Securities Act Release No. 8188, Exchange Act Release No. 47304, Investment Company Release No. 25922, 68 Fed. Reg. 6564, 6565 (Feb. 7, 2003) (codified at 17 C.F.R. pts. 239, 249, 270, 274 (2026)))).

11. See *infra* Part II (describing the history of the perceived mandate to vote most shares).

Robinhood)—suddenly voting is no longer mandatory; in fact, it is largely *prohibited* for the intermediary to engage in discretionary voting on the beneficial owner's behalf.<sup>12</sup>

It should be noted that, although the economic effect may be indistinguishable, there are concededly important *legal* differences between different types of financial intermediaries, such as brokers and mutual funds. However, it is not clear that the substantive differences are so significant as to justify diametrically opposite treatment. It is not self-evident, for instance, that carrying the legal status of a mutual fund rather than a broker makes one inherently better at voting on behalf of beneficial equity owners. While this might be true today, since policymakers have incentivized only certain intermediaries (particularly mutual funds) to build out a “stewardship” infrastructure over the last two decades,<sup>13</sup> this is not an intrinsic characteristic of such investment funds, but a legally and historically contingent one.

The contingent manner in which voting by intermediaries is either compelled or banned is perhaps nowhere better displayed than in the context of index funds. The entire investment philosophy of index funds—their basic epistemic premise and the intuition underlying their very existence—is that the governance attributes and other characteristics which make certain companies more profitable are unknown (and effectively unknowable).<sup>14</sup> The core investment thesis of buying an index fund is that we cannot discover those characteristics, so instead, we should buy the entire equity index.<sup>15</sup> Interestingly, we then task index funds with doing what their investment philosophy says is unknowable—that is, picking out which governance characteristics will make companies more or less profitable, and then enforcing those characteristics through voting and engagements.

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12. Jill E. Fisch, *Standing Voting Instructions: Empowering the Excluded Retail Investor*, 102 MINN. L. REV. 11, 28 (2017) (“Today, brokers are prohibited from exercising discretionary voting authority with respect to most issues on which shareholders are asked to vote.”).

13. Amanda M. Rose, *A Hard Look at Portfolio-Focused Stewardship*, 2024 COLUM. BUS. L. REV. 313, 343 (“Asset managers initially attempted to satisfy these obligations by soliciting voting advice from proxy advisory firms, and when proxy advisory firms began drawing regulatory scrutiny they augmented their in-house stewardship teams.”).

14. Richard A. Booth, *The Duty to Diversify and the Logic of Indexing*, 75 U.C. L.J. 555, 577–78 (2024) (“It is clear that costly research aimed at predicting the performance of individual companies is a waste of money for ordinary investors. But how does one select portfolio stocks in some rational way that has nothing to do with evaluating their individual prospects? It may be just as costly to determine which stocks make up an optimum portfolio as it is to pick winner—if not more so. One possibility is to choose stocks at random. Indeed, that idea has been taken quite seriously. A better answer is to invest in the stocks comprised by a well-constructed index.”).

15. *Id.*

Despite this rather poor epistemological fit, index fund managers are the most powerful corporate governance actors in modern equity markets,<sup>16</sup> and, as the largest shareholders in a substantial majority of large public companies,<sup>17</sup> they effectively dictate to every public company what constitutes “good corporate governance.”<sup>18</sup> The mild absurdity of the status quo—being governed by intermediary agents whose very existence is premised on the lack of identifiable positive governance characteristics—provides further evidence of the historically and legally contingent nature of the power dynamics in modern corporate governance. Indeed, the current legal allocation of governance power appears largely orthogonal to governance expertise. As a result, tremendous shifts in the allocation of raw voting power between various types of intermediaries are thus downstream of the legal distinctions between economically identical investment behavior.

This semi-involuntary investiture of voting power in the hands of certain intermediaries has created a new problem—namely, how best to comply with these new voting responsibilities. Although there are exceptions, it appears that intermediaries often approach this issue in much the same way they approach any other compliance obligation. Historically, voting by intermediaries was rare because, for most firms in their portfolio, they had weak or negative financial incentives to engage in informed voting.<sup>19</sup> Prior to voting becoming effectively mandated in many contexts, intermediaries generally voted only when they thought they could vote well, i.e., when voting mattered from the perspective of both economic significance and potential impact on voting outcomes. The SEC evidently considered this pattern of abstention inappropriate, as part of the Commission’s justification for the effective proxy voting mandate was the prior low rates of voting by asset managers.<sup>20</sup> Interestingly, post-mandate intermediaries have much

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16. Lucian Bebchuk & Scott Hirst, *Big Three Power, and Why It Matters*, 102 B.U. L. REV. 1547, 1599 (2022) (“The Big Three collectively hold more than 20% of the shares of S&P 500 companies and almost 25% of the votes cast at the annual meetings of those companies. These substantial stakes give them correspondingly significant voting power, and with it, influence over the managers of the corporations in which they invest. Their stakes and influence are likely to continue to grow.”).

17. *Id.* at 1572 n.132 (“As of December 2018, one of BlackRock, Vanguard or State Street was the largest shareholder in 438 of the S&P 500 companies, roughly 88%, and collectively the three firms owned 18.7% of all shares in the S&P 500.” (quoting Melissa Sawyer, *Annual Review and Analysis of 2019 U.S. Shareholder Activism*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Nov. 20, 2019), <https://corp.gov.law.harvard.edu/2019/11/20/annual-review-and-analysis-of-2019-u-s-shareholder-activism/> [<https://perma.cc/5MK2-EA3L>])).

18. *See infra* Section II.A (outlining the consensus corporate governance “best practices”).

19. *See infra* Part I (discussing voting rates by mutual funds prior to SEC intervention).

20. Jeff Schwartz, *Stewardship Theater*, 100 WASH. U. L. REV. 393, 421 (2022) (“In advancing voting regulations two years later, the SEC cited the industry’s history of corporate-governance complacency as a rationale for intervention.”).

stronger incentives to vote than they do to vote *well*. As a result, intermediaries frequently comply with this effective mandate by engaging in what this paper terms “mass corporate governance”—high-volume, low-value, non-firm-specific, and compliance-oriented governance activity.

By way of background, the easiest “stewardship” strategy is to apply the same rules or principles to all companies without distinction. This tactic is low-cost and efficient, and numerous asset managers take this approach to at least some governance issues. However, few commentators believe this to be optimal.<sup>21</sup> Instead, most advocate for taking at least some account of the many diverse characteristics that firms possess.<sup>22</sup> In theory, all governance decisions should be firm-specific—no two companies are exactly alike, and an ideal governance strategy would take into account the myriad ways in which firms differ.<sup>23</sup> However, while some investors with highly concentrated portfolios may make governance decisions in this manner, today’s largest asset managers decidedly do not,<sup>24</sup> and, given their business model, industry dynamics, and financial incentives, likely never will do so of their own accord.<sup>25</sup>

Thus, in a first-best world, all intermediaries who vote would do so in an informed and firm-specific manner—that is, they would engage in traditional, firm-specific corporate governance.<sup>26</sup> In a second-best world, where mass corporate governance is the most rational response to an effective voting mandate, while firms might vote in a less-informed, less

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21. See, e.g., Lund, *supra* note 10, at 493 (noting that “a low-cost, one-size-fits-all approach to governance . . . is unlikely to be in the company’s best interest”).

22. See, e.g., Sean J. Griffith, *Opt-In Stewardship: Toward an Optimal Delegation of Mutual Fund Voting Authority*, 98 TEX. L. REV. 983, 1032–33 (2020) (“There are no ‘one-size-fits-all’ governance solutions. Instead, optimal governance arrangements are endogenous to firms.”); Lund & Pollman, *supra* note 5, at 2621 (“[T]here is evidence that one-size governance solutions can destroy value”).

23. See Jeffrey N. Gordon, *Systematic Stewardship*, 47 J. CORP. L. 627, 630 (2022) (“For example, such investors generally have developed a normative model of ‘good’ corporate governance expressed in ‘guidelines’ that generates voting positions across the entire portfolio . . . These views are then uniformly applied across the portfolio, even though firm-specific analysis would surely produce governance heterogeneity.”).

24. See Lund & Pollman, *supra* note 5, at 2620–21 (discussing the rise of “one-size-fits-all governance” and indicating that major institutional investors rely upon such a generic approach to governance).

25. See Dorothy S. Lund, *In Search of Good Corporate Governance*, 131 YALE L.J.F. 854, 863–64 (2022) (“Index funds generally lack firm-specific information about the companies in their large portfolios, which means customized interventions would require additional research. In addition to increasing the fund’s costs, this research is unlikely to benefit the fund that undertakes it—mutual funds compete on the basis of relative performance, and so any investment in stewardship will increase costs while benefiting rival funds. Therefore, even cost-justified investments in monitoring and stewardship—investments that mutual fund beneficiaries would prefer the fund to undertake—will be forsaken because these expenditures will not help the fund’s portfolio manager outcompete rivals.”).

26. The difficulties of this are manifold, and, as discussed below, existing legal mandates and market forces appear unable to produce the desired outcome.

firm-specific fashion, legal rules and market incentives would at least ensure that their general, one-size-fits-all rules would be the optimal ones. That is, if intermediaries are going to engage in mass corporate governance, at least they can enforce the rules that, on average, are most aligned with shareholder interests (typically understood through a wealth maximization lens).

This Article argues that current legal rules and market incentives are largely inadequate to constrain the behavior of intermediaries even to the more limited, second-best standard, let alone ascend beyond the generalities of mass corporate governance. It concludes that, in a world of subjective shareholder value, governance discretion by intermediaries is not just unconstrained, but unconstrainable. Because there is no effective way to constrain the delegation of governance discretion inherent in the decoupling of governance power from economic ownership, investors should be allowed to choose *to whom* discretion is delegated. The result of this policy intervention would be a partial recoupling of governance authority and economic ownership which embraces the realities of shareholder value subjectivity.

The Article proceeds as follows: Part I further explores mass corporate governance. Part II examines whether legal constraints on the ends of governance discretion, such as a wealth maximand, are sufficient to cabin the agency costs of intermediaries. It finds ample subjectivity in the empirical literature on even the core set of consensus corporate governance “best practices,” undermining the efficacy of ends-based constraints. Part III explores whether market pressures on the ends of governance are sufficient to align intermediary incentives with those of their investors, and it finds them deficient. Part IV considers the efficacy of market pressures (e.g., investors “voting with their feet”) as a constraint on the means of intermediated governance, and it finds that market pressures are largely ineffective due to limitations on investors’ ability to select and/or switch between funds. Part V examines extant and proposed methods of curbing governance discretion by legally mandating that intermediaries employ specified means (e.g., polling or otherwise soliciting the input of their investors) in the exercise of governance powers, and it finds that such means-based legal constraints would either be too onerous to be practicable or too weak to be sufficiently constraining. In response to the inherent deficiencies of the various methods of constraining intermediary discretion, Part VI proposes that investors should be entitled to assign their voting rights to a delegate of their choosing. The Conclusion summarizes this Article’s findings.

## I. THE MASS CORPORATE GOVERNANCE CONUNDRUM

If voting a hyper-diversified portfolio is costly, difficult, poorly incentivized, conflicted, and relatively low-value,<sup>27</sup> why would asset managers choose to take on the herculean task of voting potentially hundreds of thousands of ballot items? The answer is that it is not, precisely, a choice. Asset managers do not freely “choose” to vote proxies only when they believe it is a cost-justified, value-adding proposition, but they instead vote nearly every share in nearly every election due to an ambiguous regulatory mandate.<sup>28</sup>

Section I.A that follows examines the SEC’s ambiguous statements and guidance with respect to compelled voting by intermediaries. Section I.B examines compelled voting by the Department of Labor in the context of Employee Retirement Income Security Act of 1974 (ERISA) plans, as well as the potential impact outside of such plans via “backdoor ERISA” liability. Section I.C explores the impact of compelled voting in the context of weak incentives and significant cost pressures, generating what this Article terms “mass corporate governance.”

### A. *Compelled Voting & the SEC—A Brief History*

The modern history of regulatory voting mandates for mutual funds, real or perceived, began in earnest in 2003 when the SEC stated the following:

Because a mutual fund is the beneficial owner of its portfolio securities, the fund’s board of directors . . . has the right **and the obligation** to vote proxies relating to the fund’s portfolio securities . . . The investment adviser to a mutual fund is a fiduciary that owes the fund a duty of ‘utmost good faith, and full and fair disclosure.’ This fiduciary duty extends to all functions undertaken on the fund’s behalf, including the voting of proxies relating to the fund’s portfolio securities.<sup>29</sup>

Although somewhat ambiguous, the text appears to make voting proxies a part of an adviser’s fiduciary duty, and it was “widely interpreted as mandating that mutual funds vote all of the shares of their portfolio

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27. Fisch & Schwartz, *supra* note 1, at 21 (“Stewardship, it turns out, is relatively hard, potentially costly, and generates little—if any—profit for fund managers.”).

28. See *infra* Section I.A (discussing the perception of mandated voting by mutual funds).

29. Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, Securities Act Release No. 8188, Exchange Act Release No. 47304, Investment Company Release No. 25922, 68 Fed. Reg. 6564, 6565 (Feb. 7, 2003) (codified at 17 C.F.R. pts. 239, 249, 270, 274 (2026)) (emphasis added).

companies.”<sup>30</sup> That same year, the SEC clarified that failing to vote all shares in all elections would not “necessarily” violate an adviser’s fiduciary duties, adding that “there may even be times” when not voting was appropriate.<sup>31</sup> The only example provided as an acceptable time to refrain from voting is “when the adviser determines that the cost of voting the proxy exceeds the expected benefit.”<sup>32</sup> Taken as a whole, this guidance appears to suggest that, while the obligation to vote is not absolute, as a practical matter, asset managers possess a fiduciary obligation to either vote or, alternatively, to be prepared to justify why the costs of voting exceeded the benefits. Thus, the default obligation is voting, although there “may even be times” where, in certain circumstances, after the asset manager makes an appropriate determination, they can abstain.<sup>33</sup>

This ambiguous but “widely interpreted” mandate guided asset managers for nearly two decades. During this time period, index funds experienced extraordinary growth,<sup>34</sup> they established and/or significantly expanded their stewardship teams,<sup>35</sup> and they solidified the basic proxy voting practices they retain today.<sup>36</sup> In 2019, the SEC seemingly moderated its prior course.<sup>37</sup> It issued guidance to the effect that proxy voting could be proscribed by agreement in certain circumstances.<sup>38</sup> It provided “several non-exhaustive

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30. Lund, *supra* note 10, at 526 (“This rule was widely interpreted as mandating that mutual funds vote all of the shares of their portfolio companies. As a result, large asset managers, including the Big Three, generally do so.”); *see also* Fisch & Schwartz, *supra* note 1, at 14 (“Before the SEC’s involvement, institutional investors were notoriously passive. Now, however, they vote over 90% of their shares whereas individuals vote less than 30%.”).

31. Proxy Voting by Investment Advisers, 68 Fed. Reg. 6585, 6587 (Feb. 7, 2003) (codified at 17 C.F.R. pt. 275 (2026)) (“We do not suggest that an adviser that fails to vote every proxy would necessarily violate its fiduciary obligations. There may even be times when refraining from voting a proxy is in the client’s best interest, such as when the adviser determines that the cost of voting the proxy exceeds the expected benefit to the client.”).

32. *See id.*

33. *Id.*

34. *See* Landon Thomas Jr., *Vanguard Is Growing Faster Than Everybody Else Combined*, N.Y. TIMES (Apr. 14, 2017), <https://www.nytimes.com/2017/04/14/business/mutfund/vanguard-mutual-index-funds-growth.html> [<https://perma.cc/9M44GYMS>] (discussing the explosive growth of indexed investing).

35. Nathan Atkinson, *If Not the Index Funds, Then Who?*, 17 BERKELEY BUS. L.J. 44, 73 (2020) (“The stewardship departments at the large asset managers have grown in recent years and the major asset managers have announced substantial plans for future growth.”).

36. For a discussion of the proxy voting practices at index funds and how they have changed over time, *see* Caleb N. Griffin, *Open Proxy*, 99 TUL. L. REV. 247 (2024).

37. *See* Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, Investment Company Act Release No. 33605, 84 Fed. Reg. 47420 (Sept. 10, 2019) (codified at 17 C.F.R. pts. 271, 276 (2026)).

38. *Id.* at 47423 (“A client and its investment adviser may agree that the investment adviser would not exercise voting authority in circumstances under which voting would impose costs on the client . . . A client and its investment adviser may agree that the investment adviser will focus voting resources only on particular types of proposals . . . A client and its investment adviser may agree that

examples” to that effect, including to facilitate securities lending, to narrow the set of proposals for consideration, and in situations where the costs outweigh the benefits.<sup>39</sup> While these exceptions do provide some additional flexibility, they do not appear to have significantly altered proxy voting behavior.<sup>40</sup> The result, whether through perceived regulatory mandate or simple inertia, is that outside of certain limited exceptions (e.g., share lending, foreign equities), asset managers continue to behave as if voting were effectively mandatory.<sup>41</sup>

However, even if asset managers perceive voting as effectively mandatory, this does not imply that they perceive it as intrinsically valuable. Indeed, it may imply the opposite—if it was particularly high-value, there would be no need to force (or, more diplomatically, nudge) them to do so.<sup>42</sup> Thus, a voting mandate alters an intermediary’s behavior only when an investment in governance has a negative expected return for the intermediary.<sup>43</sup> The result of this dynamic is that such voting is viewed as a compliance cost,<sup>44</sup> to be disposed of as quickly and cheaply as possible through low-value, high-volume, non-firm-specific voting strategies, which this Article collectively refers to as “mass corporate governance.”

## B. ERISA Matters

### 1. Mass Corporate Governance Mandates in ERISA

Although the SEC is generally responsible for regulating the proxy voting of equity assets, ERISA also grants the Department of Labor rulemaking authority with respect to proxy voting of assets held in certain employer-sponsored retirement accounts. These accounts, such as 401(k)

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the investment adviser would not exercise voting authority on certain types of matters where the cost of voting would be high, or the benefit to the client would be low.”).

39. *Id.* at 47422–23.

40. *See, e.g.,* Bebhuk & Hirst, *supra* note 16, at 1599–600 (discussing the Big Three mutual fund providers’ voting behavior in 2021).

41. *See* Dorothy S. Lund, *Asset Managers as Regulators*, 171 U. PA. L. REV. 77, 108 (2023) (discussing continued voting engagement by asset managers even following the 2019 rulemaking).

42. Schwartz, *supra* note 20, at 424 (“If asset managers found stewardship profitable, they would have participated in it since the industry’s inception. Instead, they avoided it until regulators prodded them to take voting more seriously.”).

43. Whether investments in governance will generate positive expected value for intermediaries is distinct from the question of whether it is valuable to their principals, who by definition do not suffer from the conflicts and incentive misalignment of intermediary agents.

44. Schwartz, *supra* note 20, at 440 (“Interest that escalates at the same rate as regulatory pressure suggests that any enthusiasm is feigned. Rather than generate profits, the increasing engagement seems designed to demonstrate legal compliance and blunt the case for future reforms.”).

and pension plans, collectively hold trillions of dollars in assets.<sup>45</sup> The Department of Labor has issued a number of important rulemakings with respect to governance obligations under ERISA, laying out distinct fiduciary responsibilities with respect to proxy voting of plan assets.<sup>46</sup> Broadly, the Department's position with respect to compelled proxy voting historically followed a more-or-less parallel path to guidance from the SEC. In 2001, the Department stated the following in an Interpretive Bulletin:

The fiduciary act of managing plan assets that are shares of corporate stock includes the voting of proxies appurtenant to those shares of stock. . . .

. . . The fiduciary obligations of prudence and loyalty to plan participants and beneficiaries require the responsible fiduciary to vote proxies on issues that may affect the value of the plan's investment. Although the same principles apply for proxies appurtenant to shares of foreign corporations, the Department recognizes that in voting such proxies, plans may, in some cases, incur additional costs. Thus, a fiduciary should consider whether the plan's vote, either by itself or together with the votes of other shareholders, is expected to have an effect on the value of the plan's investment that will outweigh the cost of voting.<sup>47</sup>

This language casts proxy voting as a "fiduciary act" stemming from the obligations of prudence and loyalty.<sup>48</sup> The apparent import is rather broad, in that fiduciaries are "require[d]" to vote on all matters that "may" influence the investment's value.<sup>49</sup> While the common exception for voting shares of foreign equities is present, even this exception is couched in the context of a required cost-benefit analysis.<sup>50</sup> Although there are some distinctions, this guidance is largely similar in substance to the SEC's 2003 guidance discussed above.

In 2020, shortly after the SEC's changes discussed in the preceding Section, the Department of Labor under President Trump enacted its own changes. These changes largely reversed the prior policy of ambiguously mandated proxy voting, instead stating that fulfilling ERISA's fiduciary

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45. See generally Press Release, Inv. Co. Inst., Quarterly Retirement Market Data, Fourth Quarter 2025 (Mar. 26, 2026), [<https://perma.cc/ZC2Y-K3XY>] (only available by archive link).

46. See generally Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. 55219-01 (to be codified at 29 C.F.R. pts. 2509, 2550 (2026)).

47. Interpretive Bulletin Relating to Written Statements of Investment Policy, Including Proxy Voting Policy or Guidelines, 29 C.F.R. § 2509.94-2 (2026).

48. *Id.*

49. *Id.*

50. *Id.*

duties “does *not* require the voting of every proxy or the exercise of every shareholder right.”<sup>51</sup> Additionally, it created two safe harbors where refraining from voting would still fulfill the requisite fiduciary obligations.<sup>52</sup> The first was an issue-based exclusion, which allowed a fiduciary to “limit voting resources to particular types of proposals that . . . are substantially related to the issuer’s business activities or are expected to have a material effect on the value of the investment.”<sup>53</sup> The second was based on portfolio immateriality, which allowed a fiduciary to refrain from voting in situations where, due to the plan’s limited holdings of a given firm, voting was “not expected to have a material effect on the investment performance of the plan’s portfolio,” even if the vote might be material to the value of the firm itself.<sup>54</sup> These safe harbors marked an especially substantial departure from prior practice, particularly since fiduciaries could act unilaterally if they “prudently determined” the requirements were satisfied.<sup>55</sup>

However, the changes did not last long. In 2022, the Department of Labor reversed course yet again. In a new rulemaking, the Department eliminated both the issue-based and portfolio immateriality safe harbors, stating that they “encouraged abstention as the normal course and the Department does not support that position.”<sup>56</sup> The new rulemaking also significantly walked back several of the Department’s other recent

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51. 29 C.F.R. § 2550.404a-1 (2026) (emphasis added); *see also* Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. 55219, 55223 (Sept. 4, 2020) (codified at 29 C.F.R. pts. 2509, 2550 (2026)) (“The Department’s longstanding position—that ‘the decision as to how proxies should be voted with regard to the issues that might affect the economic value of the underlying securities is a fiduciary act of plan asset management’—does not mean that ERISA requires fiduciaries to always vote such proxies. . . . In the Department’s view there is no presumption that abstaining from voting proxies appurtenant to shares of stock is a per se fiduciary breach.”).

52. 29 C.F.R. § 2550.404a-1 (“Paragraphs (e)(3)(i)(A) and (B) of this section set forth optional means for satisfying the fiduciary responsibilities under sections 404(a)(1)(A) and 404(a)(1)(B) of ERISA with respect to decisions whether to vote, provided such policies are developed in accordance with a fiduciary’s obligations under ERISA as set forth in the applicable provisions of paragraphs (e)(2)(i) and (ii) of this section. Paragraphs (e)(3)(i)(A) and (B) of this section do not establish minimum requirements or the exclusive means for satisfying these responsibilities.”).

53. *Id.* (“A plan may adopt either or both of the following policies: (A) A policy to limit voting resources to particular types of proposals that the fiduciary has prudently determined are substantially related to the issuer’s business activities or are expected to have a material effect on the value of the investment. . . .”).

54. *Id.* (“A plan may adopt either or both of the following policies: . . . (B) A policy of refraining from voting on proposals or particular types of proposals when the plan’s holding in a single issuer relative to the plan’s total investment assets is below a quantitative threshold that the fiduciary prudently determines, considering its percentage ownership of the issuer and other relevant factors, is sufficiently small that the matter being voted upon is not expected to have a material effect on the investment performance of the plan’s portfolio (or investment performance of assets under management in the case of an investment manager).”).

55. *Id.*

56. Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights, 87 Fed. Reg. 73822, 73828 (Dec. 1, 2022) (codified at 29 C.F.R. pt. 2550 (2026)).

changes.<sup>57</sup> For instance, the new rule deleted the language from 2020 stating that fulfilling ERISA's fiduciary duties "does not require the voting of every proxy or the exercise of every shareholder right."<sup>58</sup> This deletion suggests that perhaps voting every proxy (or nearly every proxy) *is* required, at least absent unique circumstances. The Department further opined that "[a]bstaining from a vote is not a neutral act," and, as a result, "proxies should be voted . . . unless a responsible plan fiduciary determines voting proxies may not be in the plan's best interest (e.g., in cases when voting proxies may involve exceptional costs or unusual requirements, such as in the case of voting proxies on shares of certain foreign corporations)."<sup>59</sup> Thus, at present, while proxy voting is not technically mandated under ERISA, there is a clear policy against abstention, absent "exceptional costs."<sup>60</sup> Moreover, by eliminating the two safe harbor provisions, the Department essentially forces the determination of abstentions on a vote-by-vote basis (rather than abstaining from a class of votes on immaterial issues or all votes at firms immaterial to portfolio value), significantly increasing the cost of abstention relative to the prior rule.

Interestingly, the Department seems highly cognizant of the costs it is imposing on plan fiduciaries, and it takes pains to offer guidance on how to conduct low-cost governance activities.<sup>61</sup> While the rulemaking implicitly acknowledges the cost savings of abstentions, which would have been allowed under the prior rule, it maintains that "[t]he solution to proxy-voting costs is not abstention," but instead, its preferred solution is for fiduciaries "to be prudent in incurring expenses to make proxy decisions."<sup>62</sup> Fiduciaries are admonished, "wherever possible, to rely on efficient structures (e.g., proxy voting guidelines, proxy advisors/managers that act on behalf of large aggregates of investors, etc.)."<sup>63</sup> Thus, the Department expressly

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57. *Id.*

58. *Id.* ("Like the NPRM, the final rule amends the current regulation to eliminate the statement in paragraph (c)(2)(ii) of the current regulation that 'the fiduciary duty to manage shareholder rights appurtenant to shares of stock does not require the voting of every proxy or the exercise of every shareholder right.' The final rule eliminates this provision because it may be misread as suggesting that plan fiduciaries should be indifferent to the exercise of their rights as shareholders, even if the cost is minimal.")

59. *Id.* at 73844, 73845 ("The Department's longstanding view of ERISA is that proxies should be voted as part of the process of managing the plan's investment in company stock unless a responsible plan fiduciary determines voting proxies may not be in the plan's best interest (e.g., in cases when voting proxies may involve out of the ordinary costs or unusual requirements, such as in the case of voting proxies on shares of certain foreign corporations.)")

60. *Id.*

61. *Id.*

62. *Id.* at 73845.

63. *Id.*

sanctions—perhaps even encourages—engaging in mass corporate governance as a cost saving measure.

The curious result of the Department’s apparent inclination toward mass corporate governance is that fiduciaries must be more informed about a given firm to *not* engage in its governance than to actively engage in governing the firm. Now that the safe harbors have been eliminated, abstaining requires individualized, vote-by-vote determinations that each potential abstention passes a mandatory cost-benefit analysis test, while *actually voting* requires no cost-benefit analysis (or even any firm-specific analysis whatsoever) and can be conducted according to a set of generic guidelines in a low-effort, high-volume fashion. Fiduciaries thus face powerful economic incentives to both mitigate risk and minimize cost by engaging in mass corporate governance.

## 2. Backdoor ERISA

In theory, ERISA’s directives are irrelevant to the governance of assets outside of ERISA plans.<sup>64</sup> Even some assets held *within* a covered plan—in particular, registered investment companies (a category which includes most mutual funds and ETFs)<sup>65</sup>—can, generally speaking, engage in proxy voting without regard to the Department of Labor’s rules.<sup>66</sup>

However, a handful of recent lawsuits have raised a new specter of ERISA liability. These lawsuits raise the risk of liability for plan fiduciaries and sponsors that fail to adequately monitor and intervene in proxy voting activity that violates their fiduciary duties under ERISA. The most important of these cases is *Spence v. American Airlines, Inc.*<sup>67</sup> The plaintiff in this case alleged that American Airlines and its Employee Benefits Committee (collectively, American Airlines) failed to adequately monitor and intervene in improper proxy voting by BlackRock, who was responsible for voting certain plan assets.<sup>68</sup> The plaintiff claimed that BlackRock,

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64. Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. 55219, 55230 (Sept. 4, 2020) (codified at 29 C.F.R. pts. 2509, 2550 (2026)) (“The proposal would not affect plans with respect to stock held through registered investment companies, because the proposal does not apply to such funds’ internal management of such underlying investments.”).

65. The category of “registered investment companies” generally includes mutual funds and ETFs. See INV. CO. INST., HOW US-REGISTERED INVESTMENT COMPANIES OPERATE AND THE CORE PRINCIPLES UNDERLYING THEIR REGULATION (2022), <https://www.ici.org/system/files/2023-06/us-reg-funds-principles.pdf> [<https://perma.cc/GVN8-URYL>].

66. Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. at 55230 (“The proposal would not affect plans with respect to stock held through registered investment companies, because the proposal does not apply to such funds’ internal management of such underlying investments.”).

67. *Spence v. Am. Airlines, Inc.*, 775 F. Supp. 3d 963 (N.D. Tex. 2025).

68. *Id.*

through its proxy votes in support of environmental, social, and governance (ESG) initiatives, improperly elevated nonpecuniary factors above the financial interests of the plan's beneficiaries, and that American Airlines violated its fiduciary duties by failing to monitor and intervene in such voting.<sup>69</sup> The court ultimately held that American Airlines did breach its duty of loyalty to plan participants.<sup>70</sup> In particular, the court held that American Airlines failed to “monitor, evaluate, and address the potential impact of BlackRock’s non-pecuniary ESG investing,” suggesting that the duty of loyalty encompasses a broader obligation to oversee the stewardship activities of outside investment managers.<sup>71</sup>

It is unclear how the still-nascent duty to monitor and intervene in proxy voting under ERISA will impact asset managers. However, it is likely that many asset managers who formerly might have ignored ERISA in the context of voting their client’s proxies will now face significant pressure to vote in a manner consistent with the client’s fiduciary responsibilities under ERISA, lest the client face potential legal liability. What remains uncertain is the extent to which ERISA’s duties are imported into the proxy voting arena at asset managers like BlackRock. Do plan fiduciaries need to monitor asset managers’ voting behavior to assure compliance with only a portion of ERISA’s fiduciary provisions related to proxy voting—for instance, only those that forbid elevating nonpecuniary benefits ahead of financial interests? Or, instead, must plan fiduciaries ensure that asset managers engaged in voting plan assets comply with ERISA’s proxy voting requirements in all respects? If the latter is true, it seems to considerably hollow out ERISA’s important exemption for registered investment companies.

Going forward, the specter of backdoor ERISA liability is likely to shape the behavior of mass corporate governors—motivating them to act as if ERISA applied to proxy voting by registered investment companies, at least with respect to assets held within ERISA plans. If they risk generating legal liability for their clients through their default proxy voting policies, they will face strong incentives either to change such policies or, alternatively, to utilize more tailored voting policies, likely in a pro rata fashion, on behalf of ERISA assets. Thus, the Department of Labor’s relatively strong voting mandate and sanction of mass corporate governance may influence the stewardship efforts of intermediaries more broadly.

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69. *Id.*

70. *Id.* at 1011 (“The facts here compellingly established fiduciary misconduct in the form of conflicts of interest and the failure to loyally act solely in the Plan’s best financial interests.”).

71. *Id.* at 1003.

### C. Conundrum Conclusions

Mass corporate governance is a multicausal phenomenon, ultimately stemming from the decoupling of economic ownership and governance rights. However, it is unlikely that mass corporate governance would exist without mandated voting, or the perception thereof. The preceding Sections have demonstrated that both the Department of Labor and the SEC effectively mandate voting to a significant degree. Because asset managers possess incentives to engage in high-value voting even in the absence of a mandate, the only voting engendered by a mandate is of a relatively low value.<sup>72</sup> Rational asset managers will dispose of these low-value proxy voting responsibilities at the lowest feasible cost, leading them to utilize the high-volume, non-firm-specific voting strategies that have created our modern mass corporate governance system. Thus, proxy voting by intermediaries can be separated into two distinct theoretical categories: (1) high-value votes, where intermediaries have strong financial incentives to vote, and which therefore receive a thorough review by asset managers and/or proxy advisors with careful attention to detailed firm-specific information; and (2) low-value votes, where intermediaries have no financial incentive to vote, and they therefore engage in mass corporate governance in an attempt to fulfill their voting obligations at the lowest cost attainable.

Unfortunately, from the perspective of the intermediary, the vast majority of proxy voting falls into the “low-value” category. Both history and theory suggest that intermediaries possess extremely weak financial incentives with respect to the overwhelming majority of all corporate ballot items. In the era prior to the effective voting mandates of the modern era, asset managers apparently saw little value in proxy voting.<sup>73</sup> Indeed, when the SEC issued the rulemaking in 2003 that effectively mandated proxy voting, it “cited the industry’s history of corporate-governance complacency as a rationale for intervention.”<sup>74</sup> The fact that asset managers only began taking proxy voting seriously when they were not-so-gently

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72. However, as discussed below, the weak financial incentives of many intermediaries may not adequately incentivize voting for even some relatively high-value ballot items.

73. See Schwartz, *supra* note 20, at 421 (“For 80 years, neither asset managers nor regulators paid much attention to voting.”).

74. *Id.* (“The asset-management industry has a long history of sleepy stewardship. For the first 80 years of its existence, how asset managers voted was not publicly disclosed, so it is difficult to definitively know the extent to which they participated in corporate governance. But the consensus is that they did not take it seriously during this period. Stewardship was apparently such an afterthought that Vanguard did not establish a team devoted to it until 2001.”).

nudged to do so suggests that they do not view voting as cost-justified in most instances.<sup>75</sup>

More abstractly, investments in governance will only benefit an intermediary (and its shareholders) if they are outcome-determinative—otherwise, the intermediary merely expends resources for no change in governance. It is relatively rare (extremely so outside of the Big Three asset managers)<sup>76</sup> for an intermediary to possess outcome-determinative governance power. Thus, most intermediaries would rationally prefer to free-ride on the governance investments of other market actors. But even in the limited circumstances where a particular manager’s vote may be outcome-determinative, to be rational, the investment in informed voting must still be cost-justified *on an asset-weighted basis*. In particular, for the ubiquitous market-weighted fund strategy, where the top equity holdings are several orders of magnitude larger than the bottom, there may be only a minority of companies where the asset manager’s holdings are significant enough to plausibly incentivize investment in governance. Just the top ten stocks in the S&P 500 make up roughly a third of its value, making them plausible candidates for high-value voting.<sup>77</sup> Outside of the top stocks, however, the financial incentives for asset managers to engage in informed voting deteriorate quickly. Part III, *infra*, presents detailed calculations supporting this argument empirically. Ultimately, the financial incentives for investing in governance are generally weak, even for unusually significant ballot items at very large intermediaries.

Thus, a common consequence of delegating governance power to intermediary agents is a lack of intrinsic motivation to pursue optimal governance. The result is a significant disconnect between the incentives of intermediaries and those of the investor-principals they are obligated to represent. Stated more generally, the basic problem is that agents, if not constrained in some manner, will generate agency costs—in this case, intermediaries with weak incentives to invest in governance will, absent some other constraint, generate governance costs. Thus, the question arises,

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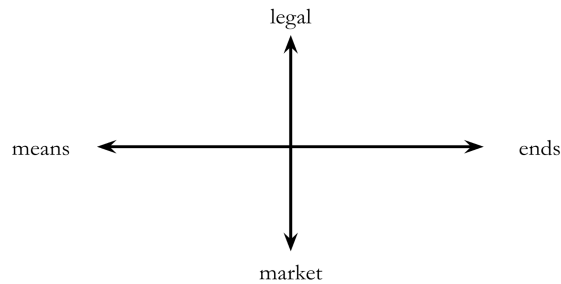
75. *Id.* at 424 (“If asset managers found stewardship profitable, they would have participated in it since the industry’s inception. Instead, they avoided it until regulators prodded them to take voting more seriously.”).

76. See Caleb N. Griffin, *Margins: Estimating the Influence of the Big Three on Shareholder Proposals*, 73 SMU L. REV. 409, 438 (2020) (discussing the situations in which Big Three voting on shareholder proposals has been outcome determinative).

77. *Is the S&P 500 Too Concentrated?*, GOLDMAN SACHS (Mar. 21, 2024), <https://www.goldmansachs.com/insights/articles/is-the-sp-too-concentrated> [<https://perma.cc/2WSK-HFRJ>] (“The 10 largest US stocks now account for 33% of the S&P 500 index’s market value, well above the 27% share reached at the peak of the tech bubble in 2000, Ben Snider, senior strategist on the US Portfolio Strategy macro team in Goldman Sachs Research, writes in the team’s report.”).

by what methods might we best constrain the governance costs of intermediaries?

FIGURE I. THEORETICAL BEHAVIORAL CONSTRAINTS ON INTERMEDIARIES

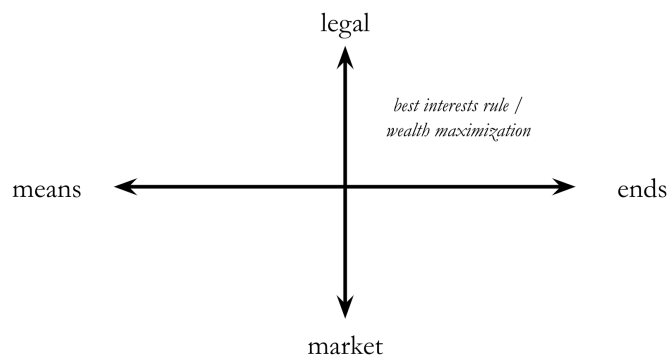


This Article proceeds by examining various extant or proposed methods of constraining governance costs generated by intermediaries, particularly large “mass corporate governors” such as the Big Four mutual fund companies (BlackRock, Vanguard, State Street, and Fidelity) and the dominant proxy advisors (Institutional Shareholder Services (ISS) and Glass Lewis) that provide voting recommendations to smaller intermediaries. This analysis groups potential policy interventions along two axes—the first axis differentiates legal and market constraints, while the second axis further distinguishes constraints by their focus on either means (the manner in which governance decisions are made) or ends (the ultimate goals pursued through governance activity). Figure I above provides a visualization of the resulting quadrants, yielding four broad categories of potential constraints on governance costs. In what follows, Part II explores legal constraints that attempt to mandate particular ends of intermediated governance. Part III analyzes market constraints on governance ends. Part IV examines market constraints on the means by which intermediaries engage in governance, and Part V considers constraining such means through legal or regulatory strategies. Ultimately, constraining the law’s grant of governance discretion to intermediaries is a difficult balancing act. Constraints on the ends are often too vague and subjective to meaningfully constrain intermediary behavior, while constraints on means face difficulties with administrability, investor expertise, and rational apathy.

## II. LEGAL CONSTRAINTS ON THE ENDS OF MASS CORPORATE GOVERNANCE

Theoretically, laws and regulations could constrain the discretion of intermediaries by requiring that they use their governance powers to pursue only certain, specified ends, while permitting such intermediaries to decide for themselves on the best means of achieving those ends. Figure II below situates such legal, ends-focused interventions in the context of other governance cost reduction strategies.

FIGURE II. THEORETICAL BEHAVIORAL CONSTRAINTS ON INTERMEDIARIES: LEGAL-ENDS



At present, both the SEC and the Department of Labor place constraints on the ends pursued by financial intermediaries in carrying out their effective voting mandates. First, the SEC imposes a duty on covered asset managers (including most mutual funds and ETFs) not only to vote proxies, but to vote them “in a manner consistent with the best interests of the fund and its shareholders.”<sup>78</sup> In this context, the “end” that such intermediaries are legally obligated to seek is the “best interests” of the fund’s investors, typically interpreted as their *financial* interests (rather than, e.g., their social interests).<sup>79</sup> While, in theory, this could function as a strict constraint, in practice, it is shockingly weak. Out of the literally millions of votes that have been cast by intermediaries, to this author’s knowledge, not a single vote has been deemed to violate this requirement. It appears that, in practice,

78. Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, Securities Act Release No. 8188, Exchange Act Release No. 47304, Investment Company Release No. 25922, 68 Fed. Reg. 6564, 6574 (Feb. 7, 2003) (codified at 17 C.F.R. pts. 239, 249, 270, 274 (2026)) (“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.”).

79. See, e.g., Fisch & Schwartz, *supra* note 1, at 21 (discussing beneficiaries’ best interests as the pursuit of long-term value).

the “best interests of the fund and its shareholders” are subjective enough to incorporate virtually any vote on any plausible ballot item.

Additionally, the Department of Labor requires that ERISA fiduciaries not prioritize nonpecuniary factors above the financial interests of plan beneficiaries.<sup>80</sup> Unlike the SEC’s “best interests” standard, this legal duty has actually produced liability for its violation, making it somewhat more substantive.<sup>81</sup> However, recent changes under the Biden administration seem to have softened the standard to some degree.<sup>82</sup> These rules significantly walked back the prior Trump-era exclusion of “nonpecuniary” factors,<sup>83</sup> with the stated objective of making it easier to consider various ESG factors that the Trump-era rules sought to bar.<sup>84</sup> Now, although fiduciaries must determine that alternative courses of action “equally serve the financial interests of the plan,” they may make such a conclusion “based on collateral benefits other than investment returns.”<sup>85</sup> However, the “paramount” concern of ERISA fiduciaries must still be “on the plan’s financial returns and risk to beneficiaries.”<sup>86</sup> Ultimately, the central goal of fiduciaries under ERISA must be to “maximize employee pension and welfare benefits,” which roughly equates to a wealth-maximization mandate.<sup>87</sup>

In their most rigorous forms, we may conceptualize both the “best interests” standard and ERISA’s fiduciary duties to maximize plan assets as effectively imposing a duty of wealth maximization.<sup>88</sup> Although there are caveats, and the strength with which this duty is enforced may vary, the primary goal of this Part is to analyze the extent to which a strict legal duty to maximize wealth can meaningfully constrain intermediaries in their governance activities. To that end, Section II.A analyzes the extent to which the obligation to maximize wealth successfully constrains the discretion of

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80. Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights, 87 Fed. Reg. 73822, 73823 (Dec. 1, 2022) (codified at 29 C.F.R. pt. 2550 (2026)) (“The Department has a longstanding position that ERISA fiduciaries may not sacrifice investment returns or assume greater investment risks as a means of promoting collateral social policy goals.”).

81. See, e.g., *Spence v. Am. Airlines, Inc.*, 775 F. Supp. 3d 963 (N.D. Tex. 2025).

82. Financial Factors in Selecting Plan Investments, 85 Fed. Reg. 72846 (Nov. 13, 2020) (codified at 29 C.F.R. pts. 2509, 2550 (2026)).

83. *Id.*

84. Prudence and Loyalty, 87 Fed. Reg. at 73823 (“The objective was to address perceived confusion about the implications of that non-regulatory guidance with respect to ESG considerations, ETIs, shareholder rights, and proxy voting.”).

85. *Id.* at 73860.

86. *Id.* at 73822 (“To maximize employee pension and welfare benefits, section 404 of ERISA dictates that the focus of ERISA plan fiduciaries on the plan’s financial returns and risk to beneficiaries must be paramount.”).

87. *Id.*

88. In less rigorous forms, these standards would operate as far weaker limitations, making the extant legal constraints on governance ends even less meaningful than they are at present.

mass corporate governors. It looks at a subset of “consensus” corporate governance issues,<sup>89</sup> and it finds substantial conflicting evidence on the financial impact of these interventions.<sup>90</sup> For an ends-focused constraint to truly limit intermediaries’ discretion, there must be clear and convincing evidence that these “best practices” are indeed optimal. However, not one of these “consensus” positions is so well supported as to limit index funds in their proxy voting behavior to one particular “wealth maximizing” position. As a result, legal mandates on the pursuit of shareholder value, whether weakly or strictly enforced, cannot meaningfully constrain the discretion of intermediaries.

Section II.B broadens the analysis laid out in Section II.A to consider the effect of mandating the pursuit of alternative ends. Although alternative maximands may better represent investors’ true preferences,<sup>91</sup> replacing the wealth maximization metric with alternative ends-based metrics would be highly unlikely to constrain agency costs. Because alternative maximands generally provide intermediaries with greater latitude in their decision making, they would constrain fiduciaries to an even lesser degree than a clear duty to maximize shareholder wealth.

#### *A. The Subjectivity of a Shareholder Wealth Maximand*

As discussed in Part I, most financial intermediaries have an effective mandate to vote on behalf of their investors, but they are neither required nor incentivized to vote particularly well.<sup>92</sup> The result is “mass corporate governance,” or one-size-fits-all governance solutions that can be applied to firms *en masse*.<sup>93</sup> Theoretically, existing limits on intermediary discretion should restrict intermediaries to governance activities that broadly maximize shareholder wealth. However, this Part critically examines whether the entities engaging in mass corporate governance are (or even can be) sufficiently constrained by such a wealth maximand.

To that end, this Section first considers the 2024 voting policies of large mass corporate governors, including four large mutual fund providers (BlackRock, Vanguard, State Street, and Fidelity)<sup>94</sup> and the two largest

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89. See Lund & Pollman, *supra* note 5, at 2620–21 (discussing intermediaries’ “consensus” best practices).

90. See *infra* Section II.A.

91. Caleb N. Griffin, *Humanizing Corporate Governance*, 75 FLA. L. REV. 689, 703–04 (2023) (providing evidence of the willingness of mutual fund investors to sacrifice profits for prosocial ends).

92. See *supra* Part I (outlining the mass corporate governance conundrum).

93. Lund & Pollman, *supra* note 5, at 2620–21.

94. While many commentators primarily discuss the “Big Three” asset managers, some commentators also include Fidelity as a fourth, terming the group the “Big Four.” See Leo E. Strine Jr.,

proxy advisors (ISS and Glass Lewis).<sup>95</sup> It considers their stated policies on twenty-two corporate governance controversies, and it sorts them into consensus positions (those shared by all six mass corporate governors), moderate consensus positions (those shared by four or five mass corporate governors), and low consensus positions (those where mass corporate governors are divided in their positions).

Were extant ends-based constraints able to meaningfully limit intermediary discretion, we would expect a high degree of agreement on most corporate governance controversies. That is, if financial research could definitively establish that a certain proposal or intervention consistently maximized shareholder wealth, and if the law effectively constrained intermediaries to the pursuit of this end, then mass corporate governors ought to have coalesced around such a value-maximizing position. However, the voting priorities of mass corporate governors in fact exhibit significant heterogeneity. As Figure III below reveals, only six of the twenty-two proposals (27%) can be considered “consensus” proposals, while nine (41%) constitute “moderate consensus” proposals, and a further seven (32%) constitute “low consensus” proposals.

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*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, 1016 (2020) (discussing the potential of the Big Four to mitigate excessive corporate political spending).

95. ISS and Glass Lewis constitute roughly 97% of the market for proxy advisory services, leading some to term it a duopoly. See Asaf Eckstein & Sharon Hannes, *A Long/Short Incentive Scheme for Proxy Advisory Firms*, 53 WAKE FOREST L. REV. 787, 818 (2018).

FIGURE III. SPECTRUM OF CONSENSUS ON CORPORATE GOVERNANCE TOPICS

*This figure summarizes the degree to which mass corporate governors (BlackRock, Vanguard, State Street, Fidelity, ISS, and Glass Lewis) share a common approach regarding core corporate governance topics as outlined in their voting guidelines for 2024. “Consensus” signifies a topic where all six have adopted a similar approach, “Moderate Consensus” signifies a topic where four to five share a common approach, and “Low Consensus” signifies a topic where they are divided in their approach.*



The lack of a common set of voting practices on most issues provides initial evidence that existing constraints on intermediary discretion are ineffectual. For the majority of interventions studied, intermediaries can and do take opposite positions without any apparent violation of their wealth maximand. In these areas, existing ends-based constraints do not necessitate any certain “wealth-maximizing” outcome.

However, there is of course a subset of “consensus” positions. All six mass corporate governors are united in their support for (1) unitary, as opposed to staggered or classified, board structure; (2) majority voting standards for director elections; (3) equal voting rights amongst shareholders; (4) minimum levels of racial, ethnic, and gender diversity amongst board members; (5) the removal or absence of shareholder rights plans; and (6) the removal or absence of supermajority vote requirements. Perhaps these positions are shared precisely because empirical research robustly establishes their positive impact on firm financials. This Part considers that empirical question.

### *1. The Limitations of Corporate Governance Empiricism*

As a general matter, efforts to empirically evaluate the impact of various corporate governance initiatives are often constrained by several interrelated methodological and contextual challenges. The first such challenge is *endogeneity*, which arises when explanatory variables exhibit a

meaningful correlation with the error term.<sup>96</sup> In the context of corporate governance, endogeneity manifests as uncertainty as to whether a given intervention causally promotes shareholder value or whether it merely serves as a proxy for other value-adding characteristics.<sup>97</sup> Governance may be both a determinant and a consequence of firm performance, with the direction of influence uncertain.<sup>98</sup>

Researchers have also recently identified significant deficiencies in commonly used corporate governance datasets.<sup>99</sup> Once such deficiencies are taken into account, conclusions reached in prior research “stand on shaky ground.”<sup>100</sup> The *unreliability* of commonly used data, and potential inaccuracies in prior research findings, complicates the hope that intermediaries might rely upon empirical insights to guide their decision making.

A further challenge is *context-specificity*, or the notion that a given governance intervention may impact firms heterogeneously.<sup>101</sup> It is likely that unique firm- or sector-specific characteristics could influence whether a governance intervention has a positive, negative, or neutral impact on firm value. For instance, takeover protections may be more valuable for firms at high-risk of takeover, and less valuable for firms at a lower risk of takeover.<sup>102</sup> Without attention to context, empirical analyses of various interventions may yield misleading conclusions.

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96. See Michal Barzuza & Quinn Curtis, *Board Interlocks and Corporate Governance*, 39 DEL. J. CORP. L. 669, 693 (2015) (discussing endogeneity in the context of board interlocks).

97. Byung Hyun Ahn, Jill E. Fisch, Panos N. Patatoukas & Steven Davidoff Solomon, *Synthetic Governance*, 2021 COLUM. BUS. L. REV. 476, 487 (“In addition, many studies of corporate governance suffer from an endogeneity problem. They cannot separate out whether governance is causing a value increase in the firm or governance is a proxy for other characteristics which enhance firm value.”); see also Yakov Amihud, Markus Schmid & Steven Davidoff Solomon, *Settling the Staggered Board Debate*, 166 U. PA. L. REV. 1475, 1502 (2018) (“The key question that stems from the issue of selection and endogeneity is whether the presence of a staggered board affects firm value, or whether the firm’s low value causes a staggered board to be adopted.”).

98. Amihud et al., *supra* note 97, at 1502.

99. Jens Frankenreiter, Cathy Hwang, Yaron Nili & Eric Talley, *Cleaning Corporate Governance*, 170 U. PA. L. REV. 1, 64 (2021).

100. *Id.*

101. Ahn et al., *supra* note 97, at 488 (“A substantial percentage of corporate governance studies assume that it will, examining the effect of a particular corporate governance provision across all firms and evaluating the effect of that provision on the average firm. Yet this assumption is problematic. Firms differ substantially along various dimensions, and the effects of specific governance terms may be heterogeneous as well.”).

102. See Lund, *supra* note 25, at 870 (“[A] governance structure that promotes accountability to shareholders might offer greater benefits at large firms than small firms because large firms face less of a threat of a takeover or proxy contest and may be under less competitive pressure. Likewise, small firms are more likely to have controlling shareholders and a high percentage of insider owners, meaning that a pro-shareholder governance structure will not offer as much (or any) benefit.”).

Furthermore, some studies of the value impact of corporate governance interventions may capture only the market's initial perception of the value of such interventions, rather than their true financial impact. To the extent that such perceptions may change over time, this may give rise to *nonstationarity*, which can reduce the reliability of standard modeling techniques.<sup>103</sup> Overall, these and related empirical challenges attenuate any potential optimism about empirically “proving” the optimality of a given governance intervention.

## 2. *Unitary v. Staggered Board Structure*

Generally speaking, a firm may have either a unitary board<sup>104</sup> or a staggered (or classified) board.<sup>105</sup> Firms with unitary boards will hold annual elections for all director positions,<sup>106</sup> while firms with staggered boards will only have a portion (commonly, one-third) of director positions open for election in a given year.<sup>107</sup> Proponents of staggered boards argue that they enable long-term planning<sup>108</sup> and reduce the risk of inefficient

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103. See Bernard S. Sharfman, *What Theory and the Empirical Evidence Tell Us About Proxy Access*, 13 J.L. ECON. & POL'Y 1, 28 (2017) (discussing nonstationarity in the context of proxy access and arguing that “as the market becomes more informed about the real impact of an event, the market may change its opinion on how the event affects shareholder value”).

104. See, e.g., DEL. CODE ANN. tit. 8, § 211 (West 2025) (“[A]n annual meeting of stockholders shall be held for the election of directors on a date and at a time designated by or in the manner provided in the bylaws.”).

105. See, e.g., DEL. CODE ANN. tit. 8, § 141 (West 2025) (“[D]irectors of any corporation organized under this chapter may, by the certificate of incorporation or by an initial bylaw, or by a bylaw adopted by a vote of the stockholders, be divided into 1, 2 or 3 classes; the term of office of those of the first class to expire at the first annual meeting held after such classification becomes effective; of the second class 1 year thereafter; of the third class 2 years thereafter; and at each annual election held after such classification becomes effective, directors shall be chosen for a full term, as the case may be, to succeed those whose terms expire.”).

106. Andrew A. Schwartz, *Corporate Legacy*, 5 HARV. BUS. L. REV. 237, 246 (2015) (“The default is an unclassified board of directors whereby every director is up for election every year.”).

107. Lucian Arye Bebchuk, John C. Coates IV & Guhan Subramanian, *The Powerful Antitakeover Force of Staggered Boards: Theory, Evidence, and Policy*, 54 STAN. L. REV. 887, 893 (2002) (“In a company with a staggered board, directors are grouped into classes (typically three), with each class elected at successive annual meetings. For example, a board with twelve directors might be grouped into three classes, with four directors standing at the 2001 annual meeting, four more directors standing for reelection in 2002, and the remaining four directors standing for reelection in 2003. With three classes, directors in each class would be elected to three-year terms.”).

108. Martin Lipton & Marshall P. Shaffer, *Wachtell Lipton Discusses Staggered Boards, Long-Term Investments and Long-Term Firm Value*, CLS BLUE SKY BLOG (Dec. 3, 2015), <https://clsbluesky.law.columbia.edu/2015/12/03/wachtell-lipton-discusses-staggered-boards-long-term-investments-and-long-term-firm-value/> [<https://perma.cc/6YXS-Y3ME>].

hostile takeovers,<sup>109</sup> while opponents argue that they reduce accountability to shareholders<sup>110</sup> and increase entrenchment.<sup>111</sup>

Amongst mass corporate governors, there is broad opposition to staggered boards.<sup>112</sup> Such widespread opposition to staggered boards might appear to imply a widespread consensus that unitary boards are objectively superior. Consistent with the theme of this Part, however, the research is inconclusive.<sup>113</sup>

FIGURE IV. SUMMARY OF EMPIRICAL RESEARCH ON VALUE IMPACT OF UNITARY V. STAGGERED BOARDS



As Figure IV above reveals, there are three strands within the empirical literature. One strand argues that staggered boards are value-decreasing.<sup>114</sup> A second strand of the research argues just the opposite—that staggered boards are value-enhancing.<sup>115</sup> A third view is that classified boards have

109. K.J. Martijn Cremers, Lubomir P. Litov & Simone M. Sepe, *Staggered Boards and Long-Term Firm Value, Revisited*, 126 J. FIN. ECON. 422, 424 (2017) (“[S]taggered boards could contribute to firm value by preventing inefficient takeovers and/or serving to bond a firm’s commitment to the firm’s long-term stakeholders”).

110. Kobi Kastiel & Yaron Nili, *The Corporate Governance Gap*, 131 YALE L.J. 782, 825 (2022) (“By requiring directors to focus on the interests of shareholders, annual elections could thereby improve firm performance and market value.”).

111. Amihud et al., *supra* note 97, at 1475 (“One theory claims that a staggered board facilitates entrenchment of inefficient management and thus harms corporate value.”).

112. *See supra* Figure III.

113. *See, e.g.*, Ahn et al., *supra* note 97, at 486 (“On the question of whether a staggered board of directors affects firm value, for example, one group of scholars has consistently argued that staggered boards reduce value. A second group finds the opposite—that staggered boards increase the value of at least some firms. A third set of scholars critiques both groups’ studies and concludes that the effect of a staggered board is idiosyncratic and firm-specific.” (footnotes omitted)); Ofer Eldar, *A Lawyer’s Guide to Empirical Corporate Governance*, 27 STAN. J.L. BUS. & FIN. 1, 68 (2022) (“Despite all the studies and all the data, there is still much we don’t know about whether staggered boards are desirable.”).

114. *See* Lucian Bebchuk, Scott Hirst & June Rhee, *Towards the Declassification of S&P 500 Boards*, 3 HARV. BUS. L. REV. 157, 164 (2013) (discussing a series of empirical studies “reporting that classified boards are associated with lower firm value and inferior outcomes for shareholders”).

115. *See, e.g.*, Cremers et al., *supra* note 109, at 422 (“We find no evidence that staggered board changes are negatively related to firm value. However, we find a positive relation for firms engaged in innovation and where stakeholder relationships matter more. This suggests that staggered boards

no impact on firm value,<sup>116</sup> or at least no consistent impact on firm value at the aggregate level.<sup>117</sup> Given the significant disagreement on this issue, it appears the debate over the value impact of staggered boards remains unsettled, despite the apparent consensus amongst mass corporate governors.<sup>118</sup>

### 3. *Voting Standards for Director Elections*

There are two main voting standards for director elections: plurality voting and majority voting. Under a plurality voting standard, nominees that receive the most “for” votes will be elected to the board of directors.<sup>119</sup> In contrast, majority voting standards require that board nominees receive more “for” votes than “withhold” or “against”<sup>120</sup> votes.<sup>121</sup> Because the vast majority of corporate elections go uncontested,<sup>122</sup> the voting standard

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promote value creation for some firms by committing the firm to undertaking long-term projects and bonding it to the relationship-specific investments of its stakeholders.”).

116. Amihud et al., *supra* note 97, at 1477 (arguing that “a staggered board has no significant effect on firm value”).

117. Lawrence A. Cunningham, *The Case for Empowering Quality Shareholders*, 46 *BYU L. REV.* 1, 41 (2020) (“The scholarly attempt to settle the board structure sub-debate is consistent with the views of quality shareholders on such issues: context matters, and different companies need different governance features. While on its face such an assertion seems obvious to make and easy to defend, many scholars and most indexers—but not quality shareholders—have assumed that staggered boards are always good or bad.”).

118. *See, e.g.*, K.J. Martijn Cremers, Simone M. Sepe & Saura Masconale, Essay, *Is the Staggered Board Debate Really Settled?*, 167 *U. PA. L. REV. ONLINE* 9, 9 (2019) (“This Essay addresses the ASDS study and shows that the staggered board debate is very much alive rather than settled.”).

119. Vincent Falcone, Note, *Majority Voting in Director Elections: A Simple, Direct, and Swift Solution?*, 2007 *COLUM. BUS. L. REV.* 844, 847 (“Director elections in the United States have traditionally been conducted by plurality voting. Under a plurality voting regime, a candidate for director must receive a greater number of the votes cast in an election than any other candidate in order to obtain a board seat, even if he or she does not receive an outright majority.”).

120. Companies with a plurality standard tend to use the term “withhold” while companies with a majority standard tend to use the term against, although this varies between individual companies. *See* ISS STOXX, U.S. PROXY VOTING GUIDELINES 10 n.2 (2025), <https://www.iss-stoxx.com/file/policy/current/americas/us-voting-guidelines.pdf> [<https://perma.cc/B95B-9TTQ>] (“In general, companies with a plurality vote standard use ‘Withhold’ as the contrary vote option in director elections; companies with a majority vote standard use ‘Against’. However, it will vary by company and the proxy must be checked to determine the valid contrary vote option for the particular company.”).

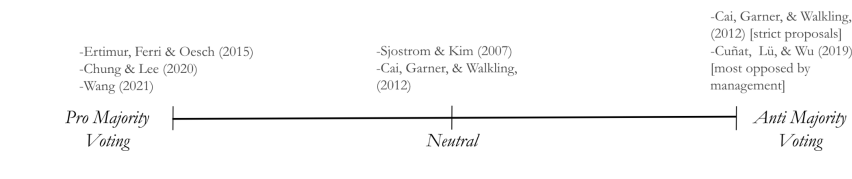
121. Geeyoung Min, *Shareholder Voice in Corporate Charter Amendments*, 43 *J. CORP. L.* 289, 307 (2018) (“Under the majority voting rule, by contrast, a candidate must receive more ‘for’ votes than ‘withhold’ votes.”).

122. William K. Sjoström, Jr. & Young Sang Kim, *Majority Voting for the Election of Directors*, 40 *CONN. L. REV.* 459, 467 (2007) (“The bottom line is that the vast majority of director elections are uncontested, and therefore under a plurality voting standard victory for management candidates is assured.”).

employed by a corporation dramatically impacts shareholder power.<sup>123</sup> Given a plurality standard, an uncontested director candidate can be elected to the board even in the face of significant opposition.<sup>124</sup> Indeed, just one single “for” vote would guarantee election, thus rendering oppositional votes functionally irrelevant.<sup>125</sup> In contrast, a majority voting standard requires an uncontested director candidate achieve majority support, such that oppositional votes could prevent the election of an unpopular director.<sup>126</sup>

Beginning in roughly 2007, a highly successful push to increase accountability to shareholders prompted widespread conversion from the plurality standard to the majority standard,<sup>127</sup> such that the majority standard now predominates.<sup>128</sup> For their part, mass corporate governors overwhelmingly support majority voting standards. BlackRock, Vanguard, Fidelity, and State Street uniformly support majority voting, as does the proxy advisory duopoly of ISS and Glass Lewis.<sup>129</sup>

FIGURE V. SUMMARY OF EMPIRICAL RESEARCH ON VALUE IMPACT OF MAJORITY V. PLURALITY VOTING STANDARDS



123. See Joshua R. Mourning, Note, *The Majority-Voting Movement: Curtailing Shareholder Disenfranchisement in Corporate Director Elections*, 85 WASH. U. L. REV. 1143, 1160–61 (2007) (“Majority voting, in giving effect to their withheld votes, provides shareholders an effective way to vote against a director.”).

124. Stephen J. Choi, Jill E. Fisch, Marcel Kahan & Edward B. Rock, *Does Majority Voting Improve Board Accountability?*, 83 U. CHI. L. REV. 1119, 1119 (2016) (“This means that in uncontested elections, a candidate who receives even a single vote is elected. Proponents of shareholder democracy have advocated a shift to a majority voting rule, in which a candidate must receive a majority of the votes cast to be elected.”).

125. *Id.*

126. Sjostrom & Kim, *supra* note 122, at 468 (“Under a majority voting standard, if shareholders holding a majority of shares were dissatisfied with a director, they could express this dissatisfaction by voting against him; the director would not receive the requisite majority vote and therefore would not be elected.”).

127. Choi et al., *supra* note 124, at 1119 (“Proponents of shareholder democracy have advocated a shift to a majority voting rule, in which a candidate must receive a majority of the votes cast to be elected. Over the past decade, they have been successful, and the shift to majority voting has been one of the most popular and successful governance reforms.”).

128. GLASS LEWIS, 2024 BENCHMARK POLICY GUIDELINES 45 (2024), <https://www.glasslewis.com/wp-content/uploads/2023/11/2024-US-Benchmark-Policy-Guidelines-Glass-Lewis.pdf> [https://perma.cc/4QKP-JUD2] (“In 2019, 89% of the S&P 500 Index had implemented a resignation policy for directors failing to receive majority shareholder support, compared to 65% in 2009.”).

129. See *supra* Figure III.

The widespread support for majority voting standards might appear to intimate their superiority. However, empirical research on majority voting remains limited and inconclusive. Some studies do, in fact, link majority voting with positive financial effects.<sup>130</sup> However, other research finds instead that majority voting standards have a negative impact on financial performance, at least at certain firms. In particular, stricter approaches to majority voting standards may be associated with a negative market reaction,<sup>131</sup> and a negative market reaction is also observed for firms most resistant to majority voting.<sup>132</sup> Still other research suggests that majority voting standards have no impact on director election, firm performance, or shareholder wealth,<sup>133</sup> and that there is no positive or negative announcement return associated with the adoption of majority voting standards.<sup>134</sup> The non-impact associated with majority voting standards may be due to their overall insignificance, or to the watered-down approach to majority voting that predominates amongst adopters.<sup>135</sup> Figure V above summarizes these findings.

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130. Yonca Ertimur, Fabrizio Ferri & David Oesch, *Does the Director Election System Matter? Evidence from Majority Voting*, 20 REV. ACCT. STUD. 1 (2015) (“Using a regression discontinuity design, we document abnormal returns of 1.43–1.60 % around annual meeting dates where shareholder proposals to adopt MV are voted upon, suggesting that shareholders perceive the adoption of MV as value-enhancing.”); see also Kee H. Chung & Choonsik Lee, *Voting Methods for Director Election, Monitoring Costs, and Institutional Ownership*, 113 J. BANKING & FIN., Jan. 2020, art. no. 105738, at 1 (arguing that “investors react favorably to the adoption of majority voting because it reduces management monitoring costs by improving the accountability of elected board members”).

131. See Ralph Walkling, *Majority Vs. Plurality: Disruption Ahead?*, DIRS. & BDS., (July 1, 2009), <https://www.directorsandboards.com/uncategorised/singlemajority-vs-plurality-disruption-ahead/> [<https://perma.cc/T38V-SDWE>] (“However, majority provisions vary in the amount of restrictions they impose on management, and the market reaction is significantly more negative when the terms of the majority voting provision are more binding.”).

132. Vicente Cuñat, Yiqing Lü & Hong Wu, *Managerial Response to Shareholder Empowerment: Evidence from Majority Voting Legislation Changes*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Oct. 1, 2019), <https://corpgov.law.harvard.edu/2019/10/01/managerial-response-to-shareholder-empowerment-evidence-from-majority-voting-legislation-changes/> [<https://perma.cc/NB3D-DDVP>] (“We find that after the enactment of the majority voting standard; however, the market reaction turns from neutral to negative. The results show that managers of firms for which the new legislation is likely to impose the greatest cost or the least benefit, tend to show the greatest resistance towards implementing the new standard. The findings indicate that managers do care about shareholder value and that majority voting can be detrimental for some firms in the sample.”).

133. Jay Cai, Jacqueline L. Garner & Ralph A. Walkling, *A Paper Tiger? An Empirical Analysis of Majority Voting*, 21 J. CORP. FIN. 119, 133 (2013) (“[M]ajority voting has no significant impact on director election, firm performance, and shareholder wealth.”).

134. Sjostrom & Kim, *supra* note 122, at 463 (finding no statistically significant market reaction to the announcement that a firm will adopt majority voting standards).

135. See Cai et al., *supra* note 133, at 119 (“Our results are consistent with the paper tiger hypothesis.”); Sjostrom & Kim, *supra* note 122, at 459 (“After analyzing the forms of majority voting implemented by these companies, we conclude that majority voting, as put into action, is little more than smoke and mirrors.”).

Overall, research on the impact of the voting standards for director elections is inconsistent on the degree, vector, and extent of the impact. The result is that even a robustly enforced shareholder value maximand would fail to obligate intermediaries to any given voting position on the issue.

#### 4. *Equal Voting Rights*

Voting-rights structures may feature equal voting rights (where one share equates to one vote)<sup>136</sup> or disproportionate voting rights.<sup>137</sup> Disproportionate voting rights are commonly achieved via dual-class share structures, wherein common stock is divided into “high vote” stock with greater voting rights and “low vote” stock with lower voting rights.<sup>138</sup> High vote stock is generally retained by founders and/or early stage investors, while low vote stock is available to the broader public.<sup>139</sup> Supporters of equal voting rights argue that such structures ensure that economic interests and control rights are well aligned, and that they minimize entrenchment and reduce agency costs.<sup>140</sup> In contrast, supporters of dual-class share structures argue that this approach insulates leadership from outside pressures and disruptions, thereby promoting innovation and preserving the corporate mission.<sup>141</sup> Mass corporate governors have adopted the former posture, and they uniformly support equal voting rights.<sup>142</sup>

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136. Min Yan, *A Control-Accountability Analysis of Dual Class Share (DSC) Structures*, 45 DEL. J. CORP. L. 1, 6 (2020) (“One share-one vote (‘OSOV’) is seen as ‘[t]he most basic statutory rule of voting’ in corporate law, especially in a world of shareholder democracy.”).

137. Gladriel Shobe & Jarrod Shobe, *The Dual-Class Spectrum*, 39 YALE J. ON REG. 1343, 1343 (2022) (“If a company grants certain shareholders a separate class of stock with disproportionate voting rights, then the company is treated as a dual-class company.”).

138. Ahn et al., *supra* note 97, at 499 (“In a company with dual class stock, all the shares of common stock have equal economic rights, but some shares, termed high-vote shares, have more voting rights than the others, which are termed low-vote shares.”).

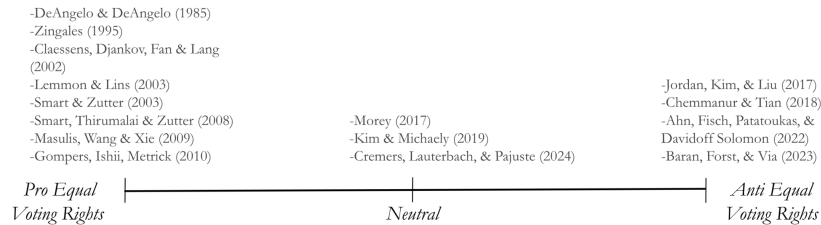
139. *Id.* at 499–500.

140. Shobe & Shobe, *supra* note 137, at 1351–52 (summarizing arguments in support of equal voting rights).

141. Dorothy S. Lund, *Nonvoting Shares and Efficient Corporate Governance*, 71 STAN. L. REV. 687, 693 (2019) (“By contrast, proponents of dual-class structures have consistently claimed that nonvoting and low-voting stock have valuable uses. Most importantly, they contend that dual-class structures allow those who control the company—whether it be the family in a family-owned business or the visionary founders of a successful technology company—to retain control without having to bear excessive risk.” (citation omitted)).

142. *See supra* Figure III.

FIGURE VI. SUMMARY OF EMPIRICAL RESEARCH  
ON EQUAL VOTING RIGHTS



As Figure VI above reveals, empirical data on the financial impact of equal and disproportionate voting rights remains inconclusive. One strand of the literature associates equal voting rights with superior financial performance,<sup>143</sup> while another strand of the literature finds just the opposite.<sup>144</sup> A third body of research suggests that the financial impact is neutral, at least at the aggregate level,<sup>145</sup> or that the financial impact of voting structure varies over a company's life cycle.<sup>146</sup> Based upon these disparate findings, there is no clear consensus on which voting rights orientation maximizes shareholder wealth. As a result, intermediaries would

143. See, e.g., Michael L. Lemmon & Karl V. Lins, *Ownership Structure, Corporate Governance, and Firm Value: Evidence from the East Asian Financial Crisis*, 58 J. FIN. 1455, 1455 (2003) (“Crisis period stock returns of firms in which managers have high levels of control rights, but have separated their control and cash flow ownership, are 10–20 percentage points lower than those of other firms.”); Ronald W. Masulis, Cong Wang & Fei Xie, *Agency Problems at Dual-Class Companies*, 64 J. FIN. 1697, 1722 (2009) (“Our evidence is consistent with the hypothesis that insiders holding more voting rights relative to cash flow rights extract more private benefits at the expense of outside shareholders.”); Paul A. Gompers, Joy Ishii & Andrew Metrick, *Extreme Governance: An Analysis of Dual-Class Firms in the United States*, 23 REV. FIN. STUD. 1051, 1084–85 (2010) (finding gaps between insiders’ voting rights and their equity ownership leads to underperformance).

144. See, e.g., Bradford D. Jordan, Soohyung Kim & Mark H. Liu, *Growth Opportunities, Short-Term Market Pressure, and Dual-Class Share Structure*, 41 J. CORP. FIN. 304, 304 (2016) (“The dual-class share structure *increases* the market valuation of high growth firms, in contrast to the finding in the literature that dual-class firms trade at lower valuations.”); Ahn et al., *supra* note 97, at 511 (back-testing the performance of “Dual Index” comprised of companies with dual-class share structures and finding that they outperform the broader market).

145. See, e.g., GABRIEL MOREY, COUNCIL OF INST. INV.’S, MULTI-CLASS STOCK AND FIRM VALUE 31 (2017), [https://www.cii.org/files/publications/misc/05\\_10\\_17\\_dual-class\\_value\\_study.pdf](https://www.cii.org/files/publications/misc/05_10_17_dual-class_value_study.pdf) [<https://perma.cc/CSS6-NM9Y>] (“[A] multi-class common equity structure with unequal voting rights neither increases nor decreases a company’s annualized return on invested capital (ROIC).”).

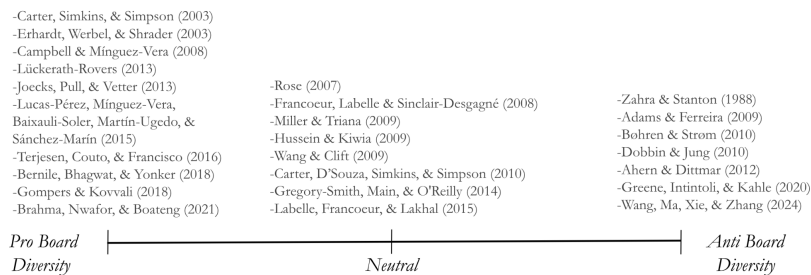
146. Martijn Cremers, Beni Lauterbach & Anete Pajuste, *The Life Cycle of Dual-Class Firm Valuation*, 13 REV. CORP. FIN. STUD. 459, 459 (2024) (“At the IPO, dual-class firms have higher mean valuations than do single-class firms, and some evidence indicates that this premium may emanate from dual-class firm founders’ unique vision and leadership skills. As firms age, the valuation premium of dual-class firms tends to dissipate, possibly because dual-class agency problems increase due to a gradual widening of the wedge (the difference between insider voting and cash flow rights) in the post-IPO years.”).

remain unbound in their voting on this issue, even presuming a strictly enforced shareholder wealth maximand.

### 5. Board Diversity

Public company board members have historically been, and continue to be, significantly unrepresentative of the broader public.<sup>147</sup> Given this inequity, there has been a movement to promote increased diversity in board membership, particularly in the form of increased racial, ethnic, and gender diversity.<sup>148</sup> There is strong support for board diversity amongst mass corporate governors, including support for at least a minimum degree of board diversity from BlackRock, Vanguard, State Street, Fidelity, ISS, and Glass Lewis.<sup>149</sup>

FIGURE VII. SUMMARY OF EMPIRICAL RESEARCH ON BOARD DIVERSITY



In addition to important moral arguments in support of board diversity,<sup>150</sup> there is a sizable body of research suggesting that board diversity improves firm financial performance.<sup>151</sup> However, there is also research indicating

147. Chris Brummer & Leo E. Strine, Jr., *Duty and Diversity*, 75 VAND. L. REV. 1, 9 (2022) (“Yet American corporate leadership is markedly unrepresentative of our nation’s diversity—a reality that stands in stark contrast to broad calls for fairer economic opportunity and participation.”).

148. See *id.* at 1 (discussing the broader movement to diversify corporate boards).

149. See *supra* Figure III.

150. Deborah L. Rhode & Amanda K. Packel, *Diversity on Corporate Boards: How Much Difference Does Difference Make?*, 39 DEL. J. CORP. L. 377 *passim* (2014) (discussing social justice, equal opportunity, and corporate reputational justifications for board diversity).

151. See, e.g., Gennaro Bernile, Vineet Bhagwat & Scott Yonker, *Board Diversity, Firm Risk, and Corporate Policies*, 127 J. FIN. ECON. 588, 588 (2018) (“We examine the effects of diversity in the board of directors on corporate policies and risk. Using a multidimensional measure, we find that greater board diversity leads to lower volatility and better performance.”); Niclas L. Erhardt, James D. Werbel & Charles B. Shrader, *Board of Director Diversity and Firm Financial Performance*, 11 CORP. GOVERNANCE 102, 107–08 (2003) (finding a positive relationship between board diversity and financial performance); Paul Gompers & Silpa Kovvali, *The Other Diversity Dividend*, HARV. BUS. REV., July–Aug. 2018, at 72, 75 (finding a positive association between diversity and performance amongst venture capital firms).

that board diversity has a neutral<sup>152</sup> or negative<sup>153</sup> impact on firm performance. Figure VII above summarizes these conflicting findings. Assuming a pure shareholder wealth maximand, these varied empirical studies are insufficient to constrain intermediary discretion on the issue of board diversity, and intermediary support for board diversity is thus not guaranteed going forward.<sup>154</sup>

### 6. Shareholder Rights Plans

Shareholder rights plans (or “poison pills”) emerged as a highly effective defense against hostile takeovers in the early 1980s.<sup>155</sup> Once triggered by an attempted hostile takeover, these rights plans permit all shareholders, except the would-be acquirer, to purchase shares of a target company or merged entity at a significant discount.<sup>156</sup> Proponents argue that rights plans enable directors to protect shareholders from coercive hostile bidders, deter self-dealing transactions, and generate a higher premium for a company’s stock in the event of a takeover.<sup>157</sup> Opponents, on the other hand, argue that rights plans entrench management,<sup>158</sup> deter beneficial takeovers,<sup>159</sup> and reduce

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152. See, e.g., David A. Carter, Frank D’Souza, Betty J. Simkins & W. Gary Simpson, *The Gender and Ethnic Diversity of U.S. Boards and Board Committees and Performance*, 18 CORP. GOVERNANCE 396, 400 (2010) (“We do not find a significant relationship between the gender or ethnic diversity of the board, or important board committees, and financial performance for a sample of major US corporations.”); Ian Gregory-Smith, Brian G.M. Main & Charles A. O’Reilly III, *Appointments, Pay and Performance in UK Boardrooms by Gender*, 124 ECON. J. F109, F109 (2014) (“[T]he article finds no support for the argument that gender diverse boards enhance corporate performance. Proposals in favour of greater board diversity may be best structured around the moral value of diversity, rather than with reference to an expectation of improved company performance.”).

153. See, e.g., Renée B. Adams & Daniel Ferreira, *Women in the Boardroom and Their Impact on Governance and Performance*, 94 J. FIN. ECON. 291, 291 (2009) (“[T]he average effect of gender diversity on firm performance is negative.”); Kenneth R. Ahern & Amy K. Dittmar, *The Changing of the Boards: The Impact on Firm Valuation of Mandated Female Board Representation*, 127 Q.J. ECON. 137, 137 (2012) (associating a Norwegian board gender quota with “younger and less experienced boards, increases in leverage and acquisitions, and deterioration in operating performance”).

154. See, e.g., Rebecca Ungarino, *BlackRock Cuts Back on Board Diversity Push in Proxy-Vote Guidelines*, BARRON’S (Dec. 30, 2024), <https://www.barrons.com/articles/blackrock-diversity-proxy-guidelines-0bd45352> [<https://perma.cc/5UBX-BLES>] (discussing how “the world’s largest money manager has pulled back from publicizing efforts to incorporate environmental, social, and corporate governance, or ESG, considerations in its decision-making after a fierce Republican-led backlash”).

155. See Patrick J. Thompson, Note, *Shareholder Rights Plans: Shields or Gavels?*, 42 VAND. L. REV. 173, 178 (1989) (“Most boards of directors have adopted poison pill plans in response to the dramatic rise in highly leveraged and speculative takeovers during the 1980s.” (footnotes omitted)).

156. See *id.* at 187–89 (discussing justifications for poison pills).

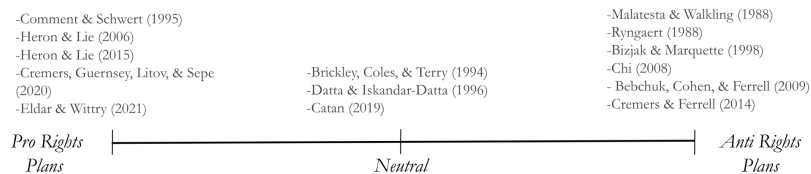
157. See *id.* at 190–91 (discussing opposition to poison pills).

158. Alan M. Long, Note, *Locking the Boardroom Door: What Can Georgia Courts Learn from Recent Delaware Poison Pill Decisions?*, 32 GA. ST. U. L. REV. 727, 746 (2016).

159. See Julian Velasco, *The Enduring Illegitimacy of the Poison Pill*, 27 J. CORP. L. 381, 384 (2002) (noting that poison pills can be used to prevent takeovers “regardless of their underlying merit”).

firm value.<sup>160</sup> Mass corporate governors, including BlackRock, Vanguard, State Street, Fidelity, ISS, and Glass Lewis, generally oppose such plans.<sup>161</sup>

### FIGURE VIII. SUMMARY OF EMPIRICAL RESEARCH ON SHAREHOLDER RIGHTS PLANS



Despite this consensus, opposition to rights plans is not mandated by a wealth maximand. As Figure VIII above reveals, the literature on the value impact of rights plans exhibits significant heterogeneity. Some studies associate rights plans with increased value for shareholders,<sup>162</sup> while other findings suggest that rights plans have a negative impact on firm value.<sup>163</sup> Still other research indicates that rights plans do not have a consistent impact on firm value.<sup>164</sup> Thus, mass corporate governors' consensus

160. Long, *supra* note 158, at 746; see John C. Coates IV, *Empirical Evidence on Structural Takeover Defenses: Where Do We Stand?*, 54 U. MIA. L. REV. 783 (2000) (“Academic hostility to defenses has been built in large part on the common belief that defenses reduce firm value, a view that is thought to be supported by both economic theory and empirical evidence.”).

161. See *supra* Figure III.

162. See, e.g., Robert Comment & G. William Schwert, *Poison or Placebo? Evidence on the Deterrent and Wealth Effects of Modern Antitakeover Measures*, 39 J. FIN. ECON. 3, 3 (1995) (“We show that poison pills and control share laws are reliably associated with higher takeover premiums for selling shareholders, both unconditionally and conditional on a successful takeover.”); K.J. Martijn Cremers, Scott B. Guernsey, Lubomir P. Litov & Simone M. Sepe, *Shadow Pills, Pill Policy, and Firm Value* (Eur. Corp. Governance Inst., Working Paper No. 595/2019, 2020), [https://www.ecgi.global/sites/default/files/working\\_papers/documents/cremersgeurnseylitovsepefinal.pdf](https://www.ecgi.global/sites/default/files/working_papers/documents/cremersgeurnseylitovsepefinal.pdf) [<https://perma.cc/AU8X-CLLX>] (“We document that a strengthened shadow pill promotes the use of actual poison pills and increases firm value – especially for more innovative firms or firms with stronger stakeholder relationships, and for hostile acquisition targets.”).

163. See, e.g., Paul H. Malatesta & Ralph A. Walkling, *Poison Pill Securities: Stockholder Wealth, Profitability, and Ownership Structure*, 20 J. FIN. ECON. 347, 349 (1988) (“Our estimates indicate that poison pill defenses reduce stockholder wealth by a statistically significant amount.”); Lucian Bebchuk, Alma Cohen & Allen Ferrell, *What Matters in Corporate Governance?*, 22 REV. FIN. STUD. 783, 783 (2009) (finding that poison pills, among other components of an entrenchment index, “are monotonically associated with economically significant reductions in firm valuation as well as large negative abnormal returns during the 1990–2003 period”).

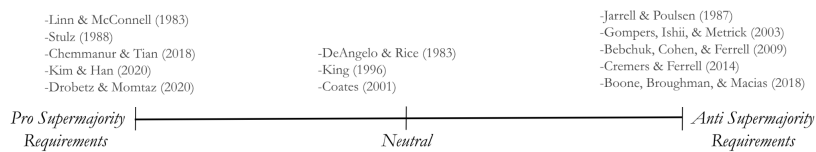
164. See, e.g., James A. Brickley, Jeffery L. Coles & Rory L. Terry, *Outside Directors and the Adoption of Poison Pills*, 35 J. FIN. ECON. 371, 371 (1994) (“We find that the average stock-market reaction to announcements of poison pills is positive when the board has a majority of outside directors and negative when it does not.”); Emiliano M. Catan, *The Insignificance of Clear-Day Poison Pills*, 48 J. LEGAL STUD. 1, 1 (2019) (“[T]he ostensive negative effect of pills on firm value is due to a spurious correlation and that prior analyses were incorrect in concluding that pill adoptions are harmful and indicative of bad governance.”).

opposition to rights plans is not the result of definitive evidence of their negative impact on firm value.

### 7. *Supermajority v. Simple Majority Vote Requirements*

Supermajority requirements mandate a heightened level of support beyond a simple majority threshold.<sup>165</sup> Such heightened thresholds may be required for charter amendments, bylaw amendments, or merger approvals.<sup>166</sup> Supporters contend that supermajority requirements promote long-term thinking, protect minority shareholders, and reduce opportunistic takeovers.<sup>167</sup> Opponents, on the other hand, argue that supermajority requirements entrench management and reduce shareholder rights.<sup>168</sup> Taking the latter view, mass corporate governors exhibit considerable opposition to supermajority vote requirements.<sup>169</sup>

FIGURE IX. SUMMARY OF EMPIRICAL RESEARCH  
ON SUPERMAJORITY VOTE REQUIREMENTS



Despite widespread opposition to supermajority vote requirements, research on the impact associated with such requirements remains inconclusive. While some studies identify negative impacts associated with supermajority requirements,<sup>170</sup> other research suggests that such

165. J.S. Park, Blasius, *Bylaw Amendment Powers & Supermajority Amendment Bylaws*, 18 U.C. DAVIS BUS. L.J. 129, 131 (2017).

166. K.J. Martijn Cremers, Saura Masconale & Simone M. Sepe, *Commitment and Entrenchment in Corporate Governance*, 110 NW. U. L. REV. 727, 731 (2016).

167. Brett W. King, *The Use of Supermajority Voting Rules in Corporate America: Majority Rule, Corporate Legitimacy, and Minority Shareholder Protection*, 21 DEL. J. CORP. L. 895, 918–19 (1996) (discussing benefits believed to be associated with supermajority voting).

168. See Park, *supra* note 165 (discussing reasons that supermajority requirements may “undermine shareholders”).

169. See *supra* Figure III.

170. See, e.g., Bebchuk et al., *supra* note 163, at 783 (finding that supermajority requirements, among other components of an entrenchment index, are linked to “economically significant reductions in firm valuation as well as large negative abnormal returns during the 1990–2003 period”); Gregg A. Jarrell & Annette B. Poulsen, *Shark Repellents and Stock Prices: The Effects of Antitakeover Amendments Since 1980*, 19 J. FIN. ECON. 127 (1987) (finding a negative association between supermajority voting requirements and returns).

requirements have a neutral or insignificant impact on firm performance.<sup>171</sup> Still other studies indicate that supermajority voting requirements may have a positive impact on firm value or firm operations.<sup>172</sup> Figure IX above summarizes these research findings.

Ultimately, this Section has revealed that mass corporate governors are entirely unconstrained by extant mandates on the ends of corporate governance. Not only do similarly situated mass corporate governors routinely vote in opposite ways on controversial ballot items, even “consensus” positions lack convincing empirical support. The result is that wealth maximands likely cannot constrain intermediaries in their stewardship behaviors.

### *B. The Subjectivity Inherent in Alternative Maximands*

However, ends-based constraints do not necessarily imply a shareholder wealth maximand. Intermediaries might instead be mandated to pursue alternative ends. While a shift to alternative maximands might better represent investors’ true interests,<sup>173</sup> it would likely only *increase* the discretion available to intermediaries, thereby exacerbating associated agency costs.

As an example, imagine that intermediaries<sup>174</sup> were obliged to maximize overall portfolio value (commonly referred to as a “portfolio primacy”

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171. See, e.g., King, *supra* note 167, at 940 (“[T]he tests conducted for this article show that in most instances, supermajority voting rules neither affect the ultimate outcome of corporate shareholder votes for targets in M&A transactions nor increase the price received by tendering shareholders.”); John C. Coates IV, *Takeover Defenses in the Shadow of the Pill: A Critique of the Scientific Evidence*, 79 TEX. L. REV. 271, 337 (2000) (“[T]his survey of the scientific evidence on takeover defenses from the past twenty years has found that it provides no strong support for either opposing or supporting defenses.”).

172. See, e.g., W. Drobetz & Paul P. Momtaz, *Antitakeover Provisions and Firm Value: New Evidence from the M&A Market*, 62 J. CORP. FIN. 2020, art. no. 101594 (“We document that, in Germany, firms with stronger ATPs, and particularly supermajority provisions, are better acquirers.”); Thomas J. Chemmanur & Xuan Tian, *Do Antitakeover Provisions Spur Corporate Innovation? A Regression Discontinuity Analysis*, 53 J. FIN. & QUANTITATIVE ANALYSIS 1163 (2018) (finding a positive impact of antitakeover provisions, including supermajority vote requirements, on innovation); Scott C. Linn & John J. McConnell, *An Empirical Investigation of the Impact of ‘Antitakeover’ Amendments on Common Stock Prices*, 11 J. FIN. ECON. 361 (1983) (identifying statistically significant, positive abnormal returns for supermajority amendments).

173. See, e.g., Griffin, *supra* note 91, at 740 (reporting a survey of investors and finding broad support for nonfinancial ends including environmental and social welfare).

174. *McRitchie v. Zuckerberg* held that fiduciary duties to shareholders in a Delaware corporation are firm-specific, seemingly rejecting portfolio primacy theory at the firm level for Delaware corporations. However, the intermediary case is arguably more compelling for portfolio primacy. Traditionally, shareholders that are not also controllers have wide discretion in their voting, and there is a reasonable argument that intermediaries should have discretion to maximize their investors’ overall portfolio. See *McRitchie v. Zuckerberg*, 315 A.3d 518, 526–27 (Del. Ch. 2024) (“The standard Delaware

approach).<sup>175</sup> Under such a framework, it is conceivable that intermediaries might support measures that reduce or even destroy value at one portfolio company in order to generate offsetting gains for their other holdings.<sup>176</sup> While this might be economically rational for their highly diversified investors, such behavior amplifies agency cost concerns: Not only would intermediaries have ample discretion to select their preferred route to wealth creation, they would have additional discretion to pursue wealth *destruction* under certain circumstances. In this way, the adoption of a portfolio primacy approach in the intermediary context would likely expand managerial discretion—and thus increase agency costs—by enabling a broader set of legally valid justifications for voting decisions.

A similar dynamic emerges under a “shareholder welfare” maximand.<sup>177</sup> Under such a framework, fiduciaries would be permitted, and potentially obligated, to advance a broader conception of investor welfare (rather than merely wealth), including both financial and nonfinancial interests of their investors. Under such a maximand, intermediaries would remain free to pursue various routes to wealth maximization, but they would also have discretion to pursue activities yielding other real or purported nonfinancial benefits. In this manner, a shareholder welfare maximand would serve to only increase intermediary discretion relative to the shareholder wealth maximand discussed in Section II.A above.

In sum, attempts to prescribe the ends of intermediary discretion do not—and likely cannot—limit intermediaries’ discretion and the attendant agency costs. Even the most stringent standard (wealth maximization) does not impose significant discipline on how intermediaries make stewardship decisions, given the subjectivity inherent in value maximization at the level of mass corporate governance. Embracing portfolio primacy or shareholder welfare maximization would presumably grant even greater discretion, permitting intermediaries to justify value destruction in addition to value creation. Consequently, attempts to legally dictate the “ends” that index funds must pursue are unlikely to limit governance discretion or to mitigate agency costs.

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formulation thus contemplates a single-firm model (or firm-specific model) in which directors of a corporation owe duties to the stockholders as investors in that corporation.”)

175. Roberto Tallarita, *The Limits of Portfolio Primacy*, 76 VAND. L. REV. 511, 527 (2023) (“Broadly diversified investors, such as the Big Three and other index fund managers, are interested in the performance of their entire portfolio rather than the performance of an individual company.”).

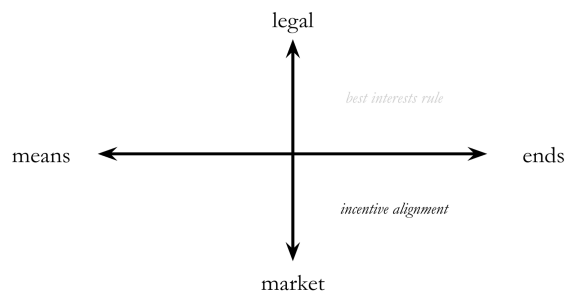
176. Rose, *supra* note 13, at 320 (“[F]inancially motivated diversified investors want to maximize the risk-adjusted value of their portfolio as a whole and are not independently concerned with the performance of any given portfolio firm.”).

177. See Oliver Hart & Luigi Zingales, *The New Corporate Governance*, 1 U. CHI. BUS. L. REV. 195, 197 (2022) (“When externalities are important and at least some investors are prosocial, we argue that shareholders will want companies to pursue *shareholder welfare maximization* (SWM) not SVM.”).

### III. MARKET CONSTRAINTS ON THE ENDS OF MASS CORPORATE GOVERNANCE

Another potential vector for limiting governance costs involves constraining the ends of governance through market forces. Broadly, strategies within this category aim to enforce fidelity to the principal's chosen ends through financial incentives and other market pressures, while granting agents discretion as to the means of achieving those ends. Figure X below situates such market-based, ends-focused solutions in the context of other governance cost reduction strategies.

FIGURE X. THEORETICAL BEHAVIORAL CONSTRAINTS ON INTERMEDIARIES: MARKET-ENDS



While the prior Part outlined the general failure of ends-focused legal rules to meaningfully constrain governance discretion by intermediaries,<sup>178</sup> one might be tempted to conclude that this is not necessarily problematic. After all, in the context of individual firms, the business judgment rule grants managers considerable discretion, and yet agency costs are more-or-less adequately controlled via other channels.<sup>179</sup> Unfortunately, as will be seen below, the mechanisms used to limit firm-level agency costs are largely absent in the intermediary context. Moreover, this problem is considerably compounded by the weak incentive alignment between intermediaries, as corporate entities, and their investors.

178. See *infra* Part II (discussing ends-based legal constraints on intermediaries' governance powers).

179. See Jonathan R. Macey, *Fraud in a Land of Plenty*, 118 NW. U. L. REV. 227, 230 (2023) ("The market forces that successfully discipline managers impose incentives on managers that feature both carrots and sticks. The carrots come in the form of high-powered executive compensation packages that reward executives for success at extraordinary levels. Executive compensation is highly correlated with firm performance, and executives at the helm of companies whose share prices perform receive incredibly rich payouts. The sticks come in the form of tenuous job security.").

### A. Individual Incentive Alignment

One key channel of agency cost reduction in the firm context is the structure of executive pay.<sup>180</sup> The basic goal is to reduce agency costs by aligning the incentives of firm managers, as agents, with shareholders, as principals.<sup>181</sup> There has been substantial research to this end spanning multiple decades—the type of pay,<sup>182</sup> how it is structured,<sup>183</sup> when it should vest,<sup>184</sup> if and when it should be clawed back,<sup>185</sup> and other such considerations.<sup>186</sup> Many law firms have whole practice groups focused on executive compensation,<sup>187</sup> public companies routinely hire executive compensation consultants to advise the board on executive pay packages,<sup>188</sup> and shareholders now have a legal right to voice their opinion on executive

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180. See Lucian Arye Bebchuk, Jesse M. Fried & David I. Walker, *Managerial Power and Rent Extraction in the Design of Executive Compensation*, 69 U. CHI. L. REV. 751, 757 (2002) (discussing the relationship between executive compensation structures, managerial incentives, and firm performance).

181. Macey, *supra* note 179, at 251 (“The benefits of performance-based executive compensation schemes are significant. They reduce agency costs, which are the costs associated with having actions taken by agents on behalf of principals, by serving to align the incentives of managers with the interests of shareholders.”).

182. James J. Park, *From Managers to Markets: Valuation and Shareholder Wealth Maximization*, 47 J. CORP. L. 435, 455 (2022) (“Over the 1960s and 1970s, executives were paid predominantly through fixed salaries. Because they did not own a significant percentage of their company’s stock, their economic fortunes did not significantly rise and fall with the wealth of shareholders. Rather than pay managers like bureaucrats, scholars like Jensen argued that they should be given the incentives of entrepreneurs by increasing their stock compensation. By the 1990s, close to half of the average CEO’s compensation was in the form of stock and options.”).

183. K.J. Martijn Cremers, Saura Masconale & Simone M. Sepe, *CEO Pay Redux*, 96 TEX. L. REV. 205, 242 (2017) (carefully examining the structure of equity-based executive compensation).

184. See, e.g., Zachary J. Gubler, *The Neoclassical View of Corporate Fiduciary Duty Law*, 91 U. CHI. L. REV. 165, 231 (2024) (“For example, in one well-known study, researchers found that on average, executive pay vests about 1.2 years after it is granted. This is a short period of time, particularly in light of the same study’s average CEO tenure of six years, which itself is short relative to the perspective of the hypothetical permanent shareholder.”).

185. See, e.g., Jesse Fried & Nitzan Shilon, *Excess-Pay Clawbacks*, 36 J. CORP. L. 721, 722 (2011) (“We explain why firms should have a clawback policy requiring directors to recover ‘excess pay’—extra payouts to executives resulting from errors in performance measures (such as reported earnings).”); David I. Walker, *The SEC’s Compensation Clawback Loophole*, 118 NW. U. L. REV. ONLINE 45, 65 (2023) (discussing the loophole in the SEC’s approach to compensation clawbacks).

186. See, e.g., Cremers et al., *supra* note 183, at 273 (discussing the relationship between board protection from market discipline and the overall efficiency of executive-compensation plans); Gubler, *supra* note 184, at 231–32 (discussing alternative executive compensation strategies focused upon long-term performance).

187. See, e.g., *Executive Compensation*, PAUL, WEISS, <https://www.paulweiss.com/practices/transactional/executive-compensation> [<https://perma.cc/7VCJ-GJQT>] (discussing the executive compensation practice group at one law firm).

188. Martin J. Conyon, *Executive Compensation Consultants and CEO Pay*, 64 VAND. L. REV. 399, 426 (2011) (providing a thorough overview of the use of executive compensation consultants and their relationship with CEO pay).

compensation in the form of “say on pay” votes.<sup>189</sup> In sum, corporate governance scholars and policymakers have put significant effort into reducing firm-level agency costs through carefully tailored incentives in executive pay.

Can the same be said for intermediary pay? For the largest and most influential intermediaries, the answer is unfortunately no. Consider the illustrative example of Larry Fink, chief executive and chairman of BlackRock, the world’s largest asset manager.<sup>190</sup> In his capacity as a BlackRock executive, Fink’s compensation appears by all accounts carefully crafted, with BlackRock’s proxy statement disclosing a three-page list of factors and formulas used in determining his annual compensation.<sup>191</sup> While one might not go so far as saying that BlackRock has “solved” agency costs for Larry Fink, it is clear there was a diligent and sophisticated effort to align his incentives with those of BlackRock shareholders. Part of that effort is that he in fact *is* a BlackRock shareholder.<sup>192</sup> Like most executives, Fink is paid largely in stock—the better to align his incentives.<sup>193</sup>

Of course, Larry Fink does not just influence how BlackRock operates. He also controls BlackRock’s stewardship activities, helping to direct how proxies are voted on behalf of investors in BlackRock’s many funds. For example, Fink personally conducts nearly 600 engagements with companies per year, and, through his own efforts and those of his subordinates, he influences how more or less every large public company governs itself.<sup>194</sup> In his capacity as a steward of the governance powers vested in him, how well-aligned are his financial incentives with those of his fund investors?

Comparing Fink’s incentive alignment with BlackRock shareholders to his incentive alignment with investors in BlackRock funds, it is clear that the latter is much less robust. Larry Fink’s personal incentive to promote his fund investors’ best interest is derivative of BlackRock’s. In turn, BlackRock’s overall financial incentive to promote value-enhancing governance policies that help its investors is, as discussed in detail below,

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189. Dorothy S. Lund, *Public Primacy in Corporate Law*, 47 SEATTLE U. L. REV. 365, 393 (2024) (“Dodd-Frank provided shareholders an advisory vote on executive compensation.”).

190. See *Larry Fink*, BLACKROCK, <https://www.blackrock.com/corporate/about-us/leadership/larry-fink> [<https://perma.cc/4N6P-A3DL>] (describing Larry Fink’s role with BlackRock).

191. BLACKROCK, 2023 PROXY STATEMENT 1, 68–70 (2023), [https://s24.q4cdn.com/856567660/files/doc\\_financials/2023/ar/blackrock-2023-proxy-statement\\_vf.pdf](https://s24.q4cdn.com/856567660/files/doc_financials/2023/ar/blackrock-2023-proxy-statement_vf.pdf) [<https://perma.cc/P9JQ-3YPW>].

192. See *BlackRock, Inc. Chairman and Chief Executive Officer Laurence D. Fink’s Pay Package for 2024*, SALARY.COM, <https://www1.salary.com/Laurence-D-Fink-Salary-Bonus-Stock-Options-for-BLACKROCK-INC.html> [<https://perma.cc/346K-3W2G>] (summarizing Larry Fink’s executive compensation package).

193. *Id.* (indicating that, in 2023, Larry Fink received a stock award worth \$16,449,974, out of annual total compensation of \$26,939,474, making his compensation over 61% stock).

194. BLACKROCK, *supra* note 191.

generally quite weak—less than one-sixth of one percent of the incremental increase in assets under management, and, even then, only such *portion* of the incremental increase that is due to governance policies.<sup>195</sup> It is difficult to quantify such an amount with any precision, even *ex post*, so the *ex ante* incentives for an asset manager like BlackRock, or for Larry Fink personally, are extraordinarily tenuous.

As a thought experiment, consider the implications if a company’s board of directors set executive compensation in the same fashion as a typical mutual fund or ETF at BlackRock (and other asset managers), utilizing an “assets under management” compensation model. The board agrees to pay the CEO, in cash, a few basis points on the firm’s overall market capitalization. How would such a compensation package be viewed in the inevitable derivative suits? Concededly, all else being equal, growing your firm’s market cap is good. Yet, as most scholars and policymakers will quickly realize, it also presents significant potential for abuse. For instance, this hypothetical CEO would face very strong financial incentives to engage in excessive mergers and acquisitions (“empire building”), even on terms that were highly unfavorable to existing shareholders.<sup>196</sup> This is due, in part, to the all-cash, single-metric nature of this compensation—the CEO is not compensated in the form of shares, nor is the compensation package otherwise tailored to align the CEO’s interests with those of the shareholders. Such a compensation structure would create, in essence, a “growth at all costs” mindset, while generating comparative indifference to overpayment, poor governance practices, or other mismanagement.<sup>197</sup> There would be comparatively weak incentives to invest in growing the firm through investments in “good governance,” when such gains are often marginal, sometimes slow, and frequently contested.<sup>198</sup> Ultimately, this compensation package would generate extremely weak incentive alignment between executives and shareholders. A board who adopted such a compensation policy would quickly find themselves inundated with

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195. See ZACHARY EVENS & BRIAN ARMOUR, MORNINGSTAR, 2023 US FUND FEE STUDY (2024) (listing BlackRock’s asset-weighted fees as 0.16% in 2023).

196. See Michal Barzuza & Eric Talley, *Long-Term Bias*, 2020 COLUM. BUS. L. REV. 104, 177 (“The common overinvestment theory of empire building posits that managers garner personal benefits from increasing the size and scope of their firms, which they achieve via investments and acquisitions.”).

197. See George W. Dent, Jr., *Corporate Governance: Still Broke, No Fix in Sight*, 31 J. CORP. L. 39, 47 (2005) (“An egregious aspect of this ‘empire building’ is unprofitable acquisitions: on average, purchasers realize no profit from acquisitions.”); Strine, *supra* note 94, at 1885 (“[A] short-term increase in productivity and stock price at the expense of long-term reinvestment and wage growth will likely harm the overall ‘portfolio’ of the human investor.”).

198. See Cremers et al., *supra* note 166, at 732–33 (discussing the relationship between incentive structures and the pursuit of long- vs. short-term financial value).

shareholder lawsuits,<sup>199</sup> and the incentive alignment the policy produces is so obviously poor that the board members who approved it might be liable for a non-exculpable violation of their fiduciary duty to act in good faith.<sup>200</sup>

And yet, this is the precise compensation structure of the mass corporate governors, who shape the governance practices of virtually all large public companies. The fact that it would not be tolerated as a method of controlling firm-level agency costs is reflective of the very different expectations and standards we have for firm-level agency costs and fund-level agency costs. At present, our controls for the agency costs imposed by financial intermediaries are simply less well-developed, less sophisticated, and less effective than our controls for firm-level agency costs. Ultimately, the fact that shareholders (and courts) would not allow agents with this compensation structure to manage even one public company suggests that the incentives it generates insufficiently mitigate agency costs. Thus, policymakers and scholars looking to constrain agency costs by intermediaries must look elsewhere in the search for an effective constraint.

### *B. Entity Incentive Alignment*

In theory, if the incentive alignment at the individual level is weak, but incentive alignment at the *entity level* is strong, the problem can be fixed with relative ease. For instance, such a fix might involve modest changes to an intermediary's compensation policy for executives or stewardship team members. However, if entity-level incentive alignment is *also* weak, a more complex, structural problem emerges, wherein "fixing" individual incentives may put them in conflict with the interests of the corporate entity. Thus, incentive alignment at the individual level is ultimately dependent on the incentives of the entity as a whole.

At a basic level, rational intermediaries are incentivized to invest in governance when it is cost-justified. That is, a given governance intervention must generate, on a present value basis, a return that justifies the costs of research and implementation. Whether a given governance intervention satisfies this standard is a function of numerous factors, including the magnitude of its holdings, the fees it charges to investors, and the likelihood that a given governance intervention is outcome-determinative (i.e., it causally determines firm-level governance outcomes).

More formally, it can be expressed as depicted in the following equation:

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199. See Lisa M. Fairfax, *Sue on Pay: Say on Pay's Impact on Directors' Fiduciary Duties*, 55 ARIZ. L. REV. 1, 51 (2013) (discussing the connection between directors' fiduciary duties and executive compensation structures).

200. See DEL. CODE ANN. tit. 8 § 102(b)(7) (West 2025).

EQUATION 1: FINANCIAL INCENTIVES OF INTERMEDIATED  
GOVERNANCE<sup>201</sup>

$$PV = [ (f \times AUM \times w \times g \times p_o \times p_v) \times (1 - e_{co}) ] / (r - g) - [ (c + SLR) ]$$

In the equation above  $f$  represents the intermediary's fees,  $AUM$  represents the intermediary's total equity assets under management,  $w$  represents the asset-weighted percentage a stock occupies in such intermediary's portfolio,  $g$  represents the governance-related change in value,  $p_o$  is the fractional likelihood that the intermediary's actions will be outcome-determinative,  $p_v$  represents firm-specific validity (i.e., the fractional likelihood that a given governance action or policy will, as implemented, have the predicted effect on stock price),  $e_{co}$  is the offsetting effects of cross-ownership of rival firms,  $c$  represents the costs of research, engagement, and voting, and  $SLR$  is the decline in share lending revenue due to recalling shares to vote. Those factors which require further explanation will be discussed in the Sections that follow.

For simplicity, this equation does not consider "flow incentives," whereby "an increase in the value of the portfolio can result in additional flows into the fund."<sup>202</sup> Such incentives are generally irrelevant with respect to indexed assets,<sup>203</sup> which make up nearly all of the public equity assets of the largest intermediaries (e.g., 90% at BlackRock).<sup>204</sup> It also excludes certain indirect governance consequences, such as the extent to which controversial governance interventions increase the probability of costly regulatory interventions<sup>205</sup> or politically motivated divestment campaigns.<sup>206</sup> Such factors likely increase the ultimate cost of governance

201. This equation is based in part on an equation by Brav et al., itself building on work by Lewellen and Lewellen. See Alon Brav, Andrey Malenko & Nadya Malenko, *Corporate Governance Implications of the Growth in Indexing*, in OXFORD RSCH. ENCYCLOPEDIA OF ECON. & FIN. (Anindya Banerjee ed., 2023); Jonathan Lewellen & Katharina Lewellen, *Institutional Investors and Corporate Governance: The Incentive to Be Engaged*, 77 J. FIN. 213 (2022).

202. See, e.g., Brav et al., *supra* note 201, at 4.

203. See *id.* at 11–12 (noting that flow incentives for "outperforming" a benchmark should be "close to zero" for index funds, but also discussing how raw returns could impact flows in a more indirect manner by influencing household savings rates and investment decisions).

204. See *Investment Stewardship: Stewardship at BlackRock*, BLACKROCK, <https://www.blackrock.com/corporate/insights/investment-stewardship> [<https://perma.cc/4GV3-W5EL>] (stating that, as of December 31, 2024, "[a]pproximately 90% of BlackRock clients' public equity assets under management are held in index equity strategies").

205. See, e.g., INDEX Act, S. 4241, 117th Cong. (2022) (an example of a legislative proposal that could have raised the costs of index fund stewardship and voting).

206. See, e.g., Richard Vanderford, *Texas Blacklists BlackRock, UBS and Other Financial Firms Over Alleged Energy Boycotts*, WALL ST. J. (Aug. 24, 2022), <https://www.wsj.com/articles/texas-black-lists-blackrock-ubs-and-other-financial-firms-over-alleged-energy-boycotts-11661381425> [<https://perma.cc/9H4L-W432>] (discussing Texas's "blacklisting" of certain financial companies for their ESG-related activities).

interventions, potentially significantly, thereby further attenuating any market incentives that may align the financial interests of intermediaries with those of their clients.

The Sections that follow theoretically and empirically analyze the key factors determining the financial incentives of intermediaries to engage in governance, ultimately providing estimates for intermediary financial incentives along a range of parameters.

### 1. *Portfolio Weight*

To be rational, the investment in informed voting must be cost-justified on an asset-weighted basis. In particular, for the ubiquitous market-weighted fund strategy, where the top equity holdings are several orders of magnitude larger than the bottom, there may be only a minority of companies where the asset manager's holdings are significant enough to plausibly incentivize investment in governance.

Consider Walgreens,<sup>207</sup> near the bottom of the S&P 500 (currently ranked 485). In a market-weighted S&P 500 portfolio, it would carry a relative weight of a bit over 0.01%. If an asset manager has one trillion dollars in funds tracking the S&P 500, it will own roughly \$100 million of Walgreens equity.

In contrast, consider Bank of America, currently within the top twenty-five largest companies in the S&P 500.<sup>208</sup> In a market-weighted S&P 500 portfolio, it will carry a relative weight of approximately 0.62%.<sup>209</sup> If an asset manager has one trillion dollars in funds tracking the S&P 500, it will own roughly \$6.2 billion of Bank of America's equity.

Obviously, greater portfolio weight correlates with more robust financial incentives. An intermediary has much stronger incentives to engage in informed governance with respect to a firm representing 1% of its portfolio than one representing 0.01% (or less still, 0.00001%).<sup>210</sup> Thus, relative

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207. The corporate entity is named Walgreens Boots Alliance, Inc., subsequent to its 2014 merger with European pharmacy company Alliance Boots GmbH. See Angela Chen, *Walgreen Shareholders Approve Alliance Boots Deal*, WALL ST. J. (Dec. 29, 2014), <https://www.wsj.com/articles/walgreen-shareholders-approve-alliance-boots-deal-1419864933> [<https://perma.cc/PM6W-YN9W>].

208. See *VFLAX: Vanguard 500 Index Fund Admiral Shares*, VANGUARD, <https://investor.vanguard.com/investment-products/mutual-funds/profile/vfiax#portfolio-composition> [<https://perma.cc/29XJ-G3R2>] (listing portfolio constituents by weight under the "Portfolio composition" heading).

209. See *id.* (obtained by dividing the market value of the fund's holdings in Bank of America by the total assets of the fund).

210. This is the approximate weight of Wag! Group Co., makers of a dog walking app that has been called the "Uber for dogs." See Dante Ramos, Opinion, *Can 'Uber for Dogs' Overcome the Fear of Strangers?*, BOS. GLOBE (July 13, 2018), <https://www.bostonglobe.com/opinion/2018/07/13/can-uber-for-dogs-overcome-fear-strangers/sd7ojO1ZrVs5iITTvblkPL/story.html> [<https://perma.cc/RCZ3-4NF6>].

portfolio weight is a key determinant for the governance incentives of intermediaries.

## 2. Fees

Intermediaries charge fees that can vary significantly. All else being equal, doubling the fees charged by a given intermediary will also double such intermediary's financial incentives to engage in informed governance. Thus, although low fees are generally better for investors in all other respects, higher fees could potentially incentivize more involved governance. Although the average management fee for a mutual fund is currently 0.36%,<sup>211</sup> many of the largest asset managers have significantly lower management fees. For instance, Vanguard's average asset-weighted management fee is 0.08%, while the average asset-weighted management fee is 0.16% for BlackRock's iShares funds, 0.14% for State Street's SPDR funds, and 0.27% for Fidelity Investments.<sup>212</sup>

## 3. Financial Impact

What is the impact of a given governance intervention? The answers to this question vary (likely dramatically) based on the precise characteristics of the intervention (e.g., voting for an incumbent director vs. initiating a proxy contest), the characteristics of the individual or entity initiating the governance intervention, as well as the unique characteristics of the firm subject to such intervention.

One meta-analysis finds that the valuation effects of shareholder proposals are roughly 0.06%, direct negotiations with managers are 0.26%, hedge fund activism is 4.97%, proxy fights are 6.77%, and takeovers are 15.33%.<sup>213</sup> Thus, both the characteristics of the individual or institution initiating a governance intervention, as well as the *type* of governance intervention, can dramatically affect its expected financial impact. In contrast, a newer meta-analysis finds no statistically significant evidence of a differential price response to *any type* of shareholder activism other than

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211. *How Fund Fees Are Evolving in the US*, MORNINGSTAR (July 16, 2024), <https://www.morningstar.com/business/insights/blog/funds/us-fund-fee-study> [<https://perma.cc/JC3Z-6DN9>].

212. EVENS & ARMOUR, *supra* note 195, at 31.

213. Matthew R. Denes, Jonathan M. Karpoff & Victoria B. McWilliams, *Thirty Years of Shareholder Activism: A Survey of Empirical Research*, 44 J. CORP. FIN. 405, 407 (2017). *But see* K.J. Martijn Cremers, Erasmo Giambona, Simone M. Sepe & Ye Wang, *Hedge Fund Activism and Long-Term Firm Value* 41 (Dec. 13, 2018), <https://ssrn.com/abstract=2693231> [<https://perma.cc/6HRG-HJXD>] (unpublished manuscript) (suggesting that abnormal returns to hedge fund activism are driven by selection effects and that non-targeted firms with similar valuations actually experience greater increases relative to targeted firms).

activism that attempts to make a firm a takeover target and, to a much lesser extent, activism that seeks board representation.<sup>214</sup>

The estimated financial impact of various interventions exhibits significant heterogeneity, with most interventions unrelated to takeover activity having a relatively modest price impact. Moreover, it is likely that these estimates, which are focused specifically on activist interventions, significantly overstate the impact of the average, non-activist governance items. Because activists will rationally pick higher-impact issues and targets, other governance items will, all else being equal, generate a lesser financial impact. More broadly, to the extent that returns to governance items are driven by removing takeover protections and/or otherwise increasing the likelihood of takeover, such returns are less broadly replicable today due to successful campaigns to remove such protections at large companies.<sup>215</sup>

#### 4. Outcome Determinacy

An intermediary's governance investment is not guaranteed to pay off. One reason is that an attempted governance intervention may fail—e.g., a shareholder proposal may not pass, or a director candidate may be elected despite an intermediary's opposition. If a vote would pass anyway without a governance investment, a rational intermediary would not expend resources on such a vote. Conversely, a rational intermediary will also not expend resources on a "lost cause" that is guaranteed not to pass. As a result, rational intermediaries only possess financial incentives to invest in governance when their investment is sufficiently likely to *do something*—namely, when it is likely to shift the outcome on a given governance issue. For small investors, the likelihood that their vote is outcome-determinative (i.e., pivotal) approaches zero. However, for the largest funds, the fractional likelihood that their votes are outcome-determinative can be significant. One scholar estimated the ability of the Big Three intermediaries to shift voting outcomes, finding that approximately 19.6% of all shareholder proposals fell within the marginal voting control of the largest member of the Big Three (Vanguard).<sup>216</sup> Thus, a useful upper bound for an asset manager's average ability to determine voting outcomes is roughly 20% for

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214. See Josef Bajzik, Tomas Havranek, Zuzana Irsova & Jiri Novak, *Does Shareholder Activism Create Value? A Meta-Analysis*, 33 CORP. GOVERNANCE: AN INT'L REV. 1039, 1053 (2025) ("Thus, our multivariate analysis does not identify significant differences in price responses to shareholder activism pursuing objectives other than company sales and greater board representation.").

215. See, e.g., Kastiel & Nili, *supra* note 110, at 827 (noting that the proportion of S&P 500 companies with staggered boards has decreased from 60% in 2000 to 11% in 2020).

216. See Griffin, *supra* note 76, at 438 tbl.15.

the largest asset manager, with corresponding decreases for smaller asset managers.<sup>217</sup>

### 5. *Firm-Specific Validity*

Another reason that an intermediary's investment in governance is not guaranteed to pay off relates to the firm-specific validity of general corporate governance concepts. More precisely, firm-specific validity refers to the fractional likelihood that a given governance action or policy will, as implemented, have the predicted effect on the specific firm's stock price. Human beings are imperfect, and stewardship team members and corporate governance researchers are no exception. This, along with the indeterminacy of various areas of corporate governance research, makes the estimated impact of various policies difficult to predict, even in the aggregate, and particularly for a given ballot item at a given firm. Moreover, predicting stock market price impact is notoriously difficult, and it is not clear that most intermediaries, particularly the largest passive asset managers, possess (or even claim) any expertise in this area.

### 6. *Common Ownership*

Common ownership may also attenuate any gains resulting from a governance intervention. Actions that benefit a given firm may harm its competitors, and vice versa. Because large intermediaries possess ownership stakes in numerous firms that compete within the same industry, such effects can be considerable. For instance, if a given action benefits a firm *at the expense of its competitors* (e.g., by lowering the firm's costs, allowing it to lower prices and capture market share from its rivals), then any gains to the firm's stock price will be attenuated by losses to the stock prices of its rivals. One study calculates that common ownership effects can reduce the benefits of such actions by 73% for the largest asset managers.<sup>218</sup> Thus, particularly for large asset managers, some expected gains from

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217. See *id.* at 418 tbl.1 (estimating the mean percentage of votes cast by the Big Three as 10.6%, 9.0%, and 5.4% for Vanguard, BlackRock, and State Street, respectively).

218. See Lewellen & Lewellen, *supra* note 201, at 217 ("To put the numbers in perspective, consider a corporate action that would increase the value of a firm at the expense of industry rivals, one-for-one (for example, a move that allows the firm to take market share away from its rivals). Our estimates suggest that institutions' ownership of multiple firms in an industry makes this strategy about 30% less valuable for most institutional shareholders than it otherwise would be and 73% less valuable for the five large indexers, for which common ownership is more important.").

governance will need to be reduced to account for the effects of common ownership.<sup>219</sup>

### 7. Cost

Of course, the benefits of a given governance issue must be weighed against the costs of researching and voting on the issue. Brav, Malenko, and Malenko break the costs that intermediaries incur with respect to governance into three categories: “costs of information,” which consist of collecting and analyzing information, “direct costs of engagement,” such as preparing and filing a Schedule 13G or 13D or developing proxy voting guidelines, and “indirect costs of engagement,” which might include political backlash or the impact of challenging management on 401(k) revenues at the challenged firms.

The empirical evidence on the costs intermediaries incur in governance is quite limited.<sup>220</sup> Perhaps the best estimate comes from a 2019 study by Lucian Bebchuk and Scott Hirst, where they calculated stewardship costs for large asset managers at slightly less than 0.2% of fees they collected.<sup>221</sup> There is some evidence that stewardship spending may have increased subsequent to their article’s publication. For instance, since 2019, BlackRock’s stewardship team has increased its personnel by approximately 56%, going from forty-five<sup>222</sup> to seventy<sup>223</sup> members, and Vanguard’s stewardship team has roughly doubled from twenty-one<sup>224</sup> to forty<sup>225</sup> or more.

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219. While some researchers also discuss potential gains from adopting certain policies in the context of common ownership (e.g., policies that benefit an industry at the expense of consumers), such policies with industry-wide effects are generally distinct from the *internal corporate governance policies* with respect to which intermediaries may engage in proxy voting. See, e.g., Lewellen & Lewellen, *supra* note 201, at 219 (discussing the financial impact of policies that benefit a given industry).

220. Brav et al., *supra* note 201 (“The evidence on the magnitude of engagement costs is scarce: estimating these costs is difficult because they are not typically observed, especially the costs of time, effort, or costs related to reputation.”).

221. Lucian Bebchuk & Scott Hirst, *Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy*, 119 COLUM. L. REV. 2029 (2019). To the extent stewardship teams have grown since Bebchuk and Hirst’s article was published, such costs are likely understated.

222. *Id.*

223. See Angel Au-Yeung, *The 70 BlackRock Analysts Who Speak for Millions of Shareholders*, WALL ST. J. (June 18, 2022), <https://www.wsj.com/articles/the-70-blackrock-analysts-who-speak-for-millions-of-shareholders-11655517497> [<https://perma.cc/C23X-L787>].

224. Bebchuk & Hirst, *supra* note 221, at 2077.

225. See VANGUARD, INVESTMENT STEWARDSHIP 3 (2021), <https://www.nl.vanguard/content/dam/intl/europe/documents/en/investment-stewardship-about-our-programme.pdf> [<https://perma.cc/U39B-K2YN>] (“Over the past 20 years, our investment stewardship efforts have expanded from a small group focused on guideline-driven voting to a global team of more than 40 multidisciplinary analysts, located in the US and the UK.”).

This Article adopts Bebchuk and Hirst's estimate while acknowledging that, to the extent stewardship team headcounts or overall stewardship expenses have outpaced growth in assets under management, it may underestimate the cost of stewardship. Additionally, although Bebchuk and Hirst acknowledge indirect costs, their quantitative estimates appear to focus primarily on direct expenses. As a result, the presence of the types of indirect expenses (e.g., reputational costs, loss of 401(k) plan revenue, or political and consumer backlash) discussed above will further reduce the incentive of fiduciaries to invest in governance and cause the estimates below to understate overall costs.

#### 8. *Share Lending Revenue*

Large asset managers generate a portion of their revenue through share lending. This revenue stream may be particularly significant for funds that charge low or zero fees.<sup>226</sup> However, engaging in shareholder voting interrupts this revenue stream, as voting such shares requires recalling them prior to the vote.<sup>227</sup> The result is that intermediaries face an important opportunity cost when deciding whether to engage in proxy voting—foregone share lending revenue, which must be weighed against the financial benefits of voting. Moreover, the revenue from share lending is relatively certain, while the revenue an intermediary expects to receive from proxy voting is typically uncertain, leading risk-averse intermediaries to potentially favor lending revenues over those derived from investments in governance.

Vanguard estimates share average lending revenues of 400 to 500 basis points per dollar loaned.<sup>228</sup> However, not all shares are loaned out at all times, and the average *realized* annual impact is generally between one and five basis points.<sup>229</sup> This analysis assumes an average return of three basis

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226. See Todd Shriber, *Fidelity Adds to Zero-Fee Fund Suite*, INVESTOPEDIA (Sept. 13, 2018), <https://www.investopedia.com/news/fidelity-adds-zero-fee-fund-suite/> [<https://perma.cc/DHQ8-5QWH>] (discussing the launch of “no-fee index funds” by Fidelity).

227. See Reena Aggarwal, Pedro A.C. Saffi & Jason Sturgess, *The Role of Institutional Investors in Voting: Evidence from the Securities Lending Market*, 70 J. FIN. 2309, 2314 (2015) (“Although lenders refer to these shares as being ‘on loan,’ the lender actually transfers ownership and voting rights.”).

228. See Erich Pingel, *The Value of Securities Lending in Three Charts*, VANGUARD (June 11, 2024), [<https://web.archive.org/web/20240618132112/https://corporate.vanguard.com/content/corporate/us/en/corp/articles/value-securities-lending-three-charts.html>] (only available by archived link) (“Vanguard funds and ETFs have generated income of between roughly 400 and 500 basis points per dollar on loan on average.”).

229. See *id.* (“For Vanguard funds and ETFs, securities lending income has added between roughly 1 and 5 basis points to annual returns on average, depending on the market capitalization category.”).

points and a restriction of share lending for a period of two weeks leading to the record date.<sup>230</sup> This may underestimate the applicable rate,<sup>231</sup> as borrowing demand and borrowing fees generally increase in connection with the record date.<sup>232</sup>

### 9. *Synthesis*

This Section synthesizes the foregoing into a series of hypothetical voting decisions. It first considers Walgreens as an example of a “mid-cap”<sup>233</sup> company, and then subsequently considers the same voting decisions at a “large-cap”<sup>234</sup> company (United Airlines) as well as a “mega-cap”<sup>235</sup> company (Bank of America).<sup>236</sup> This synthesis first examines hypothetical decisions by Vanguard, the largest of the Big Three by equity assets, with an asset-weighted average fee of 0.08%<sup>237</sup> and equity assets under management of approximately \$7.38 trillion.<sup>238</sup>

Walgreens has a weight in Vanguard’s portfolio of approximately 0.01%, consistent with its weight within the S&P 500.<sup>239</sup> Assume Vanguard is contemplating how to vote on a shareholder proposal with a valuation impact equivalent to the average shareholder proposal in the meta-analysis

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230. See Aggarwal et al., *supra* note 227, at 2316 (“The results suggest that institutions start restricting supply in advance of the proxy record date to ensure that shares can be recalled and that they can exercise the vote. In practice, institutions are generally advised to allow two weeks for a recall prior to a proxy vote, and possibly longer if the firm is ‘special’. Consistent with industry practice, we find that the drop in lendable supply starts to occur about two weeks before the record.”).

231. Indeed, repeating these calculations using estimated voting values (“VVOTE”) from Aggarwal, Saffi, and Sturgess generally yields comparable, but somewhat larger, values.

232. See Aggarwal et al., *supra* note 227, at 2316 (“We find a marked reduction in the lendable supply prior to the proxy record date and an increase in borrowing demand and the borrowing fee around the record date.”).

233. See *Market Cap Explained*, FINRA (Sept. 30, 2022), <https://www.finra.org/investors/insights/market-cap> [<https://perma.cc/V5JF-C4PE>] (defining a “mid-cap” company as one with a “market value between \$2 billion and \$10 billion”).

234. See *id.* (defining a “large-cap” company as one with a “market value between \$10 billion and \$200 billion”).

235. See *id.* (defining a “mega-cap” company as one with a “market value of \$200 billion or more”).

236. Although Walgreens is considered a “mid-cap” company in this example, it is in fact among the largest 15% of all companies in a “total stock market” index. See, e.g., *VTSAX: Vanguard Total Stock Market Index Fund Admiral Shares*, VANGUARD, <https://investor.vanguard.com/investment-products/mutual-funds/profile/vtsax#portfolio-composition> [<https://perma.cc/5E25-54YG>].

237. EVENS & ARMOUR, *supra* note 195, at 1, 31.

238. *Id.* The tables below include calculations for other large asset managers, including BlackRock, State Street, and Fidelity. See *infra* Tables 1 and 2.

239. Because Vanguard holds significant assets not included in the S&P 500, this estimate overstates Walgreens’s true weight within Vanguard’s portfolio.

discussed above (0.06%).<sup>240</sup> Per the research cited above, we assign Vanguard the ability to determine voting outcomes roughly 20% of the time,<sup>241</sup> and we charitably assume its stewardship team is able to determine the firm-specific share price impact with 100% accuracy.<sup>242</sup> With respect to common ownership, Vanguard is the largest of the “five large indexers” discussed in Denes et al.,<sup>243</sup> and the pharmacy industry is relatively concentrated,<sup>244</sup> so we accept the authors’ figure (estimating a 73% reduction in benefits due to common ownership effects for the five largest common owners) as applicable here.<sup>245</sup> Accepting Bebchuk and Hirst’s estimate for costs (approximately 0.2% of fees collected), a proportional amount of stewardship spending would equal roughly \$1,200.<sup>246</sup> For simplicity, assume that researching and voting on this shareholder proposal constituted 10% of Vanguard’s governance expenditures related to Walgreens (\$120).<sup>247</sup> Finally, as described above, this analysis assumes an

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240. Denes et al., *supra* note 213, at 407; *see also* Randall S. Thomas & James F. Cotter, *Shareholder Proposals in the New Millennium: Shareholder Support, Board Response, and Market Reaction*, 13 J. CORP. FIN. 368, 389 (2007) (finding that the “cumulative abnormal return was 0.16%” around the meeting date for their full sample of shareholder proposals and sponsors, and ultimately concluding that the “market reaction to shareholder proposals” was “consistent with earlier studies . . . generally insignificant”).

241. *See* Griffin, *supra* note 76, *passim* (estimating that Vanguard can influence the voting outcome for 19.6% of all shareholder proposals).

242. This obviously overstates the accuracy of the stewardship team’s predictions; even active fund managers, with dramatically higher financial incentives to predict such price movements, struggle to do so. *See* Jeff Sommer, *With the Odds on Their Side, They Still Couldn’t Beat the Market*, N.Y. TIMES (Apr. 14, 2023), <https://www.nytimes.com/2023/04/14/business/stock-market-2022.html> [<https://perma.cc/S28K-MQL8>] (noting that, “[o]ver 20 years, 94.8 percent [of actively managed funds] underperformed” the S&P 500).

243. Denes et al., *supra* note 213, at 407 (“Our estimates suggest that institutions’ ownership of multiple firms in an industry makes this strategy 30% less valuable for most institutional shareholders than it otherwise would be, and 73% less valuable for the five large indexers, for which common ownership is more important.”).

244. This is particularly true within certain geographic areas. *See, e.g.*, KOSALI SIMON, MARION GREENE & SUMEDHA GUPTA, *STUDY OF PHARMACY MARKET CONCENTRATION IN INDIANA BY INDUSTRY* (2022) (studying the market concentration of various metropolitan statistical areas in Indiana and finding Herfindahl–Hirschman Index (HHI) measures as high as 7881.24). For reference, the U.S. Department of Justice and the Federal Trade Commission generally refer to markets with an HHI above 1,800 as “highly concentrated.” *See* U.S. DEP’T OF JUSTICE & FED. TRADE COMM’N, *MERGER GUIDELINES* (2023) (stating that the DOJ and FTC generally consider markets with “HHI above 1,000 as concentrated markets, with HHI between 1,000 and 1,800 as ‘moderately concentrated’ and above 1,800 as ‘highly concentrated’”).

245. *See* Lewellen & Lewellen, *supra* note 201, at 217.

246. Bebchuk & Hirst, *supra* note 221. To the extent stewardship teams have grown since Bebchuk and Hirst’s article was published, such costs may be understated.

247. In the tables below, it is assumed that each shareholder proposal consumes 10% of both direct and indirect governance expenditures, direct negotiations consume 20% of such expenditures, an abstract governance improvement that increases firm market value by one percent consumes 50% of such expenditures, and the comparatively high-impact governance items (i.e., hedge fund activism,

average return of three basis points and a restriction of share lending for a period of two weeks leading to the record date.<sup>248</sup> For the given parameters, the foregone share lending revenue is equal to roughly \$8,515,<sup>249</sup> of which 10% is allocated to voting on this shareholder proposal (\$851.54).<sup>250</sup>

Filling this into the equation above and assuming, for simplicity, a 10% discount rate ( $r$ ) and a growth rate ( $g$ ) equivalent to the rate of inflation, then

$$PV = [ (f \times AUM \times w \times g \times p_o \times p_v) \times (1 - e_{co}) / (r - g) ] - [ (c + SLR) ]$$

becomes

$$PV = [ (.08\% \times \$7.38 \text{ trillion} \times .01\% \times .06\% \times 20\% \times 100\%) \times (1 - .73) / (10\% - 0\%) ] - [ (\$120 + \$851.54) ].$$

The net result is approximately -\$780.25. Thus, researching and voting on this shareholder proposal would produce a monetary loss to Vanguard, and it faces modest financial disincentives to engage in such governance activity. The table on the next page provides results for other estimated governance actions.

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proxy contests, and takeovers) each consume 100% of such expenditures. Thus, the highest-value governance items are allocated the full cost of direct and indirect governance expenditures. In such scenarios (e.g., an activist campaign or merger vote), limited governance resources will be invested in unrelated governance items. In contrast, comparatively low-value governance items are allocated a lower percentage of direct and indirect governance expenditures.

248. See Aggarwal et al., *supra* note 227, at 2316 (“The results suggest that institutions start restricting supply in advance of the proxy record date to ensure that shares can be recalled and that they can exercise the vote. In practice, institutions are generally advised to allow two weeks for a recall prior to a proxy vote, and possibly longer if the firm is ‘special’. Consistent with industry practice, we find that the drop in lendable supply starts to occur about two weeks before the record.”).

249. Walgreens has a weight of approximately 0.01% in Vanguard’s roughly \$7,380,000,000,000 portfolio, equating to an ownership interest of roughly \$738,000,000. Three basis points (0.03%) of this ownership interest are \$221,400, multiplied by 2/52 (for a two-week loan) equals approximately \$8,515.

250. This analysis allocates the opportunity cost of foregone share lending for each distinct ballot item in the same proportion as direct stewardship expenditures, discussed above. However, unlike certain other governance costs (e.g., time allocated to research a given ballot item), recalling shares for voting presents intermediaries with a binary choice (recall/not recall) that necessitates incurring the entire cost to vote on even a single ballot item. For instance, although a shareholder proposal is allocated only 10% of the opportunity cost of foregone share lending revenue, if other ballot items are not valuable enough to justify the remaining 90%, these calculations will understate the cost of voting on such a proposal.

TABLE 1: ESTIMATED FINANCIAL INCENTIVES—LOW S&amp;P 500

*This table provides estimates of realized profits for various governance actions. It uses the equation above to estimate profits for shareholder proposals, direct negotiations,<sup>251</sup> a one-percent abstract governance improvement for consistency with prior literature,<sup>252</sup> hedge fund activism, proxy contests, and takeovers from the perspective of large intermediaries invested in a mid-cap<sup>253</sup> company—Walgreens, with a market capitalization of approximately \$9 billion. The analysis assumes that the valuation impact is permanent and that increased fees are received in perpetuity. It assumes that all equity assets at Vanguard,<sup>254</sup> BlackRock,<sup>255</sup> State Street,<sup>256</sup> and Fidelity<sup>257</sup> are proportionately and exclusively invested in the S&P 500.<sup>258</sup> Altering these assumptions would reduce the estimated profitability.*

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251. These calculations assume that intermediaries engaging in “direct negotiations” in the table above also subsequently vote their shares. If, instead, no subsequent voting is conducted (or an agreed settlement is reached), then fewer or no shares may be recalled for the purpose of voting, leaving greater share lending revenues intact. Because a reduction in share lending revenue can be a significant cost, this governance intervention is, all else being equal, preferable to the intermediary. This dynamic may inform the “engagement first” strategy of the Big Three intermediaries that prioritizes the informal exercise of governance power via private engagements. See Caleb N. Griffin, *Environmental & Social Voting at Index Funds*, 44 DEL. J. CORP. L. 167, 186 (2020) (“Vanguard describes its approach to stewardship as ‘quiet diplomacy.’ Likewise, State Street indicates that it resorts to voting action when companies fail to respond to its engagement efforts. For its part, BlackRock refers to its approach to stewardship as an ‘engagement-first’ approach.”).

252. See, e.g., Lewellen & Lewellen, *supra* note 201, at 213–264; see also Brav et al., *supra* note 201, at 4.

253. See *Market Cap Explained*, *supra* note 233.

254. Morningstar estimates Vanguard’s total equity assets under management (AUM) as \$7.383 trillion. See, EVENS & ARMOUR, *supra* note 195, at 31.

255. BlackRock lists its total AUM as \$11.6 trillion, 55% of which are equity assets. See Press Release, BlackRock, BlackRock Reports Full Year 2024 Diluted EPS of \$42.01, or \$43.61 as Adjusted; Fourth Quarter 2024 Diluted EPS of \$10.63, or \$11.93 as Adjusted at 1 (Jan. 15, 2025), [https://s24.q4cdn.com/856567660/files/doc\\_financials/2024/Q4/BLK-4Q24-Earning-Release.pdf](https://s24.q4cdn.com/856567660/files/doc_financials/2024/Q4/BLK-4Q24-Earning-Release.pdf) [<https://perma.cc/ZCL6-58ZC>].

256. State Street lists its equity assets under management as \$3.007 trillion as of December 31, 2024. See Press Release, State Street, State Street Reports Fourth Quarter 2024 EPS of \$2.45; \$2.60 Excluding Notable Items at 6 (Jan. 17, 2025), [https://s203.q4cdn.com/888565246/files/doc\\_financials/2024/q4/STT-4Q24-Earnings-Press-Release-vFinal.pdf](https://s203.q4cdn.com/888565246/files/doc_financials/2024/q4/STT-4Q24-Earnings-Press-Release-vFinal.pdf) [<https://perma.cc/WR8U-TDYK>].

257. Fidelity lists its equity assets as \$3.5 trillion as of September 30, 2024. See *Fidelity by the Numbers: Asset Management*, FIDELITY (Sept. 30, 2024), [<https://web.archive.org/web/20241127231236/https://www.fidelity.com/about-fidelity/our-company/asset-management>] (only available by archived link).

258. In reality, these intermediaries own numerous stocks outside of S&P 500 firms. To the extent this overstates the portion of an intermediary’s equity investment in S&P 500 firms, the tables herein will overstate the intermediary’s governance incentives.

<b>Governance Type</b>	Impact	BlackRock	Vanguard	State Street	Fidelity
<i>Shareholder Proposal</i>	0.06%	-\$610	-\$780	-\$295	-\$287
<i>Direct Negotiations</i>	0.26%	-\$447	\$1,110	-\$271	\$141
<i>Abstract Improvement</i>	1.00%	\$811	-\$1,660	\$118	\$2,139
<i>Hedge Fund Activism</i>	4.97%	\$17,993	\$6,149	\$6,987	\$19,433
<i>Proxy Contest</i>	6.77%	\$27,915	\$11,888	\$11,079	\$28,619
<i>Takeover</i>	15.31%	\$74,990	\$39,115	\$30,493	\$72,198

As Table 1 portrays, the profitability of intermediary investments in governance at mid-size firms is generally modest or negative, even for the largest intermediaries. The relative value of such firms in a market-weighted portfolio is simply not large enough to justify significant governance outlays for any but the most dramatic governance interventions (such as proxy contests and takeovers).

TABLE 2: ESTIMATED FINANCIAL INCENTIVES—MID S&amp;P 500

*This table provides estimates of realized profits for various governance actions. It uses the equation above to estimate profits for shareholder proposals, direct negotiations, a one-percent abstract governance improvement for consistency with prior literature, hedge fund activism, proxy contests, and takeovers from the perspective of large intermediaries invested in a large-cap company—United Airlines Holdings, Inc., with a market capitalization of approximately \$33.7 billion. The analysis assumes that the valuation impact is permanent and that increased fees are received in perpetuity. It assumes that all equity assets at Vanguard, BlackRock, State Street, and Fidelity are proportionately and exclusively invested in the S&P 500. Altering these assumptions would reduce the estimated profitability.*

<b>Governance Type</b>	<b>Impact</b>	<b>BlackRock</b>	<b>Vanguard</b>	<b>State Street</b>	<b>Fidelity</b>
<i>Shareholder Proposal</i>	0.06%	-\$4,267	-\$5,448	-\$2,063	-\$2,007
<i>Direct Negotiations</i>	0.26%	-\$3,132	-\$7,772	-\$1,899	\$988
<i>Abstract Improvement</i>	1.00%	\$5,675	-\$11,620	\$823	\$14,971
<i>Hedge Fund Activism</i>	4.97%	\$125,952	\$43,043	\$48,907	\$136,034
<i>Proxy Contest</i>	6.77%	\$195,407	\$83,214	\$77,550	\$200,332
<i>Takeover</i>	15.31%	\$524,933	\$273,802	\$213,448	\$505,389

However, perhaps larger firms fare better. It is reasonable to hypothesize that a firm with a higher market capitalization in a market-weighted portfolio would generate greater financial incentives to invest in good governance. Thus, moving from one of the smallest firms in the S&P 500 (Walgreens) to a large-cap firm (United Airlines) and a mega-cap firm (Bank of America) will produce a distinct set of financial incentives. Applying the foregoing equation to intermediaries' relative investments in United Airlines and Bank of America yields the results in Table 2 (above) and Table 3 (below), respectively.

TABLE 3: ESTIMATED FINANCIAL INCENTIVES—HIGH S&amp;P 500

*This table provides estimates of realized profits for various governance actions. It uses the equation above to estimate profits for shareholder proposals, direct negotiations,<sup>259</sup> a one-percent abstract governance improvement for consistency with prior literature, hedge fund activism, proxy contests, and takeovers from the perspective of large intermediaries invested in a mega-cap company—Bank of America, with a market capitalization of approximately \$365 billion. The analysis assumes that the valuation impact is permanent and that increased fees are received in perpetuity. It assumes that all equity assets at Vanguard, BlackRock, State Street, and Fidelity are proportionately and exclusively invested in the S&P 500. Altering these assumptions would reduce the estimated profitability.*

<b>Governance Type</b>	<b>Impact</b>	<b>BlackRock</b>	<b>Vanguard</b>	<b>State Street</b>	<b>Fidelity</b>
<i>Shareholder Proposal</i>	0.06%	-\$37,794	-\$48,256	-\$18,275	-\$17,773
<i>Direct Negotiations</i>	0.26%	-\$27,740	-\$68,840	-\$16,818	\$8,747
<i>Abstract Improvement</i>	1.00%	\$50,267	-\$102,916	-\$7,285	\$132,604
<i>Hedge Fund Activism</i>	4.97%	\$1,115,572	\$381,236	-\$433,175	\$1,204,874
<i>Proxy Contest</i>	6.77%	\$1,730,747	\$737,035	\$686,874	\$1,774,369
<i>Takeover</i>	15.31%	\$4,649,410	\$2,425,102	\$1,890,537	\$4,476,305

As Tables 2 and 3 demonstrate, the hypothesis that larger firms generate stronger financial incentives is only partially correct. While the potential benefits are indeed much higher, so too are the costs. The primary issue is that both benefits *and certain costs* scale with firm size and portfolio

259. These calculations assume that intermediaries engaging in “direct negotiations” in the table above also subsequently vote their shares. If, instead, no subsequent voting is conducted (or an agreed settlement is reached), then fewer or no shares may be recalled for the purpose of voting, leaving greater share lending revenues intact. Because a reduction in share lending revenue can be a significant cost, this governance intervention is, all else being equal, preferable to the intermediary. This dynamic may inform the “engagement first” strategy of the Big Three intermediaries that prioritizes the informal exercise of governance power via private engagements. See Griffin, *supra* note 251, at 186 (“Vanguard describes its approach to stewardship as ‘quiet diplomacy.’ Likewise, State Street indicates that it resorts to voting action when companies fail to respond to its engagement efforts. For its part, BlackRock refers to its approach to stewardship as an ‘engagement-first’ approach.”).

weight.<sup>260</sup> First, foregoing share lending revenues for a greater amount of equity generally produces a greater opportunity cost. As a consequence, recalling a larger value of shares for voting likely entails sacrificing greater share lending revenue. Second, stewardship expenses also scale with firm size and portfolio weight. Generally speaking, it is rational for intermediaries to make greater governance investments for holdings that are proportionately larger. This calculation uses Bebchuk and Hirst's estimate of stewardship expenses at 0.2% of fees collected, which will naturally produce a greater absolute value for larger firms.<sup>261</sup> Thus, investing in governance research and recalling shares to vote on low-impact topics at large firms may actually be less profitable than doing so at small firms. The counterintuitive result is that firm size is positively correlated with incentives to research and vote on high-impact governance topics, but firm size is *negatively correlated* with incentives to research and vote on low-impact governance topics.

Overall, the foregoing calculations demonstrate that intermediaries possess weak financial incentives to invest in governance. These weak incentives persist even among the largest blockholders at some of the largest firms. Table 3 in particular presents a relatively favorable situation—for instance, it considers Vanguard, the biggest shareholder in roughly two-thirds of the largest public companies,<sup>262</sup> and Bank of America, among the top 1% largest publicly traded companies by market capitalization.<sup>263</sup> Generally speaking, smaller intermediaries (i.e., all other intermediaries) and smaller companies (i.e., 99% of all public companies) will generate incentives that are even weaker. Although Tables 2 and 3 present some governance items with a significant financial impact, the occurrence of such items is relatively rare. For instance, while proxy contests produce a large financial impact on average (6.77%), as few as thirteen proxy contests may

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260. By definition, in a market capitalization-weighted portfolio, firm size and portfolio weight will increase in tandem.

261. To the extent that using an average percentage for all firms overstates the necessary governance investments for one class of firms (e.g., perhaps governance investments at large firms benefit from economies of scale and require less than 0.2% of fees collected on such firms), it would also then understate the necessary governance investments for other classes of firms (e.g., smaller firms), further strengthening the case that intermediaries lack sufficient financial incentives to invest in governance for most issues at most firms.

262. See Griffin, *supra* note 76, at 411.

263. Bank of America is among the twenty-five largest public companies by market capitalization, in a universe of approximately 3600 stocks (the composition of the Vanguard Total Stock Market Index and its benchmark, the CRSP US Total Market Index). Dividing the former by the latter equals roughly 0.7%.

go to a vote each year.<sup>264</sup> Thus, even if they may be significant whenever they happen to occur, relatively rare events such as proxy contests and takeovers are likely insufficient justification for a more widespread financial incentive to invest in governance.

Moreover, even these relatively “significant” events often do not generate large financial incentives for small and midsize firms. Recall Table 1, which presents results for financial incentives with respect to intermediary governance at Walgreens.<sup>265</sup> Even if Walgreens was faced with a relatively significant governance issue—perhaps it was one of the thirteen companies where a proxy contest went to a vote that year—the financial incentives still only amount to roughly \$11,887.<sup>266</sup> If this seems to buy a rather meager amount of governance, consider that more than 85% of U.S.-listed public companies<sup>267</sup> would have lower portfolio weights than Walgreens, thus generating proportionally lower financial incentives.

Ultimately, low-value governance issues (such as most shareholder proposals) are very unlikely to generate positive financial incentives for intermediaries to invest in governance at any firm size. High-value governance issues will only do so at, charitably, the largest 15–20% of firms. Even this overstates the incentives, as the vast majority of the firms in this group will not face a proxy contest, takeover, or other high-value governance issue upon which an intermediary could vote in any given year. Additionally, it bears repeating that the calculations above assume that intermediaries can predict a given governance issue’s firm-specific price impact with 100% accuracy. In reality, the hotly contested share price impact of numerous corporate governance topics suggests that the true percentage is far lower. Thus, the financial incentives for investing in governance are weak, even for unusually significant ballot items at very large intermediaries.

#### IV. MARKET CONSTRAINTS ON THE MEANS OF MASS CORPORATE GOVERNANCE

This Part explores whether market forces successfully constrain the means by which intermediaries exercise governance power. Although

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264. William D. Regner & Marisa K. Demko, *2023 Proxy Season in Review*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Aug. 15, 2023), <https://corpgov.law.harvard.edu/2023/08/15/2023-proxy-season-in-review/> [<https://perma.cc/D2LW-S526>] (“During the 2023 proxy season, 13 election contests went to a vote, compared to 17 in the prior period.”).

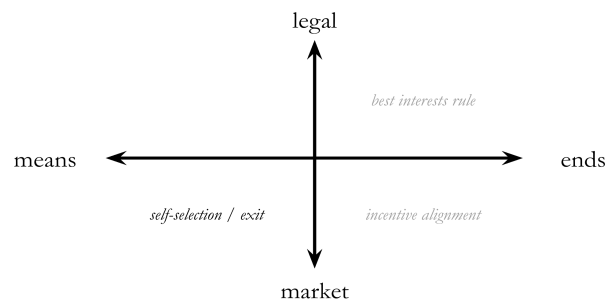
265. See *supra* Table 1.

266. See *supra* Table 1.

267. See *VTSAX*, *supra* note 236.

intermediaries generally face weak legal constraints on their ends<sup>268</sup> and lack strong market incentives to align such ends with their principals,<sup>269</sup> it is possible that market forces could constrain the methods of intermediary governance more precisely. Figure XI below situates strategies involving market-based constraints on means within the broader framework of agency cost reduction strategies.

FIGURE XI. THEORETICAL BEHAVIORAL CONSTRAINTS ON INTERMEDIARIES: MARKET-MEANS



The primary method by which the market might influence the means of intermediary governance is through investors' investment choices. That is, investors themselves may limit agency costs via market pressure on intermediaries through self-selection and exit.<sup>270</sup> More precisely, investors may observe the specific proxy voting records and/or read about the engagements (i.e., the "means" by which intermediaries exert governance power) of Fund A vs. Fund B, and then pick the fund that best matches their governance preferences.<sup>271</sup> By self-selecting into funds or asset managers that closely conform to their voting and other governance priorities, while exiting those that do not, investors will, in theory, shape the governance behavior of intermediaries and quickly mitigate any agency costs that may

268. See *supra* Part II.

269. See *supra* Part III.

270. See *Jones v. Harris Assocs. L.P.*, 527 F.3d 627, 632 (7th Cir. 2008), *vacated and remanded*, 559 U.S. 335 (2010), and *aff'd*, 611 F. App'x 359 (7th Cir. 2015) (describing how mutual fund investors may "vote with their feet and dollars"); Jill Fisch, Assaf Hamdani & Steven Davidoff Solomon, *The New Titans of Wall Street: A Theoretical Framework for Passive Investors*, 168 U. PA. L. REV. 17, 23 (2019) (noting that "[l]ike all mutual fund shareholders, investors in index funds can exit at any time by selling their shares").

271. Sarah C. Haan, *Voting Rights in Corporate Governance: History and Political Economy*, 96 S. CAL. L. REV. 881, 935 (2023) (discussing how disclosures "were designed to provide investors with tools to choose funds whose proxy voting aligned with investors' own preferences").

arise.<sup>272</sup> Intermediaries whose means of governance are both (1) fully disclosed (e.g., in a proxy voting record of Form N-PX<sup>273</sup> or via descriptions of engagements<sup>274</sup>) and (2) well-aligned with the interests of investors will, all else being equal, attract additional inflows and generate profits, while those employing poorly aligned (or undisclosed) governance means will see investors exit and their profits reduced.<sup>275</sup>

In practice, however, the ability of investors to self-select and freely exit is often highly constrained. For instance, consider the trillions of dollars of investments held in workplace retirement accounts.<sup>276</sup> These accounts offer a limited menu of employer-selected funds, usually from a single fund provider.<sup>277</sup> For investors in such workplace retirement accounts, switching to a fund provider with better governance is effectively impossible (that is, without leaving their jobs, forfeiting the considerable tax benefits associated with such accounts, and/or paying a penalty for early withdrawal).

Additionally, even for investors outside of workplace retirement accounts, there are often significant financial costs that prevent self-selection and exit.<sup>278</sup> For most such investors, exiting a fund is a taxable

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272. *Id.* at 935–36 (discussing how facilitating self-selection based upon governance practice “reduces agency costs”).

273. Press Release, U.S. Sec. & Exch. Comm’n, SEC Adopts Rules to Enhance Proxy Voting Disclosure by Registered Investment Funds and Require Disclosure of “Say-on-Pay” Votes for Institutional Investment Managers (Nov. 2, 2022), <https://www.sec.gov/newsroom/press-releases/2022-198> [<https://perma.cc/VSP3-R3DY>] (discussing amendments designed to streamline form N-PX across funds to enable investors to “compare different funds’ voting records”).

274. Bebhuk & Hirst, *supra* note 221, at 2124 (calling for greater transparency regarding engagements).

275. See Fisch et al., *supra* note 270, at 18 (“[A]lthough passive funds are locked into their investments, their shareholders are not. Like all mutual fund investors, shareholders in index funds can exit at any time by selling their shares and receiving the net asset value of their ownership interest.”).

276. Anne Tucker, *The Citizen Shareholder: Modernizing the Agency Paradigm to Reflect How and Why a Majority of Americans Invest in the Market*, 35 SEATTLE U. L. REV. 1299, 1327 (2012) (“The defined environment in which many Americans invest erodes the strength of the popular remedy of voting with dollars or feet.”).

277. John Morley & Quinn Curtis, *Taking Exit Rights Seriously: Why Governance and Fee Litigation Don’t Work in Mutual Funds*, 120 YALE L.J. 84, 113 (2010) (“Another potential obstacle to switching is the structure of 401(k) plans. These plans are tax-favored accounts set up by employers through which employees often invest in mutual funds. Employees’ choices may be limited in these arrangements, because employees can usually only select funds offered by one or two service providers chosen by their employers.”).

278. Nancy L. Conlin, *Mutual Fund Expenses: Caveat Investor?*, 13 ANN. REV. BANKING L. 365, 387 (1994) (“[I]t is deceiving to suggest that switching funds is an adequate remedy for investors. The court’s reasoning ignores the substantial costs to the investor associated with switching funds. The investor who chooses to change funds faces the prospect of paying another sales load and, possibly, a capital gains tax. These costs are likely to deter a fund investor who would otherwise consider moving to another fund with lower fees.”).

“realization event,” triggering the obligation to pay capital gains taxes.<sup>279</sup> These taxes are due even if the investor purchases an essentially identical fund tracking the same index.<sup>280</sup>

What sort of cost-benefit analysis would an investor contemplating such a decision face? Is it *ever* rational to incur 15–20% capital gains tax liability for better governance alignment?<sup>281</sup> The answer is likely no—while governance improvements could, in theory, generate offsetting gains, it is only rational for an individual investor to incur such costs if their actions have a reasonable probability of *causing* such governance change (i.e., their vote is outcome-determinative). For all but a handful of the very largest investors, this is vanishingly unlikely.<sup>282</sup> Even in the extremely unlikely event that an investor’s vote was potentially outcome-determinative, the benefits of marginally improved stewardship activities at another fund would still need to be so significant that they outweigh the sizable 15–20% tax on their gains. Thus, switching funds is likely to be a cost-prohibitive endeavor, constraining the ability of investors to exit and weakening the utility of such market-based constraints on means to mitigate agency costs of intermediaries.

Self-selection into new investments represents the most promising case for constraining the means of intermediary behavior via market incentives. Such new investments (i.e., without a prior taxable sale and outside of workplace retirement accounts) are not burdened by the costs and constraints discussed above. And yet, even here, it is still irrational for most investors to allocate their assets based on governance costs. For an investor choosing between two funds which differ only in respect to their governance, it will only be rational to incur higher fees if the difference in governance costs exceeds the difference in fees between the two funds *and* this asset allocation decision causally reduces such governance costs (i.e., these marginal votes were outcome-determinative).<sup>283</sup> This places a

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279. See *Capital Gains Tax: What You Need to Know*, VANGUARD, <https://investor.vanguard.com/investor-resources-education/taxes/realized-capital-gains> [<https://perma.cc/4YTT-YCD8>] (“Capital gains are profits on an investment. When you sell investments at a higher price than what you paid for them, the capital gains are ‘realized.’ You’ll owe taxes on your realized gains.”).

280. See Jessica Goldenring, *Who Stays, Who Switches: Tax Frictions and the Shift from Mutual Funds 1* (Nov. 18, 2025) (unpublished manuscript), <https://ssrn.com/abstract=6003854> [<https://perma.cc/R26V-B65X>] (“Unrealized gains create persistence by locking investors into funds . . . as switching triggers immediate capital gains taxes.”).

281. *Capital Gains Tax*, *supra* note 279 (discussing capital gains tax rates, which may be 0%, 15%, or 20% depending on income).

282. Dov Solomon, *The Voice: The Minority Shareholder’s Perspective*, 17 NEV. L.J. 739, 748 (2017) (“This diffused distribution means that each individual investor owns only a negligible portion of the company. Since voting power at annual meetings is proportionate to share ownership, investors holding insignificant portions of shares will have no real ability to impact the decision making.”).

283. See *id.* (discussing the cost-benefit analysis of voting decisions in a related context).

significant limitation on the ability of investors to self-select based upon stewardship characteristics.

Additionally, many intermediaries exhibit similar voting behavior, such that investors are left with a limited degree of true choice. As discussed in Part II above, voting priorities have converged between many intermediaries on certain topics.<sup>284</sup> Problematically, however, these alleged best practices are not universally supported in the literature or embraced by their clients.<sup>285</sup> The result is that there is relatively coordinated voting behavior on certain issues, potentially impeding private ordering and limiting the ability of investors to identify a fund provider that votes in a manner consistent with their personal views.

Finally, even in the most ideal of circumstances (i.e., where an investor is dealing exclusively with previously uninvested money outside of workplace retirement plans), self-selecting into investments based upon governance considerations is effectively a one-time decision. Once an investor's capital has been placed in a particular fund, it is effectively "locked in," making it difficult to relocate capital.<sup>286</sup> In contrast, governance decisions are ongoing, and, as historical evidence amply demonstrates, intermediaries' voting practices can vacillate dramatically over time.<sup>287</sup> An intermediary's past voting record is thus not a reliable indicator of its future voting behaviors, a reality which further attenuates any potential "market pressure" in the form of investor self-selection based upon governance.

In sum, despite the theoretical potential of market constraints on the means by which intermediaries engage in governance, the ability of an investor to identify and invest with a well-aligned intermediary is highly constrained in practice. Investors face significant financial incentives to select intermediaries based on factors other than their governance activity, and even if they were to prioritize governance above such other factors (e.g.,

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284. See Lund & Pollman, *supra* note 5, at 2595 ("Because proxy advisors supply voting advice on thousands of different companies each year, they are forced to be generalists on a wide range of governance issues that commonly arise, ranging from proxy access to corporate political spending disclosures. To supply advice at scale, they reach conclusions about 'best practices' on each issue and then set governance guidelines that are enforced through their voting guidance.").

285. Ahn et al., *supra* note 97, at 485 ("Despite the extensive effort that has gone into empirical analyses, there is limited consensus on the desirability of most corporate governance provisions.").

286. See Anne M. Tucker, *Locked In: The Competitive Disadvantage of Citizen Shareholders*, 125 YALE L.J.F. 163, 164 (2015) (discussing the problem of lock-in for some mutual fund investors and how it makes exit "an empty option").

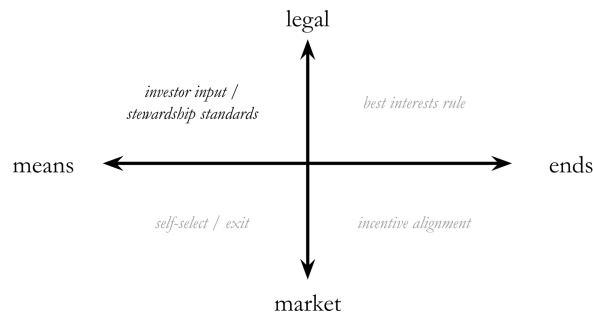
287. See, e.g., Lindsey Stewart, *Big U.S. Fund Companies Retreat on Support for ESG Proxy Votes*, MORNINGSTAR (Jan. 11, 2024), <https://www.morningstar.com/sustainable-investing/big-us-fund-companies-retreat-support-esg-proxy-votes> [<https://perma.cc/TB6F-BH4E>] (describing a "sharp drop" in support for ESG by many large intermediaries); Sarah George, *BlackRock's Support for ESG Resolutions Plummets*, EDIE (Oct. 23, 2024), <https://www.edie.net/blackrocks-support-for-esg-resolutions-plummets/> [<https://perma.cc/JT9U-CZQE>] ("BlackRock supported just 4% of the shareholder proposals on environmental and social issues it voted on in 2024, down from 47% in 2021.").

for ideological rather than economic reasons), intermediaries may freely change their future voting behavior (as they have in the past). In addition, an investor's ability to select an appealing intermediary is effectively a one-time decision, after which point, lock-in effects generally dominate other factors. The collective impact of these factors is such that market forces are unable to adequately constrain the means by which intermediaries influence corporate governance.

#### V. LEGAL CONSTRAINTS ON THE MEANS OF MASS CORPORATE GOVERNANCE

Although legal constraints on the ends of corporate governance proved too subjective to meaningfully limit governance costs by intermediaries,<sup>288</sup> perhaps more precise legal constraints on the means intermediaries employ will fare differently. This Part explores legal and regulatory avenues of agency cost reduction targeting not the ultimate ends of governance activity, but, rather, the specific structures, resources, and mechanisms employed to achieve such ends. Strategies focused on legally constraining the means of intermediated governance occupy the final quadrant of potential agency cost reduction strategies, as reflected in Figure XII below.

FIGURE XII. THEORETICAL BEHAVIORAL CONSTRAINTS ON INTERMEDIARIES: LEGAL-MEANS



These strategies break down into two further categories—strategies to constrain the specific means that intermediaries employ when engaging in governance and strategies to enhance the overall level of spending on such means. Although procedural rules, such as those mandating disclosure,

288. See *supra* Part II (arguing that the ends of corporate governance interventions are too subjective to meaningfully constrain intermediaries' discretion).

could be categorized as legal constraints on the means of governance, their primary utility is to provide information for market participants to use in their entry and exit decisions, and they are thus primarily relevant in the context of market constraints on means.<sup>289</sup> The following Sections discuss efforts to enhance spending on stewardship (Section V.A) and specific constraints on means (Section V.B) in turn.

#### *A. Enhancing Expenditures*

One approach to reducing the agency costs of intermediaries involves increasing the financial resources devoted to the means of intermediated governance.<sup>290</sup> Professors Lucian Bebchuk and Scott Hirst propose such a policy, suggesting that certain asset managers could be required to spend a specified fraction of assets under management (perhaps 0.0005–0.001%) above a threshold level on stewardship.<sup>291</sup> This policy would significantly increase the resources invested in corporate governance activity by intermediaries (the “means” by which they engage in such activity) without altering its ends. However, there are risks to mandating higher spending by agents in an attempt to solve agency costs. While asset managers may choose to utilize the additional mandated expenditures in a manner that is well-aligned with their investors, a spending mandate would leave the underlying incentive alignment untouched. Existing conflicts of interest would continue unaltered, and the amount of “skin in the game” that asset managers possess would likewise remain unchanged. A stewardship spending mandate would also not alter the weak legal obligations to act in investors’ “best interests.” Because the underlying market incentives and legal obligations have not changed, there is no assurance that the mandated expenditures would be used appropriately, or that any resulting revelations would be acted upon. If existing legal and market structures produce “empty voting” by asset managers—that is, voting by entities who possess “little or no economic interest in the shares that they vote”<sup>292</sup>—then mandating higher spending without altering such structures may simply result in *more expensive* empty voting. Ultimately, there is a significant risk that mandating higher spending by agents merely increases the amount of “empty” governance activity in which such agents engage.

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289. See *supra* Part IV (discussing the insufficiency of market constraints on means to limit intermediaries’ voting discretion).

290. Bebchuk & Hirst, *supra* note 221, at 2119–22 (2019).

291. *Id.* at 2121–22.

292. See generally Jill E. Fisch, *Mutual Fund Stewardship and the Empty Voting Problem*, 16 BROOK. J. CORP. FIN. & COM. L. 71 (2021).

### B. Specific Constraints on Means

The second category of substantive constraints on the means of intermediary governance aims to specify, with varying degrees of exactitude, the pursuit and/or implementation of various governance policies. Because the primary problem to be addressed is one of misalignment between principal and agent, policies in this category generally focus on requiring intermediary agents to solicit input from their investors and to take account of such input in their governance activities.

Corporate legal scholars have proposed soliciting the input of investors in various fashions.<sup>293</sup> Most recently, Professors Jill Fisch and Jeff Schwartz have proposed a policy of “informed intermediation,” whereby mutual fund and pension fund intermediaries would solicit the preferences of their investors and use them to generate “individualized and informed votes at each of their portfolio firms.”<sup>294</sup> Other scholars have also proposed seeking the preferences of investors in other contexts, including when voting on “social responsibility resolutions”<sup>295</sup> and using “informed discretion” in the context of proxy voting by index funds.<sup>296</sup>

In practical terms, such proposals generally involve intermediaries polling their investors in some fashion and using the information gleaned to inform their proxy voting behavior and engagements with portfolio companies. Importantly, input solicitation strategies can be distinguished from pass-through voting in that the former typically allows intermediaries to retain ultimate discretion over governance decisions, while the latter does not.<sup>297</sup>

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293. See Scott Hirst, *Social Responsibility Resolutions*, 43 J. CORP. L. 217, 220 (2018) (arguing that mutual funds should, when voting on social responsibility resolutions, “consider the preferences of their investors when determining voting policies and decisions”); Caleb N. Griffin, *We Three Kings: Disintermediating Voting at the Index Fund Giants*, 79 MD. L. REV. 954, 990 (2020) (arguing that index funds should be obligated to solicit investor input on salient governance topics); Griffin, *supra* note 91, at 723 (proposing that mutual funds should be required 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”); Fisch & Schwartz, *supra* note 1, at 1 (arguing that mutual and pension funds should be required to “seek input from their beneficiaries on their views, reflect those views in both their engagement efforts and their votes, and publicly disclose how they have complied.”).

294. Fisch & Schwartz, *supra* note 1, at 1; see also Griffin, *supra* note 293, at 990 (proposing a policy of “informed discretion” which “would entail solicitation by index fund providers of more information about the characteristics and values of their investors, which they would use to better inform their voting decisions”).

295. See Hirst, *supra* note 293, at 220.

296. See Griffin, *supra* note 293, at 990; see also Griffin, *supra* note 91, at 723.

297. See Griffin, *supra* note 293, at 993 (discussing how, in comparison to pass-through voting, informed discretion “necessitates giving considerable discretion to index fund representatives in interpreting how the characteristics and priorities of individual investors should translate into actual votes”).

Input solicitation proposals are beneficial in that they facilitate voting in greater accord with the preferences of investors on certain topics. In particular, when voting implicates contested values—such as increasingly politicized ESG topics—soliciting investor preferences may be particularly important.<sup>298</sup> Scholars have argued that seeking investor input allows asset managers “to better fulfill their fiduciary duties to index fund investors.”<sup>299</sup> Some scholars have gone further, arguing that seeking such input is in fact compulsory for intermediaries to fulfill their fiduciary duties.<sup>300</sup>

However, such proposals suffer from important limitations. First, soliciting investor input presents a variation of the “goldilocks problem”—input can either be high-level and imprecise or granular and onerous. In the former category, investors might indicate their preference for their intermediaries to “maximize shareholder wealth,” “support all corporate stakeholders,” or “support sustainable capitalism,” among other general mandates. Such a survey would be short and highly accessible to most investors, and participation rates could be relatively high. However, such high-level input very easily collapses into the ends-based constraints laid out in Part II above, and it suffers from the same weaknesses.<sup>301</sup> The subjectivity inherent in implementing vague, ends-based mandates would do little to reduce intermediaries’ discretion and the attendant agency costs, rendering this approach largely ineffective.<sup>302</sup> On the other hand, investors might be invited to indicate their preferences on a more granular level with respect to numerous ballot items, which would likely exhibit some heterogeneity year over year.<sup>303</sup> Granular, issue-specific input would have far greater potential to reduce intermediaries’ discretion, potentially requiring intermediaries to vote in a specified way on certain topics. However, in precise proportion to its specificity and capacity to constrain governance costs, such input would also be more onerous for investors to

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298. See Fisch & Schwartz, *supra* note 1, at 5 (“Now that institutions engage on a growing range of environmental, social, and political issues, their participation in corporate governance increasingly raises the question of whether they are acting in a manner consistent with the interests of their beneficiaries. Engagement on these issues implicates contested values . . .”).

299. Griffin, *supra* note 293, at 1004 (discussing how “seeking input of individual index fund investors about voting priorities and interests would be a way for index fund providers to better fulfill their fiduciary duties to index fund investors”).

300. See Fisch & Schwartz, *supra* note 1, at 1 (“We argue that the fiduciary duties of fund managers compel them to seek this input.”).

301. See *supra* Part II.

302. See *supra* Part II (discussing the subjectivity inherent in limiting intermediaries’ discretion by prescribing certain ends).

303. See Matthew Mullins, *Proxy Season Shows Corporate Governance Keeps Evolving*, U.S. CHAMBER OF COM. (Oct. 24, 2024), <https://www.uschamber.com/finance/corporate-governance/proxy-season-shows-that-corporate-governance-keeps-evolving> [<https://perma.cc/6H9P-HQH6>] (discussing the evolving nature of corporate governance).

provide and would likely generate relatively low participation rates. Although a reduction in governance discretion (i.e., requiring intermediaries to vote in alignment with the expressed interests of their shareholders) is highly desirable from the perspective of agency cost reduction, the low participation rate to be expected in granular or onerous surveys might constrain intermediaries' views expressed only by a potentially unrepresentative minority of respondents. Thus, precise, granular input (which otherwise *could* constrain agency costs) would suffer from investor apathy and lack of expertise.<sup>304</sup> On the other hand, high-level input's inherent collapse into subjectivity would allow intermediaries continued autonomy in their governance activity, thereby doing nothing to reduce agency costs.<sup>305</sup>

Relatedly, soliciting investor input presents a challenge for fiduciaries who likely represent a heterogeneous and conflicted pool of investors.<sup>306</sup> If, as is very likely, intermediaries received mixed results in their investor feedback, they would be faced with a difficult choice between splitting their votes between opposing positions and thereby diluting their influence over the outcome, or deliberately voting against the self-expressed interests of a significant portion of their fiduciaries. Because many of these minority voices have limited opportunities to self-select into better aligned funds,<sup>307</sup> they would be in the uncomfortable position of investing with an intermediary who deliberately votes against their self-expressed best interests.

Ultimately, soliciting investor input over voting decisions would be a step forward, but it would be unlikely to sufficiently constraint intermediary discretion without ostracizing a meaningful portion of fund investors. Most of the largest intermediaries have already begun to shift toward a representative model of investor input. While current iterations of this

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304. Fisch and Schwartz note that “[i]ssue-level engagement . . . leads to bad governance because of problems with apathy and expertise.” Fisch & Schwartz, *supra* note 1, at 61. However, they add that these are “problems that intermediation through elected representatives mitigates.” *Id.* Intermediation, in this case, thus likely means ignoring granular input on most governance issues, or simply not soliciting it at all. Combined with the subjectivity inherent in high-level input (e.g., “maximize wealth”), the likely result is that, for the majority of corporate governance activity, input solicitation and intermediation will have little to no effect.

305. However, as discussed in Part VI, combining delegated voting with input solicitation could represent a potential “goldilocks” solution. Such a hybrid solution would involve soliciting an amount of investor input that would be too limited to provide a comprehensive solution to the governance costs of intermediaries (i.e., too limited to constrain them in a wide variety of areas) but sufficient for the intermediary to infer a suitable delegate. *See infra* Part VI.

306. *See* LYNN STOUT, THE SHAREHOLDER VALUE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC 7 (2012) (discussing the “reality that different shareholders have different values”).

307. *See supra* Part IV (discussing the limitations on investor self-selection and exit).

representative model have proven somewhat problematic,<sup>308</sup> the potential of a representative model offers substantial advantages over investor surveys: the ability to solicit a single piece of input from investors while simultaneously and entirely removing discretion from the hands of intermediaries. Part VI, which follows, explores how to harness the current momentum toward a representative model in a manner that more effectively reduces agency costs.<sup>309</sup>

## VI. THINKING BEYOND CONSTRAINTS

The prior Parts explored potential strategies to limit the agency costs arising from discretionary governance activity by intermediaries. In each case—for every permutation of legal and market restrictions on the means and ends of corporate governance—the purported constraints failed to limit governance discretion to any meaningful degree. This Part argues that, rather than attempting to constrain governance discretion, we should allow investors to choose *to whom* such discretion is granted.

In what follows, Section VI.A describes the theoretical justifications and mechanics of delegated voting. Section VI.B explores the feasibility of delegated voting. Section VI.C outlines voting inference, and its relationship to the default voting arrangement at intermediaries. Section VI.D considers approaches to financing. Section VI.E discusses the benefits and second-order effects of this proposal's adoption.

### A. Delegated Voting

Intermediated governance, particularly as instantiated in modern mass corporate governance, is inherently a delegation of discretion. Most basically, the only two options for who will make a governance decision are (1) the agent and (2) the principal. Barring “pure” pass-through voting (where the principal precisely specifies how to vote each of many thousands of unique ballot items), the agent will necessarily exercise some discretionary governance power. The structural features of mass corporate governance exacerbate the issue further—as discussed in the preceding Parts, when effectively mandatory voting is paired with hyper-diversified, semi-commoditized holdings that compete primarily on fees, the result is high-volume, low-value, non-firm-specific, compliance-oriented governance activity. It is often impossible to objectively define the “right”

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308. See generally Griffin, *supra* note 36 (discussing the deficiencies of the “proxy choice” models recently advanced by intermediaries).

309. See *infra* Part VI (arguing for an improved representative model).

way to vote due to the subjectivity of many governance topics, costly to monitor an agent's voting on tens of thousands of ballot items annually, infeasible to sue for any allegedly incorrect proxy vote, and economically irrational to exit for governance reasons. The result is that, at present, intermediaries exercise their voting power with near-total discretion.

The most obvious solution is to pass through full voting authority to the principal, thereby bypassing the agent and, by extension, any associated agency costs. However, this solution is impracticable. No rational principal, either retail or institutional, desires to research and vote individually on tens of thousands of annual ballot items. A more reasonable option involves soliciting investor input in some fashion. Typically, this takes the form of investors answering several poll questions on a variety of specific or general corporate governance topics and tasking intermediaries with acting on the results of the poll.<sup>310</sup> However, as previously outlined in Part V, general investor input will fail to constrain intermediaries' discretion, while specific investor input suffers from issues with investor apathy and expertise.<sup>311</sup>

Delegated voting represents a superior policy solution to both "pure" pass-through voting and polling investors. Modifying the simple model above, a more complete theoretical picture of who may exercise governance authority includes the possibility of delegation. The result is reflected in Figure XIII, below:

#### FIGURE XIII. FRAMEWORK OF GOVERNANCE AUTHORITY

*This figure portrays the potential allocation of governance authority between principals, agents, and their respective delegates, as well as a brief description of the dominant policy options in each category.*

At present, agents dominate the corporate governance arena, as reflected in the left two quadrants in Figure XIII. Agents directly exercise governance control through their stewardship teams, who set proxy voting guidelines and conduct engagements with portfolio companies, and they also partially delegate a variable portion of their governance obligations to proxy advisors. While proxy advisors are useful, and perhaps essential for the modern mass corporate governance ecosystem to function, the multiple layers of intermediated agency reduce accountability and compound agency costs.

This Article argues that, rather than fighting to constrain governance activity by agents (or, compounding the problem, the behavior of their

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310. See *supra* Part V (discussing this policy proposal).

311. See *supra* Part V.

subagents and delegates), we should instead let principals choose to whom they wish to grant governance discretion. Much as intermediary agents may freely choose their own proxy advisor to guide their proxy voting, so too should principals be granted this same right. Thus, this Article proposes broadly focusing on policy solutions in the upper right quadrant of Figure XIII, whereby the *principal* may delegate voting authority, rather than an intermediary agent retaining such authority for themselves or delegating it to yet another agent.

Although this Article does not propose mandating the precise type of delegated governance that should occur, it argues that delegated governance would be enhanced by utilizing two key policy solutions: “open delegation” and “proxy inference.” An open proxy delegation policy is one where principals may delegate governance authority to an unrestricted set of agents operating in a competitive market, rather than the status quo of intermediary gatekeeping and duopolistic market power.<sup>312</sup> A proxy inference policy recognizes that inference is an essential remedy to voter apathy and collective action problems and shifts the default governance obligations of asset managers from unitary discretion to proportional inference. These policies will be further explored in the following Sections.

### *B. Toward Free Delegation of Governance Authority*

Delegated voting not only holds considerable theoretical promise, it is also well within reach as a matter of policy praxis. The strongest evidence of its feasibility is its partial implementation by large asset managers. At present, each of the world’s three largest asset managers has implemented a pilot program facilitating some measure of “voting choice,” whereby investors in certain selected funds may choose from a menu of voting policies.<sup>313</sup> Although most other asset managers have not implemented such programs, this marks a significant step, and it demonstrates that delegated voting is both clearly feasible and not cost-prohibitive. However, existing voting choice programs suffer from limitations on who may participate and, more fundamentally, on the level of “choice” that the various voting choice programs grant to investors.

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312. ISS and Glass Lewis, the two largest proxy advisors, control roughly 97% of the market share for proxy advisory services. Eckstein & Hannes, *supra* note 95, at 818.

313. See *Empowering Investors Through BlackRock Voting Choice*, BLACKROCK, <https://www.blackrock.com/corporate/about-us/investment-stewardship/blackrock-voting-choice#blackrock-voting-choice-policies> [<https://perma.cc/6V62-SWBC>].

### 1. *Facilitating Delegation*

First, delegated voting programs are currently only available to certain investors in designated funds provided by a limited number of asset managers. Given the failure of other modes to constrain the governance-related agency costs of intermediaries, this should be expanded. Specifically, this Article proposes mandating that all asset managers above a certain threshold size, perhaps \$100 billion in assets under management, must allow delegated voting for their investors. This threshold could be adjusted up or down based on market needs, but it would allow a substantial number of investors to participate in disintermediated governance through delegated voting. As a legal matter, an open delegation policy would be justified in the same manner as existing voting choice programs—namely, that, somewhat tautologically, voting according to an investor’s self-expressed “best interests” fulfills the intermediary’s fiduciary obligation to vote in the investor’s “best interests.” For clarity, however, and to facilitate rapid adoption of this policy, the SEC should add a safe harbor for delegating governance authority; such a safe harbor could be analogous to the Department of Labor’s 2023 rulemaking that exempted “participant directed pass-through voting” from various regulatory obligations.<sup>314</sup>

One potential qualification is that a complete lack of restrictions on the agents to whom investors may delegate governance authority may lead to insufficient investor protection. Although intermediaries likely possess some fiduciary obligations with respect to vetting potential governance delegates, fulfilling those obligations is a relatively low bar. Indeed, given the subjective nature of most corporate ballot items,<sup>315</sup> it is hard to see how any given proxy vote could be considered objectively “right” or “wrong” such that it would lead to liability. Moreover, even rather extreme “blanket” voting policies are evidently acceptable; for instance, Vanguard has allowed investors in its pilot programs to defer 100% of votes to the recommendations of the company’s board of directors, as well as providing them with the option to abstain from proxy voting entirely.<sup>316</sup> It is thus

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314. See Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights, 87 Fed. Reg. 73822 (Dec. 1, 2022) (codified at 29 C.F.R. pt. 2550 (2026)) (stating, with respect to “participant-directed pass-through voting,” that “[this] regulation does not apply to voting, tender, and similar rights with respect to shares of stock that, pursuant to the terms of an individual account plan, are passed through to participants and beneficiaries with accounts holding such shares.”). Such a rule should prove largely uncontroversial, if the Department of Labor’s recent rulemaking is any guide. See *id.* (“The Department did not receive comments on this provision, which is being adopted as proposed.”).

315. See *supra* Part II.

316. See VANGUARD, STATEMENT OF ADDITIONAL INFORMATION (Feb. 1, 2023), <http://edgar.secdatabase.com/1721/168386323000558/filing-main.htm> [<https://perma.cc/BE43-NBDG>] (describing, among other policies, the “Company Board-aligned Policy” and the “Not Voting” policy”).

somewhat difficult to imagine what characteristics or voting policies, precisely, might render a proxy advisor unacceptable under an open delegation policy. However, it is possible that something analogous to bad faith, such as a “conscious disregard for one’s responsibilities,”<sup>317</sup> would be appropriate grounds for exclusion. One obvious example of such conscious disregard for responsibilities would be failing to implement any voting policies at all. However, the goal should be to have a relatively high bar for exclusion. For instance, fraudulent statements or serious conflicts of interest (i.e., more serious than the existing conflicts of interest afflicting asset managers and proxy advisors) would be appropriate grounds for disqualification.

## 2. *Facilitating Competition & Choice*

In addition to expanding access to delegated voting, this Article proposes expanding the universe of potential delegates. Current voting choice programs artificially constrain investor choice in two important ways. First, investor choice is directly constrained by asset managers, who act as discretionary gatekeepers as to which voting policies and delegates investors should be allowed to select. Second, investor choice is indirectly constrained by the duopolistic market structure for proxy advisory services, which leaves investors with more limited choices than would be provided in a more competitive market.

Adopting an open delegation policy would directly solve the first issue by largely eliminating the gatekeeping authority of intermediaries to exclude proxy advisors, barring the types of fraudulent statements or serious conflicts of interest discussed above. Such a policy would also address the second issue by lessening the indirect constraints on investor choice. The fact that new proxy advisors would be presumptively allowed to compete for clients (rather than being presumptively excluded until they individually lobbied each intermediary for inclusion) would make the space much more attractive to new entrants. In the same vein, new entrants and increased competition would spur innovation in the space. Currently, the two largest proxy advisors, ISS and Glass Lewis, control approximately 97% of the market for proxy advisory services.<sup>318</sup> New entrants would be forced to innovate to compete with one another and to capture a portion of this market share from the established players.

In addition to increasing the absolute amount of competition, an open delegation system would also influence the *type* of competition that occurs.

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317. See *In re Walt Disney Co. Derivative Litig.*, 906 A.2d 27, 62 (Del. 2006).

318. Eckstein & Hannes, *supra* note 95, at 818.

To the extent that today's market is competitive, it often involves competing for the business of intermediary agents. At present, the proxy advisors face strong incentives to attempt to best meet the needs of *agents*—to satisfy the preferences and goals of intermediaries—rather than those of their investor principals. By allowing investors to make their own choices with respect to delegated voting, proxy advisors would instead begin to compete to fulfill the goals and preferences of investor principals.

### 3. *Investor Subtypes: Institutional v. Retail*

Institutional and retail investors often differ in their ability to participate in pass-through voting and delegated voting. Retail investors face a level of “voting choice” that is relatively constrained, assuming that such investors are able to participate at all. For instance, in addition to its own proxy voting policy, Vanguard offers investors in selected funds four additional voting policies,<sup>319</sup> an increase of one policy over the prior year.<sup>320</sup> Two such policies allow investors to delegate to external proxy advisors.<sup>321</sup> While a laudable improvement, particularly relative to funds outside of their pilot program (which still have no choice at all), the “closed” nature of the system significantly inhibits the development of a competitive, investor-facing market for proxy advisory services, as well as artificially limiting investor choice.

Institutional clients often face fewer constraints. For instance, some intermediaries permit institutional clients to exercise considerable control over how their investment assets are voted, even allowing them to craft their own bespoke voting plans, which the intermediary agrees to follow.<sup>322</sup> Thus, at first blush, it may seem that an open delegation policy is unnecessary in institutional context. However, even here, an open proxy delegation system

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319. See Press Release, Vanguard, Vanguard Nearly Doubles Eligible Assets in Investor Choice Program with Three New Funds (Nov. 18, 2024), <https://corporate.vanguard.com/content/corporatesite/us/en/corp/who-we-are/pressroom/press-release-vanguard-nearly-doubles-eligible-assets-in-investor-choice-program-with-three-new-funds-111824.html> [<https://perma.cc/9C5W-XE4Q>].

320. The “Mirror Voting Policy” replaced the “Not Voting Policy” available in the prior proxy season. Compare *id.*, with VANGUARD, *supra* note 316 (“The four proxy voting policies are: (i) the Vanguard-Advised Funds Proxy Voting Policy . . . (ii) the Company Board-Aligned Policy; (iii) the ‘Not Voting’ Policy; and (iv) the Glass Lewis ESG Policy.”).

321. See Press Release, Vanguard, *supra* note 319.

322. See, e.g., Press Release, BlackRock, BlackRock Expands Voting Choice to Additional Clients (Jun. 13, 2022), <https://www.blackrock.com/corporate/newsroom/press-releases/article/corporate-one/press-releases/2022-blackrock-voting-choice> [<https://perma.cc/AB8S-GLYK>] (“Some of BlackRock’s largest institutional clients have the resources and the expertise to create their own voting policies, as well as the infrastructure needed to conduct the voting. This option gives clients in our pooled vehicles the ability to apply their stewardship preferences in a consistent way across a broader share of their overall portfolio allocation and to exercise a high degree of control over the decision-making process and the voting implementation.”).

offers important benefits. While the opportunity to create bespoke voting guidelines (where available) seems like it may obviate the need for delegated voting, that is generally untrue. Much like intermediaries, institutional clients (and the agents who run them) often possess insufficient economic incentives to engage in informed governance. While the option to engage in bespoke voting is valuable, and should be permitted, the financial incentives to conduct in-depth research and vote in a firm-specific fashion are typically quite low. Given that the world's largest asset managers generally face low monetary incentives to invest in firm-specific governance (both in percentage and absolute terms) it is generally unrealistic to think that smaller institutions, often with proportionately smaller monetary incentives and much smaller stewardship teams, will perform any better. This is especially true with respect to smaller companies, each of which individually may be insignificant in the context of a market-weighted portfolio. Proxy advisors can thus play a critically important role in pooling resources, aggregating and distributing firm-specific information, and operating as "one of the few channels that contribute to governance making in smaller companies."<sup>323</sup> Ultimately, the ability to delegate voting authority to a chosen proxy advisor remains valuable even for institutional investors, particularly for institutions with less extensive stewardship teams (i.e., virtually all asset managers outside of the Big Three) and for the governance of smaller firms.

### *C. Collective Action, Apathy, & Inference*

In addition to adopting an open delegation policy, intermediaries should also utilize what this Article terms "proxy inference." Broadly, this policy involves changing the default inference about investor intent.

#### *1. Current Default Inference*

Collective action problems and rational apathy are inherent in the nature of dispersed ownership.<sup>324</sup> While delegated voting can help mitigate these issues, it is also important to acknowledge that they cannot be eliminated

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323. Kastiel & Nili, *supra* note 110, at 792.

324. See Frank H. Easterbrook & Daniel R. Fischel, *Voting in Corporate Law*, 26 J.L. & ECON. 402, 402 (1983) ("When many are entitled to vote, none of the voters expects his votes to decide the contest. Consequently none of the voters has the appropriate incentive at the margin to study the firm's affairs and vote intelligently."). See generally MANCUR OLSON, *THE LOGIC OF COLLECTIVE ACTION* (1965).

entirely.<sup>325</sup> As a result, intermediated governance necessarily involves a degree of inference. Given that some significant fraction of investors will exhibit rational apathy, what inference should be made about their governance priorities?

Currently, the implicit default is that governance priorities are inferable from an investor's choice of intermediary. That is, the act of investing money with a given intermediary is perceived as an affirmation of such intermediary's proxy voting and other corporate governance policies. The problem is this inference is completely unfounded. As discussed in Part IV, governance policies are *irrelevant* to a rational investor's choice to invest with a given intermediary.<sup>326</sup> As a result, *no inference* can be drawn regarding an investor's supposed support for the asset manager's proxy voting policy.<sup>327</sup>

## 2. *A New Default*

If assuming that investing with a given intermediary signals agreement with its governance policies is generally unfounded, what inferences are appropriate? Given the inevitability of apathy and the failure of the current default inference, this Article suggests that intermediaries should treat investor input, broadly conceived, as the best evidence of investor intent. In particular, the default assumption, that governance priorities are inferable from an investor's choice of intermediary, should be replaced with a new default: *Absent any evidence to the contrary*, a given fund investor should be considered similar to the other investors in the fund.

This Article posits that this modest inference represents the optimal default. However, it is merely that—a default rule that is easily waived. If there is any reason to infer that a given investor's governance priorities are unique, that inference trumps the default. Absent such contrary evidence, and given that a rational investor's decision to invest with an intermediary is orthogonal to support for its governance policies, the best evidence for an investor's views likely comes from their fellow investors. In the context of

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325. Delegated voting helps minimize rational apathy by distilling governance input down to the single action of delegation. It compares favorably to pure pass-through, with its thousands of decisions, and to polling, which, to be broadly useful, requires substantial investor input.

326. More precisely, if an investor is choosing between two funds with an identical expected return, it will only be rational to incur higher fees if both (1) the difference in governance costs exceeds the difference in fees and expenses between the two funds, as well as any taxes or other transaction costs incurred, and (2) this investor's asset allocation decision causally reduces such governance costs (i.e., these marginal votes were outcome-determinative). *See supra* Part IV.

327. In theory, although deeply impractical, an inference of support for an intermediary's governance policies could be drawn if we were to assume away all potential transaction costs and taxes and consider only identical funds charging identical fees.

delegated governance, this will often take the form of fund-level “mirror voting.”

*a. Mirror Voting*

There are two basic types of mirror voting: firm-level and fund-level. Firm-level mirror voting generally involves voting an investor’s proportionate equity interest in a given *firm* in the same proportion as *all other stockholders at the firm*.<sup>328</sup> In essence, by voting in an identical manner, it treats all other stockholders—hedge funds, pension funds, founders, etc.—as implicitly representative of a given fund investor’s interests. When implemented, firm-level mirror voting effectively makes intermediaries more passive with respect to governance, as it largely prevents the subject shares from impacting the firm-level voting outcomes. Its effect is similar to abstention (indeed, Vanguard has replaced its “Not Voting” policy with a firm-level mirror voting policy for the 2025 proxy season),<sup>329</sup> but it may help companies better meet quorum requirements and conduct business at their annual meetings.<sup>330</sup> Firm-level mirror voting is sometimes espoused by commentators and policymakers with a skeptical view of intermediary power—for instance, Congress recently considered proposed legislation called the “Investor Democracy is Expected Act” (often referred to as the “INDEX Act”), which included provisions for mirror voting in certain circumstances.<sup>331</sup> In sum, firm-level mirror voting essentially removes intermediaries (and their investors) from the corporate governance arena, and it allows firms to act as if the intermediated equity assets being voted in this manner simply did not exist.

In contrast, fund-level mirror voting (also referred to as “echo voting”) has very different effects.<sup>332</sup> This type of mirror voting involves voting an investor’s proportionate interest in the *fund* in the same proportion as *all other fund investors*.<sup>333</sup> In essence, it treats other investors in the fund—

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328. See Press Release, Vanguard, *supra* note 319 (describing Vanguard’s mirror voting policy “which votes an investor’s proportionate shares in approximately the same proportions as the votes cast by other shareholders”).

329. See *id.* (noting that the newly announced “Mirror Voting” policy was “replacing the ‘Not Voting’ Policy”).

330. See Griffith, *supra* note 22, at 1040 (noting that mirror voting “produces the same outcome as abstention without complicating portfolio companies’ processes for counting votes”).

331. See generally INDEX Act, S. 4241, 117th Cong. (2022).

332. See, e.g., FIDELITY INVS., PROXY VOTING GUIDELINES (2022), [https://www.fidelity.com/bin-public/060\\_www\\_fidelity\\_com/documents/Full-Proxy-Voting-Guidelines-for-Fidelity-Funds-Advised-by-FMRCo-and-SelectCo.pdf](https://www.fidelity.com/bin-public/060_www_fidelity_com/documents/Full-Proxy-Voting-Guidelines-for-Fidelity-Funds-Advised-by-FMRCo-and-SelectCo.pdf) [<https://perma.cc/BZ6D-3DNF>].

333. See, e.g., INV. CO. INST., OVERSIGHT OF FUND PROXY VOTING (2008), [https://ici-stage.ici.org/system/files/attachments/ppr\\_08\\_proxy\\_voting.pdf](https://ici-stage.ici.org/system/files/attachments/ppr_08_proxy_voting.pdf) [<https://perma.cc/X6ZG-3G6Z>] (stating that

rather than the larger group of hedge funds, pension funds, founders, and other shareholders—as implicitly representative of a given fund investor’s interests. As opposed to its firm-level counterpart, fund-level mirror voting affords participating investors continued influence on the governance of portfolio companies. Although it reduces discretionary governance input by intermediary agents, it magnifies the impact of investor input.

While fund investors are not homogenous, there is no reason to infer that they are more similar to other external shareholders than they are to one another. In fact, to the extent there is any measure of self-selection into funds based on risk tolerance, investment horizon, investment screening, portfolio composition, or numerous other factors, the opposite inference is more accurate. While inferring self-sorting by governance is irrational when considering identical investment products that differ only as to fees, it is *not* irrational to infer some degree of self-sorting into economically distinct investment assets. Thus, this Article argues that the optimal default proxy inference is that investors in the same fund are broadly similar to one another, but that this default inference should be easily negated by contrary investor input.<sup>334</sup>

One potential objection to such a policy involves the representativeness of participating investors. How similar are the views of participating investors to those of their silent counterparts? With low rates of investor participation, the answer is unclear. However, as participation in delegated voting increases, so too will its representativeness. In a recent survey, Vanguard found that two-thirds of its investors in employee retirement plans (and nearly six in ten other investors) indicated they would participate in delegated voting programs, with only a small minority (8%) of investors indicating no interest in selecting a delegate.<sup>335</sup> This does not seem unrealistic—given that somewhat less than one-third of retail investors vote,<sup>336</sup> and given that selecting a delegate is generally much easier and more efficient (i.e., it requires a single “standing” instruction for all portfolio companies rather than an individual determination of every ballot

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“this ‘echo voting’ approach . . . would merely amplify the votes already received from the other underlying fund shareholders. The adviser’s potential conflict is therefore extinguished by replicating the voting preferences expressed by the underlying fund’s other shareholders.”)

334. If more precise tailoring of investor characteristics and governance attributes is desired, funds might also experiment with bifurcating mirror voting for retail shareholders and institutional investors—i.e., calculating the percentages of delegated/undeleigated shares separately for each group and voting each group according to their respective proportions.

335. See Press Release, Vanguard, Vanguard Survey Highlights Strong Investor Interest in Proxy Voting Choice (Apr. 24, 2025), <https://corporate.vanguard.com/content/corporatesite/us/en/corp/who-we-are/pressroom/press-release-vanguard-survey-highlights-strong-investor-interest-in-proxy-voting-choice-042425.html> [<https://perma.cc/G6VB-549S>].

336. See Fisch & Schwartz, *supra* note 1, at 14.

item at every portfolio company every year<sup>337</sup>), we might reasonably anticipate that participation rates will surpass those of retail voting. Although educating investors on the availability and utility of delegated voting will take time, a strong argument exists for significant future increases in participation rates—and, in turn, the extent to which the views of participating investors are more broadly reflective of fund investors in general.

*b. Other Sources of Inference*

In addition to fund-level mirror voting, other sources of interest would also be applicable. While embracing proxy inference is most useful in the context of delegated voting, it could also enhance the utility of other types of investor input. For instance, in limited circumstances, intermediaries could potentially engage in proxy inference based on investment selection. While many investment decisions are too constrained (e.g., limited options in a retirement plan) or too generic (e.g., a decision to buy an S&P 500 index fund from a Big Three asset manager instead of a smaller, more expensive fund sponsor) to convey valid information about governance preferences, there are exceptions. This is particularly relevant in the context of certain “themed” investments, such as funds denominating themselves as “green,” “socially responsible,” “social impact funds,” or other ESG-related monikers. In limited circumstances such as these, an investment selection would convey enough information to allow valid inferences about fund investors’ governance preferences.<sup>338</sup> However, this concept is not generally applicable to most funds, or to the selection of a given asset manager, and thus this inference’s scope of effectiveness is much more limited than the inferences that are possible with delegated voting. Thus, while proxy inference is conceptually broader than (and not inherently dependent upon) delegated voting and fund-level mirror voting, this pairing represents the most broadly applicable method of implementation.

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337. For a thorough discussion of standing voting instructions, see generally Fisch, *supra* note 12.

338. See Press Release, Vanguard, Vanguard Unveils Data from Investor Choice Proxy Voting Pilot (Sept. 17, 2024), <https://corporate.vanguard.com/content/corporatesite/us/en/corp/who-we-are/pressroom/press-release-vanguard-unveils-data-from-investor-choice-proxy-voting-pilot-091724.html> [<https://perma.cc/5FKW-A5K3>] (stating that “Individual investors in the Vanguard ESG U.S. Stock ETF selected the third-party ESG policy (78.2%) at more than three-times the rate of the overall participating population (24.4%).”).

*c. Implementation*

This still leaves the question as to what input, precisely, should guide a policy of proxy inference. Indeed, the foregoing inference could be operationalized in numerous ways. Optimally, intermediaries would permit unconstrained (“open”) delegated voting. Upon receiving delegations, intermediaries would engage in fund-level mirror voting; all delegated shares would be voted per the respective delegate’s instructions, and all remaining shares would be voted in the same proportion. This approach—combining an open delegation policy with proxy inference—is synergistic. Proxy inference changes the default inference about investor intent to one that is more representative and economically rational, while an open delegation policy enhances the validity and accuracy of that inference by making sure it is based on a free and unconstrained choice. Any inference made without an open delegation policy is considerably weakened for the simple reason that an unconstrained choice in a competitive market conveys more and better information than a constrained choice in a duopolistic market. Thus, although distinct, these two policy proposals offer the highest utility when implemented in parallel.

This approach is designed to be flexible, and it can incorporate other policy variations as well. For instance, one such policy variant involves a hybrid with input solicitation.<sup>339</sup> This variation would impose an obligation to solicit investor input *for the purpose of assigning a delegate*. Rather than intermediaries utilizing investor input to inform their own largely discretionary voting, they would use the input to select a suitable delegate for their investors. This alternative would preserve an element of discretion for intermediaries and thus involve comparatively greater potential for agency costs and conflicts relative to investors choosing a delegate independently. This would be particularly important when advising whether investors should select an intermediary’s own voting policy instead of that of an external delegate. However, this hybrid method grants less discretion to intermediaries and reduces their agency costs to a greater degree than polling and “intermediation” alone.<sup>340</sup> Thus, this option could be a useful alternative for investors who would prefer to answer polling questions or who would benefit from guidance in selecting a particular voting policy or delegate.

Finally, it should also be noted that no part of the proposals herein would extinguish or “ban” proxy voting by intermediaries. For instance, Vanguard investors who like how it votes can still select Vanguard as their delegate

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339. See generally Fisch & Schwartz, *supra* note 1.

340. See generally *id.*

(and indeed, a substantial minority of participants in their pilot program have done just that).<sup>341</sup> However, the proposals do eliminate the false inference that investment in a fund offered by a given intermediary is coextensive with support for such intermediary's governance policies, instead shifting the default proxy inference to one that is more compatible with economically rational investor behavior.<sup>342</sup>

#### *D. Approaches to Financing*

What should the financial aspect of this policy proposal look like? A number of viable financing options exist. This Part explores three potential options: (1) voucher financing (discussed in Section VI.D.1), (2) a regulator-set fee minimum (discussed in Section VI.D.2), and (3) long-short incentive compensation (discussed in Section VI.D.3).

##### *1. Voucher Financing*

One approach to financing builds upon "voucher financing," a proposal by professors Stephen Choi and Jill Fisch.<sup>343</sup> Choi and Fisch propose a novel, issuer-funded mechanism for financing proxy advisory activity (and other services) that "delinks the source of funds from the authority to decide where the funds should go."<sup>344</sup> Essentially, their proposal would empower regulators to impose a mandatory fee on issuers that shareholders could then discretionarily allocate to proxy advisors and other service providers.<sup>345</sup> In the context of delegated voting, the mandatory fee would be imposed on asset managers (rather than issuers) and the power to allocate would be granted to fund investors (rather than shareholders). Regulators would have authority to set the level of such fees, which could initially be informed by the level of existing governance expenditures and increased (reduced) based

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341. See Press Release, Vanguard, *supra* note 338 (noting that 43% of investors selected the "Vanguard-Advised Funds Policy").

342. As discussed above, one possible objection to this policy proposal is the fear that investors who select a delegate will be unrepresentative of the investors as a whole. While such selection effects may exist to some degree, this objection is unpersuasive because (a) there is no evidence that asset managers' *existing* voting policies are any more representative of investors as a whole, (b) any inference of representativeness from assuming economically irrational behavior (i.e., selecting an intermediary based on governance policy rather than fees or other financial factors) is invalid, and (c) the potential for relatively high rates of participation will help mitigate such effects.

343. Stephen J. Choi & Jill E. Fisch, *How to Fix Wall Street: A Voucher Financing Proposal for Securities Intermediaries*, 113 YALE L.J. 269 (2003).

344. *Id.* at 314.

345. *Id.* at 318.

on the degree to which asset managers overinvest (underinvest) in governance.<sup>346</sup>

Adapting Choi and Fisch's voucher financing for the delegated voting context takes account of the dramatic changes to shareholding patterns in the two decades since its publication, particularly the growth and concentration of equity assets in the hands of intermediary agents. While the authors write that "the issuer is the best collectivizing agent with respect to the interests of its current and prospective investors," this role has arguably shifted to large intermediaries.<sup>347</sup> However, the benefits of harnessing the optimal collectivizing agent remain, including reducing management conflicts, solving collective action problems, increasing agent accountability,<sup>348</sup> and generating a "substantial increase in the number of independent intermediaries" as well as "a proliferation of new intermediary services for investors."<sup>349</sup> Thus, adapting voucher financing to the context of delegated voting represents a promising option for financing this Article's policy proposals.

## 2. *Mandatory Minimum*

Another alternative involves allowing funds to negotiate rates themselves, subject to a regulatory floor. Essentially, regulators would set a minimum rate for proxy advisory services, but proxy advisors and asset managers would be free to negotiate rates above the minimum based on factors such as investor demand, comprehensiveness of coverage, perceptions of quality, or additional services provided. Under this alternative, any eligible proxy advisor would have the option of receiving the minimum rate based on the volume of investors utilizing their services, but funds and advisors also retain the ability to negotiate outside of regulatory strictures. Thus, this option represents a blend of regulatory intervention and market forces.

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346. *See id.* at 319 ("In theory, the point at which the marginal value of an additional dollar of intermediary financing yields precisely a dollar of collective benefits should determine the aggregate level of funding required from issuers. Although calculating the precise amount of this allocation is beyond the scope of this Article, the initial allocation could be based on an estimate of present levels of issuer-based intermediary subsidization.").

347. *Id.* at 316.

348. *See id.* ("At the same time, the voucher proposal recognizes the problem with using managers and other nonshareholder decisionmakers to allocate intermediary funding, and restores intermediary accountability by giving allocation decisions to shareholders.").

349. *Id.* at 277.

### 3. *Long-Short Incentive Compensation*

Another potential alternative involves an incentive compensation scheme for proxy advisory services. This idea, explored in detail by Professors Asaf Eckstein and Sharon Hannes, involves devising an incentive scheme such that proxy advisors have “skin in the game” with respect to the equity values of the companies on which they advise.<sup>350</sup> Although Eckstein and Hannes primarily discuss their incentive compensation model in the context of voting on mergers and acquisitions, other incentive compensation structures are possible as well.<sup>351</sup> As Eckstein and Hannes note, incentive compensation structures are inherently more complex than a flat-fee model, and the precise contours of any such compensation agreement are best left to negotiation between intermediaries and advisors. However, if giving proxy advisors “skin in the game” would better incentivize value-enhancing investments in governance, incentive compensation structures could represent a Pareto improvement for proxy advisors (increased compensation), intermediaries (increased fees), and investors (increased equity value). Thus, long-short incentive structures may represent an important compensation model for a future, more competitive market for governance advice, but such models should result from private ordering rather than regulatory fiat.

#### *E. Benefits and Second-Order Effects*

This proposal presents advantages over both the status quo and alternative proposals in a number of corporate governance dimensions. The following Sections explore the impact of the proposed policy prescriptions with respect to (1) reducing governance-related agency costs of intermediaries, (2) overcoming investor apathy, and (3) systemic benefits for the corporate governance ecosystem.

##### *1. Governance Costs*

First, as outlined in Parts II–V, existing and proposed constraints on the governance-related agency costs of intermediaries are largely ineffectual. Even the most restrictive legal constraint on the ends of corporate governance (i.e., shareholder wealth maximization as the sole maximand) collapses into subjectivity, to say nothing of more capacious ends such as stakeholderism, portfolio primacy, or shareholder “welfare”

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350. See generally Eckstein & Hannes, *supra* note 95.

351. See *id.* at 824–26.

maximization.<sup>352</sup> Market constraints on the ends of corporate governance proved similarly ineffective, as financial incentive alignment at the fund level is dramatically weaker than what would be acceptable at the firm level.<sup>353</sup> This is true both for intermediaries at an entity level, as financial incentives to engage in informed voting are generally low in an absolute sense, and at an individual level, as key governance decisionmakers employed at the largest intermediaries receive compensation largely decoupled from investment performance.<sup>354</sup> Market constraints on the means of governance are similarly weak. Although investors can, in theory, self-select into and exit out of funds with voting records and engagements (the basic “means” by which intermediaries engage in governance), such self-selection and exit is virtually always economically irrational.<sup>355</sup> Finally, legal constraints on the means of governance, typically in the form of input solicitation from investors, are also largely ineffective. Such policies suffer key weaknesses from both the subjectivity of generalized maximands and investor’s apathy and lack of expertise with respect to more specific input.<sup>356</sup> While there may be certain “goldilocks” questions that are specific enough to meaningfully constrain intermediary voting, interesting and salient enough to overcome investor apathy, and for which overcoming such apathy is actually valuable (i.e., subjects on which investors possess valuable expertise), simultaneously meeting these three requirements will be relatively rare. Thus, legal constraints on means, while potentially useful, are far from a comprehensive solution to the agency costs of intermediaries. Ultimately, none of the potential strategies for constraining agency costs along legal or market means and ends proves sufficiently effective.

Not only are the strategies discussed above largely ineffective, they are also structurally inferior. Agency costs can be reduced, but they cannot be completely eliminated in the aggregate. It follows that additional agents will, in the aggregate, generate additional agency costs. As a result, strategies that impose multiple layers of agency and intermediation are, as a general proposition, structurally inferior to those that do not. Although this does not imply that every instantiation is inferior, it does present a thumb on the scale in favor of disintermediation. Moreover, while each governance strategy that utilizes multilayered agency or intermediation requires its own unique cost-benefit analysis, the analysis in Parts II–V strongly suggests that the outcome in most cases will be negative—that is, strategies utilizing

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352. *See generally supra* Part II.

353. *See generally supra* Part III.

354. *See generally supra* Part III.

355. *See generally supra* Part IV.

356. *See generally supra* Part V.

multiple layers of agency appear to generate additional agency costs, as the theory predicts.<sup>357</sup>

Another structural benefit of delegated voting is that it is capable of granting investors control over all aspects of governance—the means and the ends—while most other proposals address only their respective parts. For instance, an open delegation policy allows easy self-selection into and exit out of proxy advisors. An investor who wants to change the means by which wealth maximization is pursued in the governance of their portfolio (e.g., one who comes to believe that the cost of carbon will negatively impact their investment return) could easily delegate governance authority to a different proxy advisor that shares their perspective. Alternatively, an investor facing a major financial shortfall or unfunded liability could shift from incorporating charitable or altruistic goals in their governance decisions to the end of wealth maximization. While such changes would be difficult, expensive, or potentially impossible under many alternative proposals, the proposals herein would make such governance changes easy to accomplish, without incurring tax liability and with minimal transaction costs.

## 2. *Overcoming Apathy*

Another key benefit of the policy prescriptions herein is their potential to mitigate investor apathy. First, delegated voting helps minimize rational apathy by distilling governance input down to a single decision—namely, to whom governance authority should be delegated. This presents a much lower barrier to governance participation relative to pure pass-through voting, with its thousands of decisions, and even relative to polling, which, to be useful for more than a handful of issues, requires substantial investor input. By condensing investor input into the single act of delegation, it lowers the cost in time and expertise required to make more numerous governance decisions. It also increases the benefits of doing so, as delegated governance is more effective at influencing governance behavior than any of the other weak legal and market constraints on means and ends.

Second, proxy inference magnifies the impact of investor input and increases the incentives to choose involvement over apathy. More specifically, because each investor's choice of delegate proportionately influences the governance of all shares for which no input was received, the impact of such input is increased, often dramatically so. As a result, under this proposal, the greater potential impact of shareholder input generates a

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357. See *supra* Parts II–V and accompanying text.

corresponding increase in incentives for investors to provide such input. Thus, the combination of delegated voting and proxy inference will, from the perspective of an investor, both minimize the effective cost of participating in governance and increase the benefits that such an investor can realize from such participation, diminishing the investor's incentives to remain apathetic.

Finally, an open delegation policy would further decrease investor apathy. First, additional choice would allow investors to achieve greater alignment between their own governance priorities and those of the delegate they select. For instance it is possible that investors are simply not moved to participate by the ISS Global Board-Aligned Policy, the ISS Catholic Faith-Based Policy, or the ISS Socially Responsible Investment Policy—the three existing voting options that ISS offers to BlackRock clients.<sup>358</sup> In this way, a lack of suitable options due to the current “closed” proxy system could be significantly improved by implementing an open proxy delegation policy, which would spur new entrants into the duopolistic proxy advisory market. In addition to increasing the breadth of offerings, removing the barriers to open delegation would shift the market to be more-investor focused, as proxy advisors would compete to meet the needs of investors rather than the compliance goals of intermediaries. Finally, a more competitive market for proxy advisory services would present new opportunities for investors and incentivize new policy innovations for market participants, as well as spawning numerous new avenues of inquiry for academics.

One challenge is that participation rates are currently low. Vanguard reported its overall rate of investor participation in its “Investor Choice” pilot program at over 2%, and investors directly investing with Vanguard had a participation rate of approximately 4%.<sup>359</sup> However, there are numerous reasons to suspect that these rates will increase over time. First, these pilot programs are still quite new and relatively unfamiliar to most investors. For instance, Vanguard first launched its delegated voting program shortly before the start of proxy season in 2023,<sup>360</sup> and BlackRock first opened its program to retail investors in 2024.<sup>361</sup> Prior to these launches, these fund investors had no right to participate in proxy voting,

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358. See BLACKROCK, *supra* note 326.

359. See *Vanguard Investor Choice Fact Sheet*, VANGUARD (2024), [<https://perma.cc/HSG5-P5MR>] (only available by archive link).

360. See *id.*

361. See Joud Abdel Majeid & Rachel Aguirre, *BlackRock Has Expanded Proxy Voting Choice to Millions of U.S. Retail Shareholder Accounts*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Apr. 1, 2024), [<https://corpgov.law.harvard.edu/2024/04/01/blackrock-has-expanded-proxy-voting-choice-to-millions-of-u-s-retail-shareholder-accounts/>] [<https://perma.cc/G9FW-N88P>].

and it will take time to complete effective investor outreach and education with respect to delegated voting. Put simply, investor behavior will not change overnight, but interest in delegated voting is increasing.<sup>362</sup> Second, even the initial limited participation has influenced an economically significant amount of capital. For instance, at BlackRock alone, around \$600 billion in equity assets participated in a delegated voting pilot program during 2023.<sup>363</sup> Thus, because of the massive scale of the Big Three's assets under management, even seemingly small percentages of investor participation can be significant in an absolute sense. Third, as discussed in the preceding paragraph, investor participation will continue to improve as the programs themselves improve—an open market for proxy advisory services will allow investors to choose a delegate that better matches their governance priorities, enhance competitiveness, and shift the focus to serving investors rather than intermediaries. Fourth, in addition to such substantive policy changes, delegated voting programs will also experience technical improvements. Artificial intelligence tools that help intermediaries and investors clarify and generalize their voting preferences already exist—and are rapidly improving.<sup>364</sup> Fifth, proxy inference makes even limited input valuable. Investors who vote give us important insights into the preferences of non-voting investors.<sup>365</sup> Sixth, adopting proxy inference will also shift the cost-benefit calculus for investor participation in governance, helping overcome apathy by magnifying the impact of governance participation.

Thus, as delegated voting initiatives improve and mature, investor participation will increase. However, while additional investor input is generally desirable, proxy inference is specifically designed to address the unavoidable reality of limited investor input. Ultimately the policy

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362. See John Galloway, *Investor Choice*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Oct. 9, 2024), <https://corpgov.law.harvard.edu/2024/10/09/investor-choice/> [<https://perma.cc/NTV5-PZZE>].

363. See Majeid & Aguirre, *supra* note 361 (“As of the end of 2023, clients representing \$598 billion of eligible index equity assets had chosen to participate in BlackRock Voting Choice.”).

364. See generally Chen Wang, *Outsourcing Voting to AI: Can ChatGPT Advise Index Funds on Proxy Voting Decisions?*, 29 FORDHAM J. CORP. & FIN. L. 113 (2023); see also Press Release, As You Sow, New ESG+ Proxy Voting Web-App to Empower Retail Investors for Proxy Season 2023 (Apr. 27, 2023), <https://www.asyousow.org/press-releases/2023/4/27/esg-proxy-voting-web-app-empower-retail-investors-proxy-season-2023> [<https://perma.cc/RCG9-KLLM>] (describing the technology behind the Iconik proxy voting platform, which rapidly learns and implements an investor's governance preferences).

365. See Robert J. Jackson, Jr. & Jonathon Zytneck, *Individual Investor Ideology* 4–5 (Eur. Corp. Governance Inst., Working Paper No. 1097/2025, 2025), <https://ssrn.com/abstract=5054952> [<https://perma.cc/45JT-VCVU>] (discussing inferences in the context of individual investor voting, and stating that “[i]ndividual investor preferences are a matter worthy of study” both because “their votes impact voting outcomes at firms they own” and because “the votes of individuals who directly own stocks serve as a window into the preferences of all individual investors, including non-voting individuals and individuals who own institutional investors”).

proposals herein benefit investors by lowering the governance-related agency costs of intermediaries, decreasing investor apathy, enhancing the voice of the investors as economic principals, and facilitating more rational inferences by intermediaries.

### 3. *Systemic Implications*

In addition to the benefits accruing to investors, this Article's policy proposals have important systemic implications for the broader corporate governance ecosystem and beyond. Importantly, these benefits represent an independent justification for adopting the foregoing proposals. While investors' interests are often the lodestar for corporate governance policy proposals, countless other constituencies and stakeholders are often downstream of changes in governance policies. The Sections that follow discuss the systemic and public policy implications of open delegation and proxy inference.

#### a. *Concentration of Corporate Ownership*

Investment assets have become heavily concentrated in the hands of just a few institutional asset managers. Professor John Coates has termed this issue as the "Problem of Twelve," where roughly twelve individuals may soon wield governance power over virtually all large public corporations.<sup>366</sup> This concentration of power has important consequences both for the corporate governance system and the global economy, potentially inducing layoffs, reducing corporate investment, "increas[ing] the risk of bribery, mass torts, fraud or antitrust violations" through "[r]educed budgets for compliance," and granting large intermediaries the power to influence "the incidence and severity of externalities and rent-seeking."<sup>367</sup>

The policies in this Article could substantially mitigate the Problem of Twelve by recoupling governance authority and economic ownership. In combination, open delegation and proxy inference would remove considerable discretionary governance authority from intermediaries. A portion of the nominal Twelve's power would be transferred to their investors, who would have authority to choose their own delegates and voting plans. Today's voting choice plans theoretically allow such transfers,

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366. John C. Coates, *The Future of Corporate Governance Part I: The Problem of Twelve 2* (Harv. Pub. L. Working Paper No. 19-07, 2018), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3247337](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3247337) [<https://perma.cc/6G3H-YZ2H>] ("[C]ontrol of most public companies – that is, the wealthiest organizations in the world, with more revenue than most states – will soon be concentrated in the hands of a dozen or fewer people.").

367. *Id.* at 19.

but their “closed” platforms and the current proxy advisor duopoly mean that power is often merely *shifted to other members of the Twelve*, rather than actually reducing the group’s collective power. Allowing open delegation would facilitate innovation, competition, and new entrants into this space, which would effectively reduce the power of the mass corporate governors. This would deconcentrate power to a far greater extent than the current approach, which largely facilitates modest redistribution of power amongst members of the Twelve. Additionally, it would do so while preserving beneficial economies of scale at large asset managers that would be lost with more dramatic solutions to Coates’s problem, such as antitrust remedies to break up the large asset managers,<sup>368</sup> and without limiting full investor diversification.<sup>369</sup>

*b. Product Market Competition*

Common ownership by large intermediaries may also reduce competition in product markets. If a firm’s largest shareholders are also the largest shareholders of its competitors, the incentives to compete may be blunted.<sup>370</sup> The result is that prices for various goods and services may increase, ultimately harming consumers.<sup>371</sup> Although there is no clear consensus on the precise mechanisms through which common owners exert their influence, one potential mechanism is governance power. To the extent firm managers respond to (likely implicit) governance pressure from large, cross-owning intermediaries to compete less than vigorously, reducing the concentrated power of such intermediaries will also reduce the negative effects of common ownership on product markets.

*c. Labor Market Competition*

Large, concentrated shareholder power may also harm American labor interests. Professors Zohar Goshen and Doron Levit discuss the potential tradeoffs between “strong governance” by concentrated owners and the interests of American workers.<sup>372</sup> They link common ownership of equity assets with decades of wage stagnation and the declining share of economic

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368. See Zohar Goshen & Doron Levit, *Agents of Inequality: Common Ownership and the Decline of the American Worker*, 72 DUKE L.J. 1 (2022).

369. See Eric A. Posner, Fiona M. Scott Morton & E. Glen Weyl, *A Proposal to Limit the Anticompetitive Power of Institutional Investors*, 81 ANTITRUST L.J. 669, 678 (2017) (discussing a proposal to restrict large asset managers from investing in more than a single firm in a given industry).

370. See, e.g., José Azar, Martin C. Schmalz & Isabel Tecu, *Anticompetitive Effects of Common Ownership*, 73 J. FIN. 1513 (2018).

371. *Id.*

372. See Goshen & Levit, *supra* note 368.

surplus allocated to labor.<sup>373</sup> The proposals herein would weaken Goshen and Levit's hypothesized "strong governance" by effectively "breaking up" the Big Three's governance power, rather than the Big Three themselves. As a result, these policy proposals may achieve the goals of benefiting labor interests while imposing lower costs than resorting to antitrust to break up the Big Three asset managers in a more literal sense.

*d. Asset Managers as Regulators*

Asset managers have come to occupy a quasi-regulatory function in modern capital markets. Because the largest intermediaries own significant share blocs in essentially every large public company, they have effectively become the "arbiters of corporate law controversies and the framers of market-wide governance standards."<sup>374</sup> To the extent such regulations represent broadly beneficial actions, this dynamic may be beneficial. For instance, Professors Yaron Nili and Kobi Kastiel suggest that the Big Three asset managers play an important role in promoting beneficial corporate governance characteristics at large firms.<sup>375</sup> However, Professor Dorothy Lund critically assesses this "novel privatization dynamic," noting that the quasi-regulatory proclamations of large intermediaries may not further the public interest, and that they are lacking in democratic accountability and government oversight.<sup>376</sup> Ultimately, reducing the concentrated power of large intermediaries will lessen their power as *de facto* regulators, which will likely facilitate greater governance heterogeneity and private ordering at public companies.<sup>377</sup>

## CONCLUSION

Modern shareholder democracy is now the province of a concentrated cadre of intermediary agents. These agents control assets rivalling the gross domestic product of the world's largest economies on behalf of their investors. Despite this vast governance power, market dynamics are such that these agents often face weak financial incentives to exercise their power in an informed manner. In addition to the failure of market-based incentives, legal constraints also fail to substantially limit the governance discretion of

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373. *Id.*

374. Griffin, *supra* note 293, at 954.

375. Kastiel & Nili, *supra* note 110, at 847 ("[T]he Big Three are more likely to engage with companies within the S&P 500 than with any other companies").

376. See Lund, *supra* note 41, at 78.

377. See generally Lund, *supra* note 25 (discussing the "governance gap" between large and small public companies as a function of the power of large asset managers to impose uniform governance standards).

intermediaries. Although they face powerful incentives to vote in most circumstances, intermediaries presently possess the discretion to do so without regard to their investors' interests.

Part I of this Article explored this tension in the context of the "mass corporate governance conundrum." This Part analyzed the dynamics that led to the current corporate governance status quo. It explored the history of the effective mandate to vote, both under the regulatory ambit of the Department of Labor and the Securities and Exchange Commission. It also laid out the governance challenges of modern, hyper-diversified investing, which may require voting on well over 100,000 individual ballot items while maintaining extraordinarily low fee levels. Moreover, it highlighted that the majority of ballot items at the majority of firms will be low-value votes from the perspective of intermediaries. One of the most fundamental consequences of delegating governance power to intermediary agents is that they frequently lack intrinsic motivation to pursue optimal voting. And yet, they face what is essentially a "comply or explain" regulatory mandate to vote in most circumstances. The ultimate result of this odd pairing of semi-mandatory voting with, quite commonly, no meaningful legal or market incentive to vote *well* is what this paper has termed mass corporate governance: high-volume, low-value, non-firm-specific, and compliance-oriented governance activity.

Part II explored the legal constraints on the ends of mass corporate governance. It found that the "best interests" standard grants mass corporate governors an incredible amount of latitude with respect to voting and other governance activities. It explored the most stringent (and most common) maximand of shareholder wealth maximization, and it concluded that the subjectivity inherent in determining what, precisely, maximizes shareholder value allows intermediaries to take virtually any position they may desire on almost any governance issue. Exploring alternative maximands, such as stakeholderism or shareholder welfare maximization, only heightens intermediary's discretion. Ultimately, barring the most egregious conflicts of interest, legal constraints on the ends of corporate governance do very little to reduce the governance costs imposed by intermediaries.

Part III considered market constraints on the ends of mass corporate governance. The basic intuition of this Part was that if the incentives of all parties are properly aligned, legal constraints may be largely unnecessary. However, it found that these incentives were largely absent, both at the individual level (such as executives and stewardship team members at the intermediary) and at the entity level (i.e., the corporate interests of the intermediary itself). While especially significant ballot items at very large firms may produce meaningful incentives for some of the very largest

intermediaries, the overwhelming majority of governance items on which intermediaries are asked to weigh in generate insufficient (and often negative) financial incentives. Thus, market constraints on ends will not meaningfully limit the agency costs of intermediaries.

Part IV analyzed market constraints on the means of mass corporate governance, including the extent to which investors can self-select into desirable governance arrangements and exit undesirable arrangements. It found that, in practice, the ability of investors to self-select and freely exit is often highly constrained. Investors face significant financial incentives to select intermediaries based on factors other than their proxy voting policies or other governance activity. Moreover, even in the event investors choose to prioritize governance above such other factors (e.g., for ideological rather than economic reasons), intermediaries may freely change their future voting behavior (as they have in the past), leaving the investor effectively locked-in. Ultimately, market forces also fail to adequately constrain the means by which intermediaries influence corporate governance.

Part V explored legal constraints on the means of mass corporate governance. It first considered general proposals to increase the resources invested in corporate governance activity by intermediaries (the “means” by which they engage in such activity) without altering their ends. However, there are risks to mandating higher spending by agents in an attempt to solve agency costs. Enhancing expenditures in this manner would not affect the weak incentive alignment facing intermediaries or their underlying legal obligations, and there are ultimately no guarantees that such expenditures would be utilized appropriately. Additionally, this Part considered more specific constraints on means, such as requiring intermediaries to solicit and act upon governance-related input from their investors. While input solicitation might be a useful strategy in certain contexts (e.g., assisting in delegate selection), it fails as a broad-based solution to the agency costs of intermediaries. On the one hand, while precise input could theoretically constrain agency costs, it would face potentially insurmountable obstacles with respect to investor apathy and expertise. On the other hand, the inherent collapse into subjectivity faced by high-level investor input would simply perpetuate intermediaries’ current governance autonomy, thereby doing nothing to reduce agency costs. Ultimately, legal constraints on the means of governance also failed to constrain intermediary behavior.

Finally, Part VI presented this Article’s policy proposals. It first framed the basic choice of allocating governance authority along two axes: whether principals or agents possessed governance authority, and whether such authority was delegated or direct. It then explored the benefits of principal-directed delegated voting. It argued that, rather than fighting to constrain

governance activity by agents, we should instead let principals choose to whom they wish to grant governance discretion. To facilitate this grant of discretion, it advocated a policy of open proxy delegation, where intermediaries are generally forbidden from gatekeeping investors' selection of delegates. Additionally, it proposed changing the default inference of investor intent. While the current default inference holds that governance priorities are inferable from an investor's choice of intermediary, the fact that no economically rational investor chooses an intermediary based on its governance suggests that this inference is entirely invalid. Instead, intermediaries should treat investor input, broadly conceived, as the best evidence of investor intent. When investors in the fund select delegates, that should inform an intermediary's understanding of the proportional interests of the fund's other investors. While traditional firm-level mirror voting infers that investors are best represented by the voting behavior of the external, non-fund investors in a given firm, *fund-level* mirror voting infers that investors in the same fund are broadly similar to one another. Although fund investors are not homogenous, there is no reason to infer either that they are more similar to other external shareholders than they are to one another, or that they made an economically irrational choice to invest with a given intermediary based on governance priorities rather than fees or other factors. Thus, the optimal default is that, absent any evidence to the contrary, a given fund investor should be considered similar to the other investors in the fund.

This Article has important policy ramifications for scholars and policymakers. The proposals herein will decrease the governance-related agency costs of intermediaries, enhance investor choice, mitigate investor apathy, and generate systemic benefits to the corporate governance ecosystem and economy at large. Additionally, its second-order effects may help mitigate the potential anticompetitive impact of common ownership, benefiting both American workers and consumers, as well as facilitating more robust private ordering. Finally, it raises crucial new lines of inquiry for academics, legislators, and regulators with respect to the unique, dynamic potential of a world that transcends mass corporate governance.