
CORPORATE TECHNOCRACY: ESG GOVERNANCE BEYOND SHAREHOLDER DEMOCRACY OR MANAGERIALISM

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This Article advances a novel paradigm for governing corporate ESG that accounts for the principal-agent challenges undermining prevailing proposals. ESG (Environmental Social Governance) advocates typically advance one of two corporate governance paradigms for delivering on their objectives—shareholder democracy or managerialism. Shareholder democracy seeks to expand shareholder involvement in defining and monitoring corporate ESG agendas. Managerialism claims broader discretion for executives to govern in the interest of a corporation’s stakeholders. Both paradigms fail to account for novel agency challenges generated by prosocial corporate purpose, leaving unresolved core concerns about ESG accountability and efficacy.

This Article offers an alternative to the two prevailing ESG governance paradigms and argues that “corporate technocracy” can account for the novel agency challenges generated by ESG, while addressing the structural and legal shortcomings of both shareholder democracy and managerialism. Technocracy refers to rule by technical experts. It emphasizes institutional accountability, promotes legibility and measurability of corporate purpose, and characterizes shareholders and stakeholders as an information source for defining ESG materiality, particularly for emerging or controversial issues. Technocracy

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depoliticizes both managers' and shareholders' role in defining ESG, relegating managers to the role of administrators rather than statesmen, and shareholders to the role of informational satellites rather than political subjects. Technocracy offers a framework for ESG governance that is consistent with controlling Delaware corporate law doctrine and federal securities law. This Article offers a way beyond the political dogma that plagues contemporary ESG debates and advances a normatively defensible and practically administrable paradigm for ESG governance.

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I. INTRODUCTION

The ESG wars rage on among political ideologues and corporate practitioners alike.¹ A debate over corporate

¹ See, e.g., Brett Samuels, *Biden Issues First Veto, Rejecting Bill to Reverse ESG Rule*, THE HILL (Mar. 20, 2023), <https://thehill.com/home-news/3883293-biden-issues-first-veto-rejecting-bill-to-reverse-esg-rule/> [<https://perma.cc/5FYU-6DA6>]; Warren Rojas, *Republicans Stoke 2024 Culture Wars by Attacking Biden's Socially Conscious Investing Rule*, BUS. INSIDER (Mar. 1, 2023), <https://www.businessinsider.com/republicans-attack-biden-esg-investing-culture-wars-2024-election-2023-3> [<https://perma.cc/DHU9-85DN>]; Brooke Masters & Patrick Temple-West, *Vivek Ramaswamy's Fund Manager Strive Sticks to its 'Anti-Woke' Mission*, FIN. TIMES (Feb. 24, 2023), <https://www.ft.com/content/c7ccc5ea-3e8f-49a1-b250-31365f4f33e0> [<https://perma.cc/9BYT-SWP7>]; Mark Niquette & Kevin Crowley, *Pence Rips ESG Investing as Injecting Left-Wing Politics Into Business*, L.A. TIMES (May 10, 2022), <https://www.latimes.com/business/story/2022-05-10/pence-rips-esg-investing> [<https://perma.cc/X7KN-N792>]; Andrew Edgecliffe-Johnson, *The War on 'Woke Capitalism'*, FIN. TIMES (May 27, 2022), <https://www.ft.com/content/e4a818e5-4039-46d9-abe0-b703f33d0f9b> [<https://perma.cc/A32T-2AAS>]; David A. Katz & Laura A. McIntosh, *Politics and Purpose in Corporate America*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Oct. 30, 2020), <https://corpgov.law.harvard.edu/2020/10/30/politics-and-purpose-in-corporate-america/> [<https://perma.cc/UL9P-D6MN>]; Mind Your Own Business Act of 2021, S. 2829, 117th Cong. (2021), <https://www.congress.gov/bill/117th-congress/senate-bill/2829> [<https://perma.cc/5KKB-NUHT>]; Protection Act of

Environmental, Social, and Governance (ESG) agendas conjures familiar terms of a long-running concern with corporate purpose: shareholder profit versus stakeholder welfare.² More fundamentally, however, the debate over corporate purpose implicates competing accounts of corporate control. Even those who begin from a shared normative premise—that corporations *should* pursue prosocial ends—fervently disagree about *who* should set a corporation’s ESG agenda, how they

2021, S. 530, 117th Cong. (2021), <https://www.congress.gov/bill/117th-congress/senate-bill/530> [<https://perma.cc/YG2A-BFXW>].

² A dominant narrative among ESG critics is that it is merely cover for mismanagement and waste by expanding managers’ protected discretion without providing metrics to evaluate their performance. *See, e.g.*, Sanjai Bhagat, *An Inconvenient Truth About ESG Investing*, HARV. BUS. REV. (Mar. 31, 2022) <https://hbr.org/2022/03/an-inconvenient-truth-about-esg-investing> [<https://perma.cc/9QZQ-6M85>] (“There’s also some evidence that companies publicly embrace ESG as a cover for poor business performance.”). Hedge fund manager Paul Singer characterizes “stakeholder supremacy” as a ruse masking poor managerial performance. Paul Singer, *Of Owners and Ownership*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Nov. 25, 2021), <https://corpgov.law.harvard.edu/2021/11/15/of-owners-and-ownership/> [<https://perma.cc/7FUZ-HJCS>]. Senator Marco Rubio argues that ESG and other forms of corporate social and political activity only serve as woke-washing and provide cover for managerial rent-seeking, while Senate Minority Leader Mitch McConnell admonishes that in promoting social activism, corporate America is acting like “a woke parallel government.” *See* Ellen Meyers, *Rubio, Republicans Step Up Attacks on Corporate Embrace of ESG*, ROLL CALL (Sept. 30, 2021), <https://rollcall.com/2021/09/30/rubio-republicans-step-up-attacks-on-corporate-embrace-of-esg/> [<https://perma.cc/9DWZ-6WQC>]; Burgess Everett, *McConnell: Big Business Acting Like ‘Woke Parallel Government’*, POLITICO (Apr. 5, 2021), <https://www.politico.com/news/2021/04/05/mcconnell-corporate-america-woke-parallel-government-479042> [<https://perma.cc/5FTR-2DW9>]. The SEC’s Republican members, Commissioner Hester Pierce and former Commissioner Elad Roisman, have opposed the SEC’s Biden-era support for mandatory ESG disclosure, arguing that it privileges stakeholders’ voices over shareholders’ financial interests. Hester M. Peirce, Commissioner, *My Beef with Stakeholders: Remarks at the 17th Annual SEC Conference*, Center for Corporate Reporting and Governance, SEC (Sept. 21, 2018), <https://www.sec.gov/news/speech/speech-peirce-092118> [<https://perma.cc/N97F-PRUC>]; Hester M. Peirce, Commissioner, *Markets, Morality, and Mobsters: Remarks at the 18th Annual Corporate Governance Conference*, SEC (Aug. 27, 2020), <https://www.sec.gov/news/speech/peirce-markets-morality-mobsters-2020-08-27> [<https://perma.cc/8KCG-T5N6>].

should define and implement it, and within what limits they are legally permitted to do so.³ These disagreements have important legal and governance implications concerning managers and directors' fiduciary duties of care and loyalty, the domain of shareholder voice, the function of shareholder suffrage, and the scope of shareholder minority protections in the context of corporate activism.

The disagreement over ESG governance stems from a more fundamental challenge: ESG destabilizes the terms of a traditional agency relationship between shareholder principals and managerial agents that defines contemporary corporate governance and the corresponding allocation of power among shareholders, managers, and directors. Generally, matters concerning a corporation's essential structure and purpose are reserved to its shareholders, while decisions concerning ordinary business operations are ceded to its managers. ESG confounds this distinction, representing a combination of strategic and operational objectives, and normative and financial rationales. Notions like sustainability, diversity, or political responsibility can be defined in myriad ways and for different ends. Who gets to decide these goals, to what end, and with what checks and limits?

Two main positions respond to these questions. The first position, shareholder democracy or shareholder pluralism, claims for shareholders greater power to define and oversee corporate ESG. The second position, managerialism or stakeholderism, grants managers an expanded scope of protected discretion to account for the interests of a broad range of corporate stakeholders. Both paradigms introduce novel agency challenges to an existing corporate governance structure premised on shareholder principals, managerial agents, and an end goal of profit generation. Corporate law scholars have only obliquely addressed the contradictions and tensions that

³ For example, Marty Lipton, Colin Mayer, and Leo Strine, among others, advance that boards of directors are best positioned to identify stakeholders and mediate among them, *see infra* notes 56–58, while Cathy Hwang, Yaron Nili, and Roberto Tallarita, among others, argue that it is shareholders who are best positioned to lead corporate ESG efforts. *See infra* notes 63–64.

ESG presents for this default corporate governance paradigm, and they have largely failed to address these challenges in the terms of agency theory.

This Article steps beyond the traditional terms of a corporate purpose debate that has waged on for nearly a century, between supporters of shareholder profit maximization on the one hand and advocates for stakeholder welfare on the other. Instead, it acknowledges ESG as a *fait accompli*, evidenced by a multi-trillion-dollar investment industry⁴ and

⁴ Investors are increasingly choosing to put their savings in funds that consider ESG as part of their portfolio selection; ESG investments have experienced massive growth in the last decade to reach \$17 trillion dollars of U.S. assets under management in 2020, comprising a third of the total investment market. *ESG Assets Rising to \$50 Trillion Will Reshape \$140.5 Trillion of Global AUM by 2025, Finds Bloomberg Intelligence*, BLOOMBERG (July 21, 2021), <https://www.bloomberg.com/company/press/esg-assets-rising-to-50-trillion-will-reshape-140-5-trillion-of-global-aum-by-2025-finds-bloomberg-intelligence/> [<https://perma.cc/JA7L-8UJK>]. Together with advocacy groups, shareholders lobby corporate leaders to advance their social agendas by submitting proxy proposals on political, social, environmental, and governance matters, by demanding expanded disclosures on ESG, and by filing shareholder derivative suits seeking to hold directors and officers accountable for delivering on their ESG commitments. *See e.g., Shareholder Advocacy, AS YOU SOW*, <https://www.asyousow.org/shareholder-advocacy> [<https://perma.cc/V2RS-G5U8>] (last visited Oct. 26, 2023); Jessie K. Liu, Susan L. Saltzstein & Tansy Woan, *Shareholder Suits Demand More Progress on Diversity*, SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP (Apr. 13, 2021), <https://www.skadden.com/insights/publications/2021/04/the-informed-board/shareholder-suits-demand-more-progress> [<https://perma.cc/84YX-VA6M>]. Investors leverage their market power to engage with corporate managers on ESG and urge them to take stakeholder interests into account in furthering the sustainable pursuit of profit. The most notable is Larry Fink, CEO of the world's largest money manager, BlackRock. In recent years, Fink's annual letters to shareholders have embraced questions of purpose and stakeholders. *See, e.g., Larry Fink, Larry Fink's 2019 Letter to CEOs: Purpose and Profit*, BLACKROCK, <https://www.blackrock.com/corporate/investor-relations/2019-larry-fink-ceo-letter> [<https://perma.cc/UQG3-XALJ>] (last visited Oct. 26, 2023). Other investors, like the activist fund Engine No. 1, center ESG performance in their campaigns against incumbent corporate boards. *See, e.g., George Casey, Scott Petepiece & Lara Aryani, Recent Shareholder Activism Trends*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Nov. 29, 2021), <https://corpgov.law.harvard.edu/2021/11/29/recent-shareholder-activism-trends/> [<https://perma.cc/TY7D-FB65>]. More

mainstreamed managerial rhetoric, and focuses on the corporate political economy advanced by distinct ESG governance proposals. It argues that even those who agree on ESG as an end hold deeply conflicting visions of how it should be achieved, and that the two prevailing proposals suffer from fundamental principal-agent challenges. This Article proposes an alternative governance paradigm to shareholder democracy and managerialism in the form of a corporate technocracy. It argues that ESG governance by experts with technical specialization accounts for novel principal-agent challenges provoked by a more nuanced pursuit of corporate purpose while defusing the ideological polarization of the contemporary ESG debate.

In this Article, I identify and address the agency problems of ESG governance and make a case for “corporate technocracy” as an alternative to both shareholder pluralism and managerialism. I advance that approaching ESG governance through a corporate technocracy can overcome the agency costs generated by a pursuit of corporate purposes beyond profit that the two current paradigms fail to account for. I argue that technocracy offers a framework for acknowledging, interrogating, and managing the political aspects of ESG governance while tempering them through the logic of materiality and the constrained mandate of technical expertise. The corporate technocracy emphasizes institutional capacity and technical expertise which render corporate purpose legible, and therefore measurable and administrable. It remains consistent with Delaware corporate law doctrine and federal securities law. Technocracy offers a way to redeem the promises of managerialism while also allowing a role for shareholders in promoting prosocial corporate decision-making.

I begin in Part II by providing conceptual clarity for a muddled discussion of ESG. I set out a taxonomy of “ESG” along

mainstream activists like Elliott Management and Third Point are highlighting ESG to win the support of big funds for their campaigns. Corrie Driebusch, *The Next Wave in Shareholder Activism: Socially Responsible Investing*, WALL ST. J. (Mar. 8, 2020), <https://www.wsj.com/articles/the-next-wave-in-shareholder-activism-socially-responsible-investing-11582892251> [on file with the Columbia Business Law Review].

the dimensions of purpose and power. I argue that ESG implicates a claim about corporate purpose (ends) and a claim about corporate control (means). The two claims combined determine corporate political economy and the agency relationships that comprise it. In Part III, I develop a structural critique of the principal-agent challenges provoked by prosocial accounts of corporate purpose. I identify principal-agent relationships at the heart of the two prevailing ESG governance proposals—shareholder democracy and managerialism—and argue that each proposal engenders new agency challenges that are not accounted for under current governance arrangements or by proposed governance reforms. In Part IV, I elaborate the corporate technocracy as an alternative governance paradigm that furthers the goals of ESG while remaining reconcilable with Delaware corporate law doctrine and federal securities law. I make a normative case for the corporate technocracy and outline its three main structural features. I develop the consequences of adopting a technocratic approach to ESG through the examples of climate risk, corporate political speech, and diversity, equity, and inclusion (DEI). Corporate technocracy overcomes key governance concerns raised by ESG critics and fills gaps neglected by proponents.

This Article offers a way beyond the political dogma that plagues contemporary ESG debates and offers a normatively defensible and practically administrable model for advancing corporate ESG.

II. ESG: A TAXONOMY

ESG has many meanings among practitioners, scholars, and policymakers. It motivates varying—even contradicting—corporate governance projects.⁵ In this section, I set out a taxonomy of “ESG” that identifies how corporate purpose combines with corporate control to determine corporate political economy. I argue that each ESG paradigm advances a claim about corporate purpose and a claim about corporate control. I advance that those who promote ESG must contend with

⁵ Elizabeth Pollman, *The Making and Meaning of ESG* 32–35 (Eur. Corp. Governance Inst., Working Paper No. 659, 2022).

both ends (purpose) and means (control) to deliver accountable and effective ESG governance.

I go on to map four prevailing interpretations of ESG along the axes of corporate purpose and corporate control to demonstrate that while these interpretations might share a commitment to corporate prosociality, each generates different principal-agent relationships and demands its own set of corresponding governance reforms. It is only by defining and accounting for these relationships that ESG might deliver on its objectives while avoiding major shortcomings touted by its critics.

A. The Ends of ESG

What's a corporation for? Scholars, jurists, and legal practitioners have debated corporate purpose for nearly a century. The classic orientations align with shareholder primacy or stakeholder governance and claim their origins in an early 1930s exchange in the *Harvard Law Review* between Adolf Berle and Merrick Dodd.⁶

⁶ Adolf Berle, *Corporate Powers as Powers in Trust*, 44 HARV. L. REV. 1049, 1049 (1931) (“[A]ll powers granted to a corporation or to the management of a corporation, or to any group within the corporation, whether derived from statute or charter or both, are necessarily and at all times exercisable only for the ratable benefit of all the shareholders as their interest appears.”); E. Merrick Dodd, Jr. *For Whom are Corporate Managers Trustees?*, 45 HARV. L. REV. 1145, 1147–48 (1932) (“The present writer is thoroughly in sympathy with Mr. Berle’s efforts to establish a legal control which will more effectually prevent corporate managers from diverting profit into their own pockets from those of stockholders, and agrees with many of the specific rules which the latter deduces from his trusteeship, principle. He nevertheless believes that it is undesirable, even with the laudable purpose of giving stockholders much-needed protection against self-seeking managers, to give increased emphasis at the present time to the view that business corporations exist for the sole purpose of making profits for their stockholders.”); Adolf Berle, *For Whom Corporate Managers Are Trustees: A Note*, 45 HARV. L. REV. 1365, 1367 (1932) (“Now I submit that you can not abandon emphasis on ‘the view that business corporations exist for the sole purpose of making profits for their stockholders’ until such time as you are prepared to offer a clear and reasonably enforceable scheme of responsibilities to someone else.”). Modern proponents of shareholder wealth maximization attribute their position to Berle while stakeholderists

Since the late twentieth century, shareholder primacy has been accepted as the corporation's default purpose.⁷ Shareholder primacy defines managers' mandate and constrains the scope of their discretion. *Dodge v. Ford Motor Co.*⁸ was long considered the controlling legal precedent supporting shareholder primacy, though this account confronted considerable dispute.⁹ In 2010, Delaware's Supreme Court affirmed this default purpose in *eBay Domestic Holdings, Inc. v. Newmark*.¹⁰

claim Dodd as their intellectual forefather. Historical revisionists argue that this is a mischaracterization of the debate and that both Berle and Dodd would have been on the side of stakeholderism today by virtue of their corporatist orientation. Notwithstanding this critique, the Berle-Dodd debate has been used to support and advance the binary that characterizes corporate purpose today. See William W. Bratton & Michael L. Wachter, *Shareholder Primacy's Corporatist Origins: Adolf Berle and the Modern Corporation*, 34 J. CORP. L. 99, 101 (2008).

⁷ See, e.g., Leo E. Strine, Jr., *The Dangers of Denial: The Need for a Clear-Eyed Understanding of the Power and Accountability Structure Established by the Delaware General Corporation Law* 10 (U. Pa. Inst. for L. & Econ., Research Paper No. 15-08, 2015); Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L.J. 439, 439 (2001).

⁸ 170 N.W. 668, 684 (Mich. 1919) ("A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of directors is to be exercised in the choice of means to attain that end, and does not extend to a change in the end itself, to the reduction of profits, or to the nondistribution of profits among stockholders in order to devote them to other purposes.").

⁹ See, e.g., Lynn A. Stout, *Why We Should Stop Teaching Dodge v. Ford*, 3 VA. L. & BUS. REV. 163, 168 (2008); Einer Elhauge, *Sacrificing Corporate Profits in the Public Interest*, 80 N.Y.U. L. REV. 733, 772-76 (2005).

¹⁰ 16 A.3d 1, 34 (Del. Ch. 2010) ("Having chosen a for-profit corporate form, the craigslist directors are bound by the fiduciary duties and standards that accompany that form. Those standards include acting to promote the value of the corporation for the benefit of its stockholders."). *eBay* is often read as a modern *Dodge v. Ford* with a more explicit affirmation of the corporation's shareholder wealth maximization mandate. Its significance is further enhanced as it comes in the form of a clear holding out of the Delaware Supreme Court.

In recent years, however, corporate purpose has become unsettled¹¹ by demands from millennial investors,¹² progressive political narratives,¹³ and populist disenchantment with the social and economic consequences of corporate

¹¹ Tom Lin attributes the renewed interest in corporate purpose to three background phenomena: the convergence of government and private enterprise, maturation of corporate social responsibility movements, and expansion of corporate political rights by legal doctrine. Tom C. W. Lin, *Incorporating Social Activism*, 98 B.U. L. REV. 1535, 1558 (2018). Jonathan Macey argues that the rise of stakeholderism in the form of ESG may be attributed to the failure of government and the public's increasing turn to the private sector to address societal problems. Jonathan Macey, *Why is the ESG Focus on Private Companies, Not the Government?*, BLOOMBERG LAW (Aug. 19, 2021), <https://news.bloomberglaw.com/us-law-week/why-is-the-esg-focus-on-private-companies-not-the-government> [on file with the Columbia Business Law Review]. Stephen Bainbridge observes a leftward shift among corporate elites and notes a corresponding embrace of a left-leaning advocacy agenda. See Stephen M. Bainbridge, *Corporate Purpose in a Populist Era*, 98 NEB. L. REV. 543, 551 (2020) ("Today, populists find themselves increasingly at odds with an emergent class of social justice warrior CEOs, whose views on a variety of critical issues are increasingly closer to those of blue-state elites than those of red-state populists.").

¹² ERNST & YOUNG, SUSTAINABLE INVESTING: THE MILLENNIAL INVESTOR (2017) https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/financial-services/ey-sustainable-investing-the-millennial-investor.pdf [<https://perma.cc/AC7T-ASZM>] ("Demand for sustainable investments is being driven, in part, by millennials who prefer to invest in alignment with personal values."). Assets under management that use some form of ESG criteria have topped \$35 trillion globally, while U.S. investments make up more than half of that market. See, e.g., *ESG May Surpass \$41 Trillion Assets in 2022, But Not Without Challenges, Finds Bloomberg Intelligence*, BLOOMBERG (Jan. 24, 2022), <https://www.bloomberg.com/company/press/esg-may-surpass-41-trillion-assets-in-2022-but-not-without-challenges-finds-bloomberg-intelligence> [<https://perma.cc/HRT8-ECZ4>]; U.S. SUSTAINABLE INV. F., SUSTAINABLE AND IMPACT INVESTING—OVERVIEW (2020), <https://www.ussif.org/Files/Trends/2020%20Trends%20Report%20Info%20Graphic%20-%20Overview.pdf> [<https://perma.cc/7V5S-WU8V>]; U.S. SUSTAINABLE INV. F., REPORT ON US SUSTAINABLE AND IMPACT INVESTING TRENDS 1 fig. A, 2 fig. B (2020) <https://www.ussif.org/files/US%20SIF%20Trends%20Report%202020%20Executive%20Summary.pdf> [<https://perma.cc/77WE-6NRU>].

¹³ Grant Hayden & Matthew Bodie, *The Corporation Reborn: From Shareholder Primacy to Shared Governance*, 61 B.C. L. REV. 2419, 2422–23 (2020).

capitalism.¹⁴ Serious consideration of stakeholderism¹⁵ and ESG has penetrated mainstream corporate law and governance scholarship and practice.¹⁶

In this section I distinguish two main interpretations of corporate purpose that appear in mainstream corporate law and governance scholarship and practice: shareholder primacy and stakeholderism.

1. Shareholder Primacy

The prevailing interpretation of corporate purpose is shareholder primacy.¹⁷ Some accounts interpret shareholder

¹⁴ See, e.g., *Big Business – Gallup Historical Trends*, GALLUP, <https://news.gallup.com/poll/5248/big-business.aspx> [<https://perma.cc/J5MJ-VFDY>] (last visited Oct. 26, 2023) (popular perception of corporations ebbs and flows: notably, dissatisfaction rose after the 2008 financial crisis before returning to pre-crisis levels, and levels of dissatisfaction now match or exceed those observed directly after 2008); John Gerzema, *Americans to Companies: “Do More for Society”*, THE HARRIS POLL (June 24, 2020), <https://theharrispoll.com/briefs/americans-to-companies-do-more-for-society/> [<https://perma.cc/GV8Z-RV8F>].

¹⁵ *Statement on the Purpose of a Corporation*, BUS. ROUNDTABLE (Aug. 19, 2019), <https://s3.amazonaws.com/brt.org/BRT-StatementonthePurposeofaCorporationJuly2021.pdf> [<https://perma.cc/XC2Q-F3FJ>].

¹⁶ See, e.g., Stephen M. Bainbridge, *Making Sense of the Business Roundtable’s Reversal on Corporate Purpose*, 46 J. CORP. L. 285, 289 (2021); Edward B. Rock, *For Whom is the Corporation Managed in 2020?: The Debate over Corporate Purpose* 3–4 (Eur. Corp. Governance Inst., Working Paper No. 515, 2020); Hester M. Peirce, Commissioner, *My Beef with Stakeholders: Remarks at the 17th Annual SEC Conference, Center for Corporate Reporting and Governance*, SEC (Sept. 21, 2018), <https://www.sec.gov/news/speech/speech-peirce-092118> [<https://perma.cc/N97F-PRUC>] (“There is no denying that employees, suppliers, and localities often feel the effects of the choices a company’s board makes. The question of who might be affected by a decision is, however, a different question from whether the company must consider their interests—separate and apart from the company’s own interests—as part of any decision-making. That question is, in turn, separate from the question of whether these individuals, by virtue of their status as ‘stakeholders,’ are entitled to a say in how the company conducts its business. I posit that the proper answer to these last two questions is ‘no.’”).

¹⁷ In the tradition of Milton Friedman, shareholder primacy equates with shareholder wealth maximization. Milton Friedman, *The Social*

primacy as short-term shareholder wealth maximization, while others interpret it as long-term enterprise value creation.¹⁸ Generally, however, shareholder primacists agree that shareholders are the corporation's principals and that managers are their fiduciaries and agents.¹⁹ They argue that limiting managers' mandate promotes efficiency: shareholder wealth maximization identifies a uniform preference among diverse shareholders,²⁰ which creates accountability from

Responsibility of Business is to Increase its Profits, N.Y. TIMES (Sept. 13, 1970), <https://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html>[<https://perma.cc/U4DS-WPMT>]. The more recent formulation advanced by Oliver Hart and Luigi Zingales suggests a liberalized shareholder primacy that represents shareholder welfare maximization. See Oliver Hart & Luigi Zingales, *Companies Should Maximize Shareholder Welfare Not Market Value*, J. L. FIN. & ACCT. 247, 248 (2017). Until now, this account has not been used to justify a sacrifice of shareholder wealth even where broader shareholder welfare is claimed. In both the Friedman and the Hart and Zingales accounts, shareholders remain as the underlying principals of the corporate governance endeavor and managers are their agents charged with representing and accounting for shareholders' pluralist pro-social preferences.

¹⁸ David Millon, *Radical Shareholder Primacy*, 10 U. ST. THOMAS L.J. 1013, 1013–14 (2013) (explaining that “traditional shareholder primacy” is oriented towards long-term corporate value, distinguishable from “radical shareholder primacy,” which is oriented towards short term shareholder wealth maximization).

¹⁹ Proponents of shareholder wealth maximization defend it on normative and practical grounds. One position grounds its claim in a contract theory of the corporation that justifies shareholders' privileged position among other corporate stakeholders by appealing to their status as the corporation's sole residual claimants. Sung Eun Kim, *Tracing the Diverse History of Corporate Residual Claimants*, 95 S. CAL. L. REV. POSTSCRIPT 43, 44 (2021). Another position takes root in property theory, claiming that shareholders, as the corporation's owners, are entitled to a position of primacy among its various stakeholders. Julian Velasco, *Shareholder Ownership and Primacy*, 2010 U. ILL. L. REV. 897, 898–99.

²⁰ See, e.g., Frank H. Easterbrook & Daniel R. Fischel, *Voting in Corporate Law*, 26 J.L. & ECON. 395, 405–06 (1983) (“[S]hareholders of a given firm at a given time are a reasonably homogeneous group with respect to their desires for the firm.”); Henry G. Manne, *Some Theoretical Aspects of Share Voting*, 64 COLUM. L. REV. 1427, 1442 (1964) (“Few fights for control of a corporation, therefore, are likely to involve any fundamental difference of opinion among shareholders on ultimate goals; they are much more likely

managers and a clear financial metric for evaluating and monitoring performance.

A more nuanced variation of shareholder primacy claims is that a corporation's purpose is to deliver enlightened shareholder value by combining profit and purpose.²¹ Accordingly, managers have a mandate to generate profit for shareholders while considering implications for social welfare when selecting among different possible operational decisions or strategies. This position seeks governance reforms that incentivize efficient decision-making that serves shareholders' interests while also producing favorable social externalities or, at least, minimizing social harm. Some critics argue that this interpretation of "enlightened" shareholder value is already baked into managers' mandate and that enlightened shareholder value is merely a rhetorical repackaging of ordinary shareholder primacy.²²

2. Stakeholderism

The foil to shareholder primacy is stakeholderism, which claims that corporations should be governed in the interests of their stakeholders. Interpretations of "stakeholders" vary from the specific to the abstract. A narrow account is labor codetermination, which considers workers to be nonequity investors alongside traditional investors.²³ A more abstract account considers stakeholders to include all those who are

to represent differences about how the company can best assure the maximization of a common interest.").

²¹ See Dorothy S. Lund, *Enlightened Shareholder Value, Stakeholderism, and the Quest for Managerial Accountability*, in RESEARCH HANDBOOK ON CORPORATE PURPOSE AND PERSONHOOD 91, 92 (Elizabeth Pollman & Robert Thompson eds., 2021).

²² See Lucian A. Bebchuk & Roberto Tallarita, *The Illusory Promise of Stakeholder Governance*, 106 CORNELL L. REV. 91, 110 (2020) ("Given the positive connotations of the term 'enlightened,' enlightened shareholder value sounds better than shareholder value. However, enlightened shareholder value is not conceptually different from the 'old-fashioned' shareholder value In other words, enlightened shareholder value is only a particular articulation of shareholder value.").

²³ See Kent Greenfield, *Reclaiming Corporate Law in a New Gilded Age*, 2 HARV. L. & POL'Y REV. 1, 24 n.83 (2008).

affected by its decisions and operations, such as communities, consumers, or others.²⁴

Proponents of stakeholder governance defend their position on both normative and practical grounds. One normative position begins from a conception of the corporation as a nexus of contracts, some of them formal and others implied, and argues that stakeholders additional to shareholders have a claim to corporate benefits.²⁵ Another version grounds itself in a concession theory of the firm and argues that the corporation is a creation of the state and that, in exchange for the many public benefits that it receives, it owes certain obligations to the public interest.²⁶ A third approach is pragmatic, relying on economic reasoning and arguing that a firm performs better when it accounts for various stakeholder interests or when various stakeholder constituencies are involved in decision-making.²⁷

²⁴ See Colin Mayer, *Shareholderism Versus Stakeholderism – A Misconceived Contradiction. A Comment on The Illusory Promise of Stakeholder Governance by Lucian Bebchuk and Roberto Tallarita* 1 (Eur. Corp. Governance Inst., Working Paper No. 522, 2020) (explaining that “stakeholderism’...[is] the idea of promoting the interests of the stakeholders of a firm (its customers, employees, suppliers, societies, and the environment)”).

²⁵ See, e.g., Kent Greenfield, *Defending Stakeholder Governance*, 58 CASE W. RES. L. REV. 1043, 1057–58 (2008) (“Some employees’ wage and salary claims (though not all) may be fixed in the short term, but employees also have both implicit and explicit claims against the enterprise that are more valuable when the company does well and are worth less (or nothing) when the company does poorly.”).

²⁶ See, e.g., Reza Dibadj, *(Mis)Conceptions of the Corporation*, 29 GA. ST. U. L. REV. 731, 775–78 (2013) (“It is difficult to deny the basic premise that corporations are created by the State as a means of furthering the public welfare.”) (citation omitted); William W. Bratton, Jr., *The New Economic Theory of the Firm: Critical Perspectives from History*, 41 STAN. L. REV. 1471, 1475 (1989) (“Concession theory . . . attributes the corporation’s very existence to state sponsorship.”).

²⁷ See, e.g., Dame Vivian Hunt et al., *The Case for Stakeholder Capitalism*, MCKINSEY & CO., Nov. 12, 2020, <https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/the-case-for-stakeholder-capitalism> [<https://perma.cc/66Y4-UPVJ>] (“In a study that looked at 615 large- and mid-cap US publicly listed companies from 2001–15 . . . [companies that emphasized stakeholder capitalism] outperformed the rest in earnings, revenue, investment, and job growth.”).

B. The Means of ESG

A corporation's purpose is implemented and optimized through its governance arrangement. Modern corporate governance is concerned with allocating decision-making power between a corporation's principals, its shareholders, and their agents, directors and managers, to maximize efficiency. Though the term corporate governance dates back to the early 1960s,²⁸ by the 1980s it has been captured by an agency framework.²⁹ In *The Corporate Governance Machine*, Dorothy Lund and Elizabeth Pollman observe that corporate governance is grounded in a shareholder value framework and that related reforms remain consistent with this ideology.³⁰ Accordingly, contemporary scholarship and policy reform focus on minimizing costs between shareholder principals and managerial agents, deterring rent-seeking, and optimizing incentives alignment towards a more efficient corporate pursuit of profit.³¹

Within corporate governance scholarship, one major position lobbies for increasing shareholder power and granting them a greater role in overseeing and disciplining managerial waste.³² A second major position lobbies for increasing management's power to privilege their expertise and limit shareholder micromanagement.³³ Those who advance greater shareholder control rights favor governance reforms that grant shareholders more direct involvement in major corporate decisions, including the power to amend a corporate

²⁸ Dorothy S. Lund & Elizabeth Pollman attribute the term's origins to Richard Eell's 1962 book "Government of Corporations." *The Corporate Governance Machine*, 121 COLUM. L. REV. 2563, 2571 n.32 (2021).

²⁹ *Id.* at 2573–74.

³⁰ *Id.* at 2575–78.

³¹ *Id.* at 2603–05.

³² See, e.g., Lucian Arye Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833, 899 (2005) ("Permitting shareholder intervention would thus reduce the agency costs . . . [and address the] insulation [that] weakens incentives to avoid managerial slack.").

³³ See, e.g., Stephen M. Bainbridge, *Director Primacy* (UCLA Sch. of L., L. & Econ. Rsch. Paper Series, Research Paper No. 10-06, 2010), <https://ssrn.com/abstract=1615838> [<https://perma.cc/8HQ4-FYUK>].

charter, change its state of incorporation, and oversee corporate political speech.³⁴ By contrast, those who advocate for greater managerial control promote governance reforms that weaken shareholder control rights and that provide for greater managerial discretion in the form of anti-takeover defenses, nonvoting share classes, and staggered boards.³⁵ Each position advances a contemporary project to support its claim that greater shareholder or managerial control is more conducive to shareholder wealth maximization.³⁶

More recently, corporate governance scholars and practitioners have extended these arguments to claim that ceding greater power to shareholders, managers, or stakeholders optimizes corporate performance in service of stakeholders.³⁷ These claims are bolstered by some account justifying that a given group can deliver for stakeholders more effectively or efficiently than others by appealing to inherent virtue or to institutional limitations.

³⁴ Bebchuk, *supra* note 32, at 865–70 (“[Shareholders] would be able to initiate and approve by vote both changes in the corporate charter and changes in the company’s state of incorporation.”); Lucian A. Bebchuk & Robert J. Jackson, Jr., *Corporate Political Speech: Who Decides?*, 124 HARV. L. REV. 83, 84 (2010) (“[W]e suggest that lawmakers consider adopting rules that . . . provide shareholders with a role in determining the amount and targets of corporate political spending.”).

³⁵ Stephen M. Bainbridge, *Director Primacy in Corporate Takeovers: Preliminary Reflections*, 55 STAN. L. REV. 791, 802–03 (2002) (“[T]akeover defenses—especially the combination of a poison pill and a staggered board—have gone a long way towards restoring director primacy.”).

³⁶ See, e.g., Robert J. Rhee, *A Legal Theory of Shareholder Primacy*, 102 MINN. L. REV. 1951, 1952 (2017) (“[S]hareholder primacy instructs the board to manage the corporation for the purpose of maximizing shareholder wealth.”); Bainbridge, *supra* note 33, at 3 (“To be sure, the directors are obliged to use their powers towards the end of shareholder wealth maximization, but the decisions as to how that end shall be achieved are vested in the board not the shareholders.”).

³⁷ See, e.g., Cathy Hwang & Yaron Nili, *Shareholder-Driven Stakeholderism*, 2020 U. CHI. L. REV. ONLINE *1, *2, *6–*7; Leo E. Strine, Jr., Kirby Smith & Reilly S. Steel, *Caremark and ESG, Perfect Together: A Practical Approach to Implementing an Integrated, Efficient, and Effective Caremark and EESG Strategy*, 106 IOWA L. REV. 1885, 1893–95 (2021); Brett McDonnell, *Stakeholder Governance as Governance by Stakeholders*, 47 SEATTLE U. L. REV. 511 (2024).

1. Shareholder Control

One leading approach to governance prioritizes shareholder control and views managerial discretion with skepticism. Its proponents advance that corporate governance is organized on behalf of shareholders, the putative owners of the firm or its key residual claimants, and that shareholders accordingly wield control over key decisions.³⁸ A shareholder primacy approach to governance assumes greater distrust of management and emphasizes the importance of levers that shareholders can use to discipline managers and to limit rent-seeking. This position supports stronger shareholder rights that shift the locus of control away from managers and towards shareholders. Related reforms emphasize mandatory disclosures;³⁹ liberalized standards for Section 10-b claims,⁴⁰

³⁸ See, e.g., Lucian A. Bebchuk, *The Myth of the Shareholder Franchise*, 93 VA. L. REV. 675 (2007) (arguing for stronger shareholder voting powers).

³⁹ See, e.g., Sara K. Orr & Sofia Martos, *Corporate ESG Disclosure: Recent Trends and Developments*, LEXISNEXIS PRACTICAL GUIDANCE (Oct. 8, 2021), <https://www.kirkland.com/publications/article/2021/10/corporate-esg-disclosure-orr-martos> [<https://perma.cc/7VXY-3PKS>].

⁴⁰ See, e.g., Aisha I. Saad & Diane Strauss, *The New “Reasonable Investor” and Changing Frontiers of Materiality: Increasing Investor Reliance on ESG Disclosures and Implications for Securities Litigation*, 17 BERKELEY BUS. L. J. 391, 425 (2020) (proposing that courts should “re-center” the reliance-based approach for materiality for a section 10(b) claim and broaden the definition of a “reasonable investor” to be “based on investor demographics, preferences, and decision-making [which] will better serve the needs of today’s reasonable investor.”).

books and records requests, and *Caremark* claims;⁴¹ liberalized rules for shareholder proposals;⁴² and proxy access.⁴³

2. Managerial Control

A second leading approach to governance favors weaker shareholder power and stronger managerial power. This view is skeptical of shareholders' direct participation in governance and characterizes such attempts as micromanagement that interferes with managers' capacity to govern efficiently. Director or managerial primacy assumes greater trust of executives and emphasizes the protected discretion that they require to deliver for shareholders.⁴⁴ This position seeks stronger managerial rights that shift the locus of control away from shareholders and towards managers and directors. Related reforms emphasize a more protective interpretation of the business judgment rule and stronger anti-takeover provisions.⁴⁵

⁴¹ See, e.g., Eduardo Gallardo, *Boards of Directors' Duty of Oversight and ESG Matters: "Caremark" Revisited*, CLS BLUE SKY BLOG (July 2, 2019), <https://clsbluesky.law.columbia.edu/2019/07/02/boards-of-directors-duty-of-oversight-and-esg-matters-caremark-revisited/> [https://perma.cc/WB6N-NZFB] (“[G]iven societal concerns around ESG matters, *Caremark* might come to play a more prominent role in gently guiding boards and corporations towards more actively incorporating these concerns in their decision-making process.”).

⁴² See, e.g., Renee Jones, *The Shareholder Proposal Rule: A Cornerstone of Corporate Democracy*, SEC (Mar. 8, 2022), <https://www.sec.gov/news/speech/jones-cii-2022-03-08> [https://perma.cc/MS3M-QAVR].

⁴³ Holly J. Gregory et al., *The Latest on Proxy Access*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Feb. 1, 2019), <https://corpgov.law.harvard.edu/2019/02/01/the-latest-on-proxy-access/> [https://perma.cc/J6YH-42ZB].

⁴⁴ Stephen Bainbridge first wrote about director primacy in 2002, characterizing the board of directors as a “nexus for the various contracts making up the corporation” rather than as an agent of the shareholders. Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, 97 NW. U. L. REV. 547, 560 (2002).

⁴⁵ Lynn A. Stout, *Do Antitakeover Defenses Decrease Shareholder Wealth? The Post/Ex Ante Valuation Problem*, 55 STAN. L. REV. 845, 856 (2002); Steven M. Bainbridge, *supra* note 35, at 807 n.92.

3. Stakeholder Control

A third governance position seeks to involve stakeholders directly in corporate governance. Some proposals envision giving stakeholders like workers a direct equity stake,⁴⁶ while others envision granting them board representation.⁴⁷ Codetermination advocates often point to the European experience, but several examples can also be identified in the early 20th century U.S.⁴⁸ Most recently, Senators Bernie Sanders and Elizabeth Warren pushed for worker representation on corporate boards that exceed a certain size.⁴⁹

⁴⁶ See, e.g., Jonathan Burton, *Workers Would Get Money And Voting Power Under This Radical Profit-Sharing Idea*, MARKETWATCH (Sept. 21, 2019), <https://www.marketwatch.com/story/forcing-companies-to-share-the-wealth-with-employees-could-save-capitalism-2019-09-13> [<https://perma.cc/69Z6-4SKS>]; Douglas L. Kruse & Margaret M. Blair, *Worker Capitalists? Giving Employees an Ownership Stake*, BROOKINGS (Sept. 1, 1999), <https://www.brookings.edu/articles/worker-capitalists-giving-employees-an-ownership-stake/> [<https://perma.cc/VF54-XHPD>].

⁴⁷ Lenore Palladino, *Worker Representation on U.S. Corporate Boards*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Dec. 30, 2019), <https://corpgov.law.harvard.edu/2019/12/30/worker-representation-on-u-s-corporate-boards/> [<https://perma.cc/4H8N-C73S>].

⁴⁸ Grant M. Hayden & Matthew T. Bodie, *Codetermination in Theory and Practice*, 73 FLA. L. REV. 321, 325 (2021); While not in effect today, several states have codified codetermination statutes that would acknowledge workers as principals and grant them direct participation in governance. See e.g., MASS. GEN. LAWS ANN. ch. 156, § 23 (2018) (“A manufacturing corporation may provide by by-law for the nomination and election by its employees of one or more of them as members of its board of directors . . . A director elected by the employees shall have the same rights and powers and shall be subject to the same duties and responsibilities as a director elected by the stockholders.”).

⁴⁹ On the presidential campaign trail, Senator Bernie Sanders proposed democratizing corporate boards and requiring federal stakeholder charters for large companies. Bernie Sanders, *Issues: Corporate Accountability and Democracy*, BERNIE, <https://berniesanders.com/issues/corporate-accountability-and-democracy/> [<https://perma.cc/V6AT-JF9B>] (last visited Feb. 10, 2023) (Under this proposed plan, “all publicly traded companies must obtain a federal charter from a newly established Bureau of Corporate Governance at the Department of Commerce. This new federal charter will require corporate boards to consider the interests of all of the stakeholders in a company – including workers, customers, shareholders, and the

C. Four ESG Governance Paradigms

The intersection of claims concerning corporate purpose and corporate power yield four main ESG paradigms. Each of these paradigms advances a distinct corporate political economy. While all of these paradigms purportedly share a common end, as a matter of governance reform they require distinct and at times even contradictory agendas.

1. Enlightened Shareholder Primacy

Enlightened shareholder primacy maintains that corporate purpose is profit generation for shareholders, but that managers should account for other prosocial objectives when they do not come in conflict with this end. The business judgment rule⁵⁰ insulates managerial decisions from challenge by shareholders⁵¹ if they have a plausible rational business

communities in which the corporation operates.”). The Accountable Capitalism Act introduced by Senator Elizabeth Warren in 2018 would require corporate boards to “include substantial employee participation” with “no fewer than 40% of its directors [being] selected by the [its] employees.” This too, reflects an expanded principal base. Elizabeth Warren, *Accountable Capitalism Act*, <https://www.warren.senate.gov/imo/media/doc/Accountable%20Capitalism%20Act%20One-Pager.pdf> [<https://perma.cc/Y76V-S8F9>] (last visited Dec. 12, 2023).

⁵⁰ A cornerstone of Delaware law, the business judgment rule (BJR) prevents second guessing of board decisions by the courts “absent an abuse of discretion.” *Orman v. Cullman*, 794 A.2d 5, 19–20 (Del. Ch. 2002); *See also Westmoreland Cnty. Emp. Ret. Sys. v. Parkinson*, 727 F.3d 719, 725 (7th Cir. 2013) (“[T]he business judgment rule establishes a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.”) (citation omitted). The presumption in favor of management for ordinary business decisions is in the interest of decision-making efficiency. *See* Stephen M. Bainbridge, *The Business Judgment Rule as Abstention Doctrine*, 57 VAND. L. REV. 83 (2004).

⁵¹ Delaware corporate law delegates operational decisions to managers, while reserving to shareholders a role in certain special corporate decisions. These include amending a corporate charter or bylaws, merging, and approving equity compensation plans. *See, e.g.*, DEL. CODE ANN. tit. 8, § 251(c) (2001) (requiring shareholder approval for certain mergers); *id.* § 242(b) (requiring shareholder approval for charter amendments); Order Approving NYSE and Nasdaq Proposed Rule Changes Relating to Equity

purpose or if they occur in the “ordinary course of business.”⁵² Controlling doctrine allows considerable leeway within these parameters by insulating managers’ decisions from review absent an abuse of discretion.⁵³

Related governance reforms aim to improve incentives for managers to exercise their discretion in ways that recognize and account for externalities and stakeholder impacts. One recent governance innovation has attempted to link executive compensation to ESG performance, for example, but it has been fraught with complications as ESG indicators and performance metrics remain ambiguous.⁵⁴

2. Managerialism

Managerialism prevailed in the first half of the twentieth century and considered corporate managers the stewards of a

Compensation Plans, 68 Fed. Reg. 39995 (July 3, 2003) (approving exchange-listing rules requiring firms to obtain shareholder approval for equity-based compensation plans).

⁵² In *Lee v. Jenkins Bros.*, 268 F.2d 357, 365 (2d Cir. 1959), the Second Circuit held “that the president [of a corporation] only has authority to bind his company by acts arising in the usual and regular course of business but not for contracts of an ‘extraordinary’ nature.” Delaware courts will not second-guess the board’s judgment unless it can conclude that a decision cannot be attributed to any rational business purpose related to the company. *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1, 33 (Del. Ch. 2010) (“When director decisions are reviewed under the business judgment rule, this Court will not question rational judgments about how promoting non-stock-holder interests—be it through making a charitable contribution, paying employees higher salaries and benefits, or more general norms like promoting a particular corporate culture—ultimately promote stockholder value”).

⁵³ *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984) (elaborating the “business judgment rule” as “a presumption that in making a business decision, the directors of a corporation acted on an informed basis in good faith and in the honest belief that the action was taken in the best interests of the company.”).

⁵⁴ Lucian A. Bebchuk & Roberto Tallarita, *The Perils and Questionable Promise of ESG-Based Compensation*, 48 J. CORP. L. 37, 74–75 (2022) (analyzing ESG compensation metrics in S&P 100 companies and concluding that the current use of ESG metrics serves executives rather than stakeholders).

broad public interest, ceding to them an expanded domain of discretion. This position corresponds with Merrick Dodd's characterization of managers as trustees of a public interest.⁵⁵ Managers have been characterized as disinterested public servants, or "mediating hierarchs" in the writings of Margaret Blair and Lynn Stout,⁵⁶ Colin Mayer,⁵⁷ and Marty Lipton,⁵⁸ among others.

Managerial stakeholderism goes farther than enlightened shareholder primacy in relaxing the parameters of corporate "ends," thereby expanding the scope of managers' legitimate discretion. Managers govern the corporation in the interest of a corporation's stakeholders, not just shareholders. Advocates for expanding managerial control over ESG seek to grant them a greater scope of protected discretion to take stakeholder interests into account.⁵⁹ One consequence of this

⁵⁵ Dodd, Jr., *supra* note 6.

⁵⁶ Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247 (1999).

⁵⁷ Mayer advances that directors already exercise considerable judgment in pursuing a corporation's declared purpose and that expanding this purpose to stakeholderism does not change their role in exercising judgment to balance a company's various purposes and values. *See* Mayer, *supra* note 24, at 2–3.

⁵⁸ Lipton and colleagues advance that "[t]he task of identifying stakeholders, and mediating amongst them, properly rests with boards of directors acting on their informed business judgment." Martin Lipton, Steven A. Rosenblum, William Savitt & Karessa L. Cain, *Wachtell Lipton on How Boards and Management Should Handle ESG and Stakeholder Governance*, CLS BLUE SKY BLOG (June 4, 2020), <https://clsbluesky.law.columbia.edu/2020/06/04/wachtell-lipton-on-how-boards-and-management-should-handle-esg-and-stakeholder-governance/> [<https://perma.cc/JC77-N2XE>]; Lipton critiques Bebhuk's scholarship on stakeholderism, arguing that "Bebchuk's methodology is a farce" and the high-level corporate governance documents where he seeks to identify evidence of delivery on the business roundtable letter are not the right places to be looking: "the documents Bebhuk reviewed cannot establish his claim because there is no reason they would reflect evidence of stakeholder engagement." Martin Lipton, *More Myths from Lucian Bebhuk*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Aug. 24, 2021) <https://corpgov.law.harvard.edu/2021/08/24/MORE-MYTHS-FROM-LUCIAN-BEBCHUK/> [<https://perma.cc/LNS9-JVEU>].

⁵⁹ *See, e.g.*, Strine, Jr. et al., *supra* note 37.

expanded discretion is weakened fiduciary duties to shareholders.

Managerial stakeholderism presents a radical departure from shareholder primacy: it substitutes the putative class of shareholder principals for stakeholder principals. This perspective is reflected in the 2019 Business Roundtable Statement on the Purpose of a Corporation “outlin[ing] a modern standard for corporate responsibility”⁶⁰ and asserting “a fundamental commitment to all of [a company’s] stakeholders.”⁶¹ The fundamental weakness of this proposition is that it modifies the class of corporate principals while retaining a governance architecture based on shareholder principals and managerial agents. This agenda fails to account for the agency costs that follow from its proposal. Scholars like Ann Lipton have proposed overcoming associated agency costs through stakeholder disclosures, for example, but thus far there has been no argument for creating fiduciary duties to stakeholders or for a stakeholder franchise.⁶² These gaps are in large part a function of the more fundamental challenge of defining stakeholders within administrable parameters.

3. Shareholder Democracy

Shareholder democracy reinterprets shareholder primacy to emphasize shareholder heterogeneity, maintaining that

⁶⁰ *Business Roundtable Redefines the Purpose of a Corporation to Promote ‘An Economy That Serves All Americans,’* BUS. ROUNDTABLE (Aug. 19, 2019), <https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans> [https://perma.cc/Y9KE-MDTA].

⁶¹ Signatories to the statement committed to deliver value to all of their stakeholders, listing customers, employees, suppliers, communities, and shareholders. Coverage of the Statement prompted a flood of commentary on corporate purpose. Much of the commentary contrasted the Statement with Milton Friedman’s 1970 article, “The Social Responsibility of Business is to Increase its Profits.” David Benoit, *Move Over, Shareholders: Top CEOs Say Companies Have Obligations to Society*, WALL ST. J., (Aug. 19, 2019), <https://www.wsj.com/articles/business-roundtable-steps-back-from-milton-friedman-theory-11566205200> [https://perma.cc/4HRS-NGF9].

⁶² Ann Lipton, *Not Everything is About Investors: The Case for Mandatory Stakeholder Disclosure*, 37 YALE J. ON REGUL. 499 (2020).

managers are the stewards of shareholder interests while also advancing that shareholders today tend to prefer corporate purposes beyond profit maximization. This model has been elaborated in recent scholarship by Roberto Tallarita,⁶³ Cathy Hwang and Yaron Nili,⁶⁴ and in earlier work by Lucian Bebchuk and Robert Jackson.⁶⁵

Shareholder democracy's core proposition is that expanding managerial discretion to account for stakeholder interests exacerbates rent-seeking, and that shareholders would be more efficient sponsors of stakeholder interests. It is a questionable proposition for stakeholders, however, because shareholder democracy does not recognize an agency relationship between stakeholders and shareholders just as managerialism fails to do so between stakeholders and managers. From stakeholders' perspective, shareholder democracy is no different from enlightened shareholder primacy in terms of its structural limitations.

Advocates of shareholder democracy advance reforms that would shift control over corporate purpose from managers to shareholders by liberalizing shareholder proposal rules, for example, expanding the use of SEC Rule 14a-8 as a

⁶³ Tallarita picks up where his and Lucian Bebchuk's critiques of managerialist stakeholderism leave off. After discrediting a management-controlled stakeholderism, Tallarita offers an alternative account that relies on "shareholder power" rather than "managerial power" through what he terms "stockholder politics." See Roberto Tallarita, *Stockholder Politics*, 73 HASTINGS L.J. 1697, 1710 (2022).

⁶⁴ Hwang & Nili, *supra* note 37, at 4 ("[I]n public companies, *shareholders*, not management, have been the driving force behind the environmental, social, and governance principles that often align with stakeholder governance.").

⁶⁵ A decade ago, in the wake of the *Citizens United v. FEC* decision when the Supreme Court opened the floodgates to corporate political spending, Bebchuk and Jackson advanced a version of that shareholder-controlled stakeholderism position that transfers easily to a broader range of stakeholder subjects now considered to be ESG. This approach appears to be a sort of resigned compromise by those who have long advocated for a shareholder-controlled shareholder wealth maximizing position but who recognize its increasing incongruence with broader practice. Their proposal allows shareholders to retain more discretion over nonpecuniary corporate decisions. See Bebchuk & Jackson, Jr., *supra* note 34, at 84 (2010).

mechanism for democratic participation in corporate governance, and weakening proxy campaign restrictions. They have succeeded in advancing recent regulatory reforms furthering these objectives. One example is an interpretation of Rule 14a-8⁶⁶ governing the shareholder proposal process. The Rule allows shareholders to submit proposals as part of a company's proxy statement, and previously required that proposals have some economic nexus to company operations. The Rule includes a provision permitting managers to exclude proposals that constitute micromanagement. In a recent Staff Legal Bulletin (SLB 14L), however, the SEC modified its interpretation to allow the distribution of proposals with no economic nexus if issues have "a broad societal impact."⁶⁷ These reforms

⁶⁶ SEC Staff Legal Bulletin No. 14L (CF), 87 FED. REG. 45052 (Nov. 3, 2021), <https://www.sec.gov/corpfin/staff-legal-bulletin-14l-shareholder-proposals> [<https://perma.cc/E96B-NWDA>] [hereinafter SEC Legal Bulletin]; see also *infra* notes 79, 140. SEC Rule 14a-8 has served as a platform for competing corporate governance approaches to stakeholderism. This rule determines who can promote ESG topics and on what subjects. This has important implications for stakeholderism because ESG proposals, which were, until relatively recently, only a fringe subset of shareholder proposals, now garner attention by shareholders, corporate directors, corporate law firms, proxy voting advisory firms, and institutional investors as an indicator of the issues that investors care about and are receiving a much higher voting turnout than before. Two rules have notably been amended by both the Trump and Biden administrations, and Republican and Democrat controlled SECs, evidencing a back-and-forth struggle over shareholders' role in governing stakeholderism. One concerns ownership requirements with respect to number of shares and duration of ownership required to submit a shareholder proposal. The second concerns the types of subjects that may be addressed in a shareholder proposal, dealing specifically with subjects that may be excluded by managers. The Republican-controlled SEC limited subjects appropriate for shareholder proposals to those passing a test of economic significance and having some nexus to a company's operations and going beyond ordinary business matters. Press Release, SEC, SEC Adopts Amendments to Modernize Shareholder Proposal Rule (Sept. 23, 2020), <https://www.sec.gov/news/press-release/2020-220> [<https://perma.cc/9VYA-83ET>]. The Democrat-controlled SEC, on the other hand, recently expanded permissible subjects to matters of a broad social significance thus expanding shareholder-control over ESG. *Supra* SEC Legal Bulletin.

⁶⁷ SEC Legal Bulletin, *supra* note 66 ("[S]taff will no longer focus on determining the nexus between a policy issue and the company, but will instead focus on the social policy significance of the issue that is the subject

notably expand shareholder power, giving shareholders greater leverage in setting corporate ESG agendas.

4. Codetermination

Though it is not considered a part of the mainstream ESG debate, codetermination is often folded into a broader discussion of corporate purpose. Advocates of codetermination seek to include stakeholders, namely labor, in the procedures of corporate governance. They view stakeholderism not merely as an end to be achieved through manager or shareholder sponsorship, but as a participatory corporate governance project. For example, Kent Greenfield advances that non-equity stakeholders hold equal entitlements to shareholders and, accordingly, that they have a right to direct corporate resources to meet collective welfare objectives.⁶⁸ Grant Hayden and Matthew Bodie⁶⁹ observe that this position appears in some state laws as a permissive provision and that, while not in effect today, several states have codified codetermination statutes on the books.⁷⁰ On the presidential campaign trail, Senator Bernie Sanders proposed democratizing corporate boards and requiring federal stakeholder charters for large companies.⁷¹ Senator Elizabeth Warren's Accountable Capitalism

of the shareholder proposal. In making this determination, the staff will consider whether the proposal raises issues with a broad societal impact, such that they transcend the ordinary business of the company.”).

⁶⁸ Kent Greenfield & D. Gordon Smith, *Debate: Saving the World with Corporate Law?*, 57 EMORY L.J. 947 (2008).

⁶⁹ Hayden & Bodie, *supra* note 48, at, 325.

⁷⁰ See e.g., MASS. GEN. LAWS ANN. ch. 156, § 23 (2018) (“A manufacturing corporation may provide by by-law for the nomination and election by its employees of one or more of them as members of its board of directors . . . A director elected by the employees shall have the same rights and powers and shall be subject to the same duties and responsibilities as a director elected by the stockholders.”).

⁷¹ Under this proposed plan, “all publicly traded companies must obtain a federal charter from a newly established Bureau of Corporate Governance at the Department of Commerce. This new federal charter will require corporate boards to consider the interests of all of the stakeholders in a company – including workers, customers, shareholders, and the communities in which the corporation operates.” Sanders, *supra* note 49.

Act reflects a similar position: the Act would require corporate boards to “include substantial employee participation” with “no fewer than 40% of its directors [being] selected by [its] employees.”⁷² Beyond a claim for worker participation, however, codetermination has not yet elaborated a framework for selecting participating stakeholders and for refereeing between their competing interests.

III. ESG’S GOVERNANCE PROBLEMS

Each of the four ESG governance paradigms elaborated in Part II makes a claim about a corporation’s principals, their agents, and control rights allocated to each. An embrace of prosocial corporate purpose creates misalignments between power and oversight that, until now, remain governed by the default arrangements of shareholder primacy. Consequently, each ESG paradigm suffers from unaddressed agency costs.

The separation of ownership and control is a defining feature of the modern corporation. For over half a century, agency theory has guided governance solutions attempting to account for the costs of diverging interests between principals (shareholders) and agents (managers).⁷³ Modern corporate

⁷² Elizabeth Warren, *Accountable Capitalism Act*, <https://www.warren.senate.gov/imo/media/doc/Accountable%20Capitalism%20Act%20One-Pager.pdf> [https://perma.cc/6JTN-XFSE] (last visited Dec. 12, 2023).

⁷³ This defining feature of the modern corporation generates three main types of agency problems: 1) conflicts between shareholders and managers, 2) conflicts between majority or controlling stakes and minority or non-controlling stakes, and 3) conflicts between a corporation and other parties that it contracts with including creditors, employees, and customers. See John Armour, Henry Hansmann & Reinier Kraakman, *Agency Problems and Legal Strategies*, in *THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH* 35, 36 (2d ed. 2009). Armour et al. identify key legal strategies for mitigating agency costs of the corporate form. They group these into regulatory strategies that directly constrain an agent’s behavior, and governance strategies that facilitate principal’s control over agent’s behavior. Regulatory strategies constrain agents by prohibiting decisions and transactions that harm principals’ interests through rule-based regulation governing proxy voting and annual disclosure for example, and through standards such as requiring directors to act “in good faith” or for self-dealing transactions to be “entirely fair.” *Id.* at 40.

governance aims to reduce agency costs between shareholder principals and managerial agents. Governance strategies include legal and market mechanisms.⁷⁴ They rely on principals generating compliance from agents through selection, threat of removal, or direct decision-making on key issues, for example.⁷⁵

ESG advocates advance two main corporate governance reform agendas: one advancing shareholder primacy, and a second advancing managerialism. In large part, they fail to account for the structural agency implications engendered by their proposed ESG paradigm and to provide a coherent framework for who should control ESG and how. In this section, I extend analysis of the principal-agent relationship that runs through all major corporate governance questions and apply it to ESG. By identifying and addressing the agency costs of ESG, proponents might advance governance reforms that deliver on these objectives, that limit unchecked discretion by managers, and that establish checks for shareholder activism to protect minority shareholder interests. I argue that ESG governance is not as simple as assigning control rights to shareholders or to managers. Rather, it requires identifying the nature of an ESG objective, the new governance dynamics it engenders, the agency costs it creates and exacerbates, and devising mechanisms to account for them.

A. ESG's Principal-Agent Challenges

Because the current structure of corporate governance is premised on corporate purpose as shareholder primacy, traditionally interpreted to mean shareholder wealth maximization, deviations from this norm and an embrace of prosocial corporate purpose introduces new agency costs. In this section, I begin by identifying the basic premises of modern

⁷⁴ Michael C. Jensen & Richard S. Ruback, *The Market for Corporate Control: The Scientific Evidence*, 11 J. FIN. ECON. 5, 6, 40 (1983).

⁷⁵ *Id.* at 43–44 (describing strategies devised to limit agency and coordination problems). These measures depend on effective coordination among principals.

corporate governance and then go on to demonstrate how ESG problematizes these terms and introduces new agency costs.

From an agency perspective, a traditional corporate governance arrangement is premised on four key claims.

- Claim 1: Shareholders are the corporation's principals.
- Claim 2: Corporate principals have a shared preference of maximizing share value.
- Claim 3: Managers are agents of corporate principals.
- Claim 4: Corporate governance serves corporate purpose by aligning principals' preferences with agents' incentives.

A governance arrangement animated by the purpose of shareholder wealth maximization holds the first three claims constant, while competing ideologies disagree about how to best achieve the fourth claim. Managerialists seek increased discretion for directors and managers, while shareholder primacists seek a greater governance role for shareholders and stronger monitoring and disciplining mechanisms.

Replacing shareholder wealth maximization with socially oriented corporate purpose complicates this set-up. ESG proposals problematize claims about principals and their preferences, agents, and the purpose of corporate governance. A corresponding governance debate does not merely concern how to best align agents' incentives with principals' preferences, but must first identify the new principal-agent relationships that ESG generates and define shareholders' and managers' roles accordingly.

1. Principals

In practice, ESG is consistent with the claim that corporate principals are shareholders. Reforms attempt to accommodate their prosocial preferences within a traditional governance arrangement. However, proposed ESG governance paradigms in the form of managerial stakeholderism or codetermination⁷⁶

⁷⁶ Matthew Bodie argues that employees "have invested their labor, reputations, and firm-specific individual capital in the firm and cannot pull

redefine a corporation's principals to include stakeholders.⁷⁷ Most accounts gesture to stakeholders who affect and who are affected by a corporation's activities but fail to elaborate a limiting principle. These proposals lack a framework for selecting relevant stakeholders or for refereeing among their competing interests. This standard is practically unwieldy: for a major greenhouse gas emitter like ExxonMobil, for example, the entire global population is affected by its contributions to climate change.

2. Principals' Preferences

Multiple corporate principals with competing interests present coordination costs to the corporate governance process. Traditional corporate governance theory overcomes this challenge by assuming shareholder homogeneity.⁷⁸ However, ESG governance in the form of shareholder democracy modifies the premise that shareholders uniformly prefer wealth maximization and acknowledges competing shareholder preferences. Heterogeneity among shareholders requires a mechanism for interpreting preferences.⁷⁹

these investments out” and that that they are “more attached to the firm, and within the auspices of the firm, than the other stakeholders.” *The Next Iteration of Progressive Corporate Law*, 74 WASH. & LEE L. REV. 739, 755 (2017). While not in effect today, several states have codified codetermination statutes that would acknowledge workers as principals and grant them direct participation in governance. *See e.g.*, MASS. GEN. LAWS ANN. Ch. 156, § 23 (2018) (“A manufacturing corporation may provide by by-law for the nomination and election by its employees of one or more of them as members of its board of directors A director elected by the employees shall have the same rights and powers and shall be subject to the same duties and responsibilities as a director elected by the stockholders.”). *See also supra* notes 71, 72 and accompanying text.

⁷⁷ The composition of corporate principals under these accounts is highly contested. *See supra* notes 24, 25.

⁷⁸ Grant M. Hayden & Matthew T. Bodie, *One Share, One Vote and the False Promise of Shareholder Homogeneity*, 30 CARDOZO L. REV. 445, 477–98 (2008) (discussing the premise of shareholder homogeneity that is used to support shareholder primacy).

⁷⁹ The SEC's Staff Legal Bulletin 14L issued in November 2021 acknowledged and expanded the informational role of shareholder proposals

While managers already acknowledge some shareholder heterogeneity⁸⁰ concerning, for example, portfolio diversification, time horizon of investment, and majority versus minority interests, adding non-pecuniary preferences as a feature of shareholder heterogeneity exacerbates coordination costs among shareholders. Expanding the domain of shareholder preferences also invites expenditures associated with proxy contests. For example, McDonald's spent an estimated \$16 million in response to Carl Icahn's animal-welfare motivated proxy contest.⁸¹ As shareholders increasingly engage in socially motivated proxy contests, managers will have to divert more resources to defend against them.

3. Agents

Under current practice, ESG governance remains consistent with the claim that managers are agents of corporate principals: shareholder pluralists assume that shareholders are principals while managerialists assume that stakeholders are principals. ESG problematizes the role of managerial agents. Shareholder-centered ESG softens the separation of ownership and control as shareholders seek a more involved role in defining and administering ESG objectives.

A recent controversy concerning the activist fund Engine No. 1 demonstrates diverging interpretations of discretion that should be ceded to managerial agents, even among shareholders who, apparently, align on substantive ESG objectives. Engine No. 1 achieved notoriety in 2021 when it successfully replaced members on ExxonMobil's board with candidates

by removing limitations on the subjects that may be included in a proxy statement. SEC Legal Bulletin, *supra* note 66.

⁸⁰ See, e.g., GRANT M. HAYDEN & MATTHEW T. BODIE, *Shareholder Homogeneity*, in RECONSTRUCTING THE CORPORATION: FROM SHAREHOLDER PRIMACY TO SHARED GOVERNANCE 68 (2021).

⁸¹ Amelia Lucas, *Carl Icahn Loses Proxy Fight with McDonald's Over Animal Welfare*, CNBC (May 26, 2022), [https://www.cnbc.com/2022/05/26/carl-icahn-loses-proxy-fight-with-mcdonalds-over-animal-welfare.html#:~:text=Activist%20investor%20Carl%20Icahn%20lost,the%20treatment%20of%20pregnant%20pigs.\[https://perma.cc/VS47-EJDX\]](https://www.cnbc.com/2022/05/26/carl-icahn-loses-proxy-fight-with-mcdonalds-over-animal-welfare.html#:~:text=Activist%20investor%20Carl%20Icahn%20lost,the%20treatment%20of%20pregnant%20pigs.[https://perma.cc/VS47-EJDX]).

who would champion its climate change agenda. A year later, the fund faced criticism for voting against climate-related resolutions at Citi, Bank of America, and Wells Fargo.⁸² The proposals in question called on banks to adopt policies by the end of 2022 ensuring that their financing does not contribute to new fossil fuel supplies in keeping with International Agency Association's recommendations.⁸³ Engine No. 1's managing director explained that the proposals had too much micromanagement and "as written they did not provide adequate flexibility for banks to finance the fossil fuel and energy transition."⁸⁴ BlackRock adopted a similar position, observing that shareholder proposals concerning climate disclosures have been too "constraining" and "prescriptive."⁸⁵ This incident highlights that the scope of deference granted to agents and the reach of shareholder participation in governance remain disputed even by those who agree on corporate purpose.

Proposed ESG governance paradigms of shareholder democracy or codetermination problematize the claim that

⁸² Tim McDonnell, *The Hedge Fund That Beat Exxon Isn't Ready for a Climate Coup at Banks*, QUARTZ (Apr. 29, 2022), <https://qz.com/2160507/why-engine-1-voted-against-climate-proposals-at-big-banks/> [<https://perma.cc/RLJ3-ZJ6K>].

⁸³ TRILLIUM ASSET MGMT., *Proposal: Financing Consistent With IEA Net Zero 2050 Scenario* (2022), <https://collaborate.unpri.org/group/9996/stream> [<https://perma.cc/29PC-A4KP>]; HARRINGTON INV. & BOS. COMMON ASSET MGMT., *Proposal: "Financing Consistent With IEA Net Zero 2050 Scenario"* (2022), https://www.iccr.org/wp-content/uploads/2022/06/citigroup_2022_harrington_resolution.pdf [<https://perma.cc/MCX2-J7UR>]; SIERRA CLUB FOUND., *Proposal: Financing Consistent with IEA Net Zero 2050 Scenario* (2022), https://www.iccr.org/wp-content/uploads/2022/06/goldman_sachs_2022_sierra_club_foundation_1.pdf [<https://perma.cc/B622-ZZBP>].

⁸⁴ McDonnell, *supra* note 82.

⁸⁵ BLACKROCK, *2022 Climate-Related Shareholder Proposals More Prescriptive Than 2021* (May 2022), <https://www.blackrock.com/corporate/literature/publication/commentary-bis-approach-shareholder-proposals.pdf> [<https://perma.cc/46VN-9Y9G>] ("Having supported 47% of environmental and social shareholder proposals in 2021, BIS notes that many of the climate-related shareholder proposals coming to a vote in 2022 are more prescriptive or constraining on companies and may not promote long-term shareholder value.").

managers are agents of stakeholder principals. Shareholder democracy considers shareholders to be sponsors of stakeholder agendas, making them simultaneously agents to stakeholders and principals to managers. Under a codetermination paradigm, stakeholder representatives in the position of managers or directors are agents of their respective stakeholder principals.

4. Corporate Governance

A corporate governance paradigm allocates power between shareholders and managers based on how it interprets each of the above claims. Modifying one or more claims has implications for the overall governance structure. For example, if a proposal indicates that a corporation's principals are its stakeholders and that managers are their agents, then associated monitoring and bonding mechanisms⁸⁶ should be devised to align stakeholders and managers rather than shareholders and managers.

When governance reforms fail to account for the structural consequences of revised premises, they generate inefficiencies and unaccountable power.⁸⁷ For example, stakeholder constituency statutes in more than thirty states allow managers to take stakeholder interests into account in the context of a takeover.⁸⁸ They substitute shareholder principals with stakeholders, but do not modify bonding or monitoring mechanisms to account for this change. It comes as no surprise then that empirical analysis finds managerial agents failing to

⁸⁶ See Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 308 (1976). Bonding and monitoring mechanisms refer to the mechanisms that can limit divergences from principals' interest. Bonding costs refer to resources that principals will pay an agent to "guarantee that he will not take certain actions which would harm the principal or to ensure that the principal will be compensated if he does take such actions" while monitoring costs are "designed to limit the aberrant activities of the agent." *Id.*

⁸⁷ See generally Armour et al., *supra* note 73.

⁸⁸ See Lucian A. Bebchuk, Kobi Kastiel & Roberto Tallarita, *For Whom Corporate Leaders Bargain*, 94 S. CAL. L. REV. 1467, 1489 (2021).

deliver on the interests of stakeholder principals.⁸⁹ Substituting principals requires revised bonding and monitoring mechanisms that reflect the new agency relationship.

B. Shareholder Democracy's Agency Challenges

ESG governance in the form of shareholder democracy relies on expanding shareholder power through direct engagement. Shareholder democracy introduces both agency costs and coordination costs. At a first level, there are agency costs between stakeholders and their sponsors. At a second level, there are coordination costs among shareholders due to a plurality of nonpecuniary objectives. Shareholder democracy advocates propose no direct mechanisms for stakeholders to oversee their shareholder agents. Their proposal suffers from an ambiguous account of principals and from a nested agency problem.

1. Direct Shareholder Democracy

One related reform seeks to liberalize the shareholder proposal rule, SEC Rule 14a-8, to give shareholders a greater role in defining corporate ESG agenda.⁹⁰ Other proposed reforms include liberalizing proxy voting and other measures that give shareholders and asset managers greater power to pressure corporate managers.⁹¹

As shareholders increasingly engage in socially motivated proxy contests, managers have to divert more resources to defend against them—in turn generating costs for all shareholders. If, as in the case of Engine No. 1's campaign, an ESG objective is underwritten by a pecuniary logic, then these costs can be justified as promoting shareholder welfare in the long run. If, however, an ESG objective is purely idiosyncratic and expressive with no overt pecuniary rationale, then these costs

⁸⁹ *Id.* at 1524–25.

⁹⁰ SEC Legal Bulletin, *supra* note 66.

⁹¹ Kai Liekefett, Derek Zaba & Leonard Wood, *Welcoming the Universal Proxy*, HARV. L. SCH. FOR. ON CORP. GOVERNANCE (Aug. 8, 2022) <https://corpgov.law.harvard.edu/2022/08/08/welcoming-the-universal-proxy/> [<https://perma.cc/UDB2-3SUC>].

do not benefit all shareholders in the long run. As managers expend resources responding to niche agendas, some shareholders are taxed to advance the expressive preferences of other shareholders. One example is the proxy campaign waged by Carl Icahn in support of animal welfare rights in early 2022. Icahn waged a proxy contest against McDonald's board due to its failure to deliver on a commitment to end the use of gestation crates for pregnant sows.⁹² Icahn only owned roughly 200 shares of the company's then 744 million shares,⁹³ and he nominated two members to McDonald's board⁹⁴ with the express aim of advancing a nonpecuniary objective. McDonald's spent an estimated \$16 million defending against Carl Icahn's animal-welfare motivated proxy contest.⁹⁵

It is worth noting that shareholder democracy does not have inherent social or political valence—it is not inherently “woke” or progressive. It allows shareholders to advance their social or political preferences, whatever those happen to be. Today, ESG's advocates might strategically overlook governance shortcomings of shareholder democracy because of their progressive slant,⁹⁶ but this perspective is myopic. Corporate

⁹² Cara Lombardo, *Relentless Wall Street Billionaire Has a Secret Cause*, WALL ST. J., Feb. 8, 2022, <https://www.wsj.com/articles/carl-icahn-mcdonalds-pigs-gestation-crates-11644335198> [on file with the Columbia Business Law Review].

⁹³ See *Number of shares outstanding for McDonald (MCD)*, COMPANIES-MARKETCAP, <https://companiesmarketcap.com/mcdonald/shares-outstanding/#:~:text=Number%20of%20shares%20outstanding%20as,company%20had%20727%2C200%2C000%20shares%20outstanding> [https://perma.cc/TR2F-P2MY] (last visited Dec. 20, 2023).

⁹⁴ Cara Lombardo, *Carl Icahn Nominates Two to McDonald's Board*, WALL ST. J. (Feb. 20, 2022), <https://www.wsj.com/articles/icahn-nominates-two-to-mcdonalds-board-sources-say-11645390277> [on file with the Columbia Business Law Review].

⁹⁵ Amelia Lucas, *Carl Icahn Loses Proxy Fight with McDonald's over Animal Welfare*, CNBC (May 26, 2022), <https://www.cnbc.com/2022/05/26/carl-icahn-loses-proxy-fight-with-mcdonalds-over-animal-welfare.html> [https://perma.cc/8DL2-FVHY].

⁹⁶ See, e.g., Stephen M. Bainbridge, *Corporate Purpose in a Populist Era*, 98 NEB. L. REV. 543, 573–76 (2020) (noting that the values of elites and

governance arrangements that are used to advance a progressive agenda today, through insulated managerial discretion or portfolio regulation by institutional investors, could conceivably be harnessed to pursue prosocial, antisocial, or neutral ends. Consider the hypothetical example of an activist shareholder who seeks to promote a gun rights agenda. He might lobby retailers, like Walmart and Dick's Sporting Goods, to adopt retail decisions that expand access to assault style weapons at every retail location across the country in the interest of vindicating a Second Amendment agenda. While selecting product mix is typically a managerial consideration, he promotes specific product stocking even when it does not serve retail efficiency. The point of this example is that shareholder participation should not be considered a panacea for pro-social corporate behavior and that structural accountability for non-pecuniary shareholder participation is critical to achieving accountable and efficient governance. Corporate prosociality does and will remain dependent on the set of preferences that a corporation's principals adopt and advance through available mechanisms.

A pragmatic defense of shareholder democracy argues that it overcomes agency costs that would otherwise be generated through managerial stakeholderism. However, this proposition is not borne out through structural reform: shareholder democracy advocates have not proposed to give stakeholders any power over shareholders. The focus instead, in policy and in scholarship, has been on minimizing agency costs between managers and their pluralist shareholders.⁹⁷ Rather than

non-elites have been diverging for decades, and that corporate elite social activism leans liberal).

⁹⁷ Roberto Tallarita focuses on the monitoring problem presented by pluralist shareholder preferences. He notes that "corporate managers may make socially relevant decisions that do not reflect the social and political preferences of shareholders," but most shareholders lack "sufficient incentives to monitor and correct the decisions made by corporate managers." Tallarita explains that a small number of specialized players cooperate across companies and industries to mitigate this agency problem, providing a solution to the type of coordination problem identified by Armour et al., *supra* note 73, at 36. See Tallarita, *supra* note 63, at 1704, 1733, 1742. Adi Libson also proposes two solutions to the agency costs of shareholder

overcome the agency costs of managerial stakeholderism, shareholder democracy merely displaces them from a management-stakeholder agency relationship to a shareholder-stakeholder agency relationship.

2. Intermediated Shareholder Democracy

The rise of large asset managers advancing ESG agendas also presents a nested agency problem.⁹⁸ Institutional investors are simultaneously agents of their underlying investors and principals of corporate managers. The agency problems traditionally observed between retail shareholders and corporate executives manifest at a subsidiary level between investors and intermediary asset managers. This dynamic has flagged regulatory attention,⁹⁹ and asset managers have begun to innovate solutions. BlackRock recently began allowing certain of its clients to vote their shares directly on shareholder proposals, director elections, and takeovers,¹⁰⁰ but the

pluralism: a bottom-up model that relies on shareholder proposals and a top-down model that functions through an independent board subcommittee. See Adi Libson, *Taking Shareholders' Social Preferences Seriously: Confronting a New Agency Problem*, 9 U.C. Irvine L. Rev. 699, 699 (2019).

⁹⁸ John C. Coates, *The Future of Corporate Governance Part I: The Problem of Twelve*, 19 (Harv. Pub. L. Working Paper No. 19-07,2018), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3247337 [<https://perma.cc/HF2E-K49C>] (“A small number of unelected agents, operating largely behind closed doors, are increasingly important to the lives of millions who barely know of the existence much less the identity or inclinations of those agents.”); 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, 863 (2013).

⁹⁹ See, e.g., *Considering the Index Fund Voting Process: Hearing on S. 4241 Before the S. Comm. on Banking, Housing, and Urban Affairs*, 117th Cong. (Jun. 14, 2022), <https://www.banking.senate.gov/hearings/considering-the-index-fund-voting-process> [<https://perma.cc/N5D8-GJJH>]; Investor Democracy is EXpected Act, S. 4241, 117th Cong. (2022).

¹⁰⁰ In his 2022 letter, Larry Fink referred to Blackrock’s recent voting policy change as a way “to give more of our clients the option to have a say in how proxy votes are cast at companies their money is invested in.” He justifies this move as bringing “more democracy and more voices to capitalism.” Larry Fink, *The Power of Capitalism*, BLACKROCK,

percentage of owners doing so remains small.¹⁰¹ Other proposals would require asset managers to ask shareholders how they want to vote through such approaches as “index proxy polling”¹⁰² or to pass legislation requiring government pension-fund managers to vote a state’s shares directly.

C. Managerialism’s Agency Challenges¹⁰³

The second leading ESG governance proposal relies on granting managers a widened scope of discretion, protected by the business judgment rule. Whether in the form of

<https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter> [<https://perma.cc/AX66-H2NC>] (last visited Dec. 22, 2023).

¹⁰¹ BlackRock’s new voting policy applies to about 40% of the \$4.8 trillion in assets invested in its equity index strategies, which comprise about half of assets under management. See Simon Jessop & Ross Kerber, *BlackRock to Give Clients More Say on Holding Companies to Account*, REUTERS (Oct. 7, 2021), <https://www.reuters.com/business/finance/blackrock-give-clients-more-say-holding-companies-account-2021-10-07/> [on file with the Columbia Business Law Review]. BlackRock reported that owners of more than \$530 billion of its \$11 trillion in assets under management are now voting their shares directly. This comprises 4.8% of BlackRock’s total assets. See, Brooke Masters, *BlackRock Investors Taking Voting Power amid Scrutiny of Asset Managers*, FIN. TIMES (June 13, 2022), <https://www.ft.com/content/7fd8d6ff-0120-4095-9a0e-a2729e2014e1> [<https://perma.cc/8PAC-DKWL>]. In a June 2022 whitepaper, BlackRock, with an objective of democratizing participation in proxy voting, indicated that it would be expanding client eligibility for its “Voting Choice” program and signaled its ambition to expand choice to “all investors, including individual investors in funds.” See BLACKROCK, *IT’S ALL ABOUT CHOICE: EMPOWERING INVESTORS THROUGH BLACKROCK VOTING CHOICE 3* (2022), <https://www.blackrock.com/corporate/literature/publication/its-all-about-choice.pdf> [<https://perma.cc/7L7P-MY8D>].

¹⁰² See Jeff Sommer, *A Glimpse of a Future with True Shareholder Democracy*, N.Y. TIMES (May 21, 2021), <https://www.nytimes.com/2021/05/21/business/stock-funds-shareholder-democracy.html> [on file with the Columbia Business Law Review].

¹⁰³ Managerial Stakeholderism and Enlightened Shareholder Primacy are distinct ESG paradigms with differing ends (stakeholder welfare in the case of the former and shareholder welfare in the case of the latter). However, from a governance perspective they share a parallel set of agency challenges between managers and stakeholders, in the case of the former, or managers and shareholders, in the case of the latter.

managerial stakeholderism¹⁰⁴ or enlightened shareholder primacy,¹⁰⁵ managerialism introduces agency costs, as stakeholders and managers have no principal-agent relationship.

1. Managerial Stakeholderism

Managerial stakeholderism as a governance proposal is evidenced in the Business Roundtable 2019 *Statement on the Purpose of the Corporation*. More than 200 CEO members of the Business Roundtable affirmed a commitment to stakeholder governance, “outlin[ing] a modern standard for corporate responsibility” and asserting “a fundamental commitment to all of [a company’s] stakeholders.”¹⁰⁶ The statement was characterized as a radical departure from fifty years of shareholder primacy,¹⁰⁷ “reframing the purpose of business and corporations as stakeholder value, not solely shareholder value.”¹⁰⁸ Signatory CEOs have staked out positions on nearly every recent political or social issue of national importance, including racial justice, LGBTQ rights, gun control, abortion rights, immigration, and many others.¹⁰⁹ Managers justify

¹⁰⁴ See *supra* Section II.C.2.

¹⁰⁵ See *supra* Section II.C.1.

¹⁰⁶ *Business Roundtable Redefines the Purpose of a Corporation to Promote ‘An Economy That Serves All Americans,’* BUS. ROUNDTABLE (Aug. 19, 2019), <https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans> [<https://perma.cc/2ABU-8QGC>].

¹⁰⁷ David Gelles & David Yaffe-Bellany, *Shareholder Value Is No Longer Everything, Top C.E.O.s Say*, N.Y. TIMES (Aug. 19, 2019), <https://www.nytimes.com/2019/08/19/business/business-roundtable-ceos-corporations.html> [on file with the Columbia Business Law Review].

¹⁰⁸ Jim Ludema & Amber Johnson, *The Purpose of the Corporation? Business Roundtable Advances the Conversation, Now We All Need to Contribute*, FORBES (Aug. 20, 2019), <https://www.forbes.com/sites/amberjohnson-jimludema/2019/08/20/the-purpose-of-the-corporation/?sh=62d47cd33846> [<https://perma.cc/X82T-9ABY>].

¹⁰⁹ See, e.g., *‘Bathroom Bill’ to Cost North Carolina \$3.76 Billion*, CNBC (Mar. 27, 2017), <https://www.cnbc.com/2017/03/27/bathroom-bill-to-cost-north-carolina-376-billion.html> [<https://perma.cc/PM7B-EV2C>] (discussing corporate reaction to N.C. HB2, including actions by PayPal, Deutsche Bank, and Adidas); David Gelles, *The C.E.O. Taking on the Gun Lobby*, N.Y. TIMES (Oct. 25, 2019),

deploying the corporation's brand and its resources in political debate as a counterbalance to government, claiming that "corporate America holds government accountable and speaks out on important issues."¹¹⁰

<https://www.nytimes.com/2019/10/25/business/ed-stack-dicks-sporting-goods-corner-office.html> [on file with the Columbia Business Law Review] (discussing corporate activism on gun control by companies including Walmart and Dick's Sporting Goods); Alex Hern, *Apple, Google, Facebook and Microsoft File Opposition to Trump's Travel Ban*, GUARDIAN (Feb. 6, 2017), <https://www.theguardian.com/technology/2017/feb/06/apple-google-facebook-microsoft-file-opposition-to-donald-trump-immigration-ban> [<https://perma.cc/9ERP-42PN>] (discussing nearly 100 technology companies filing an amicus brief opposing President Donald Trump's travel ban on seven predominantly Muslim countries); Tiffany Hsu, *Corporate Voices Get Behind 'Black Lives Matter' Cause*, N.Y. TIMES (May 31, 2020), <https://www.nytimes.com/2020/05/31/business/media/companies-marketing-black-lives-matter-george-floyd.html> [on file with the Columbia Business Law Review] (discussing corporate support of the Black Lives Matter movement including companies like Nike, Twitter, Citigroup, and Netflix); Emily Glazer & Chip Cutter, *How the Capitol Riot Thrust Big American Companies Deeper into Politics*, WALL ST. J. (Jan. 15, 2021), <https://www.wsj.com/articles/capitol-riot-business-trump-biden-11610591424> [on file with the Columbia Business Law Review] (discussing corporate actions taken by Twitter, Simon & Schuster, Airbnb, Stripe, and others in the wake of the U.S. Capitol riot); David Gelles & Andrew Ross Sorkin, *Hundreds of Companies Unite to Oppose Voting Limits, but Others Abstain*, N.Y. TIMES (Apr. 14, 2021), <https://www.nytimes.com/2021/04/14/business/ceos-corporate-america-voting-rights.html> [on file with the Columbia Business Law Review] (discussing the decisions of Amazon, BlackRock, Google, and other companies to sign onto a statement opposing discriminatory voting legislation); Emma Goldberg & Lora Kelley, *Companies Are More Vocal Than Ever on Social Issues. Not on Abortion.*, N.Y. TIMES (Jun. 24, 2022), <https://www.nytimes.com/2022/06/24/business/abortion-roe-wade-companies.html> [on file with the Columbia Business Law Review] (discussing a range of corporate actions after *Dobbs v. Jackson Women's Health Organization*, where some companies, like Starbucks, Tesla, Yelp, and others, said they would cover employee travel expenses for abortions).

¹¹⁰ Clare Duffy, *Lyft General Counsel: I Hope That More of Corporate America Takes a Stand on Texas Abortion Law*, CNN (Sept. 6, 2021), <https://www.cnn.com/2021/09/06/tech/lyft-general-counsel-texas-abortion-law-response/index.html> [<https://perma.cc/LC4Y-FPJK>] (interviewing Lyft's general counsel who defended the company's stance as executives

Managerial stakeholderism is vulnerable to the critique that the expanded discretion required to account for stakeholder interests will serve as cover for managerial rent-seeking. As a matter of governance, managers are accountable to shareholders who are granted a franchise¹¹¹ that allows them to modify a charter or bylaws,¹¹² to initiate and vote in proxy contests,¹¹³ and to submit and vote on shareholder proposals.¹¹⁴ In some cases, managers are influenced by labor, like high skill tech workers at Google and Amazon, or consumers, like those for companies that are highly brand sensitive and consumer facing like Disney, but managers are not structurally accountable to these stakeholders.¹¹⁵

Extending managerial accountability to stakeholders presents several problems. First is the problem of defining

doing what they see as right and asserted that founders and CEOs have responsibilities regarding issues not directly relevant to their business).

¹¹¹ Martin Lipton & William Savitt, *Stakeholder Governance—Issues and Answers*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Oct. 25, 2019), <https://corpgov.law.harvard.edu/2019/10/25/stakeholder-governance-issues-and-answers/> [<https://perma.cc/7JAF-6M4E>] (“Insightful commentators accurately emphasize that shareholders alone enjoy the corporate franchise, and with it the power to select directors.”).

¹¹² *Boilermakers Local 154 Ret. Fund v. Chevron Corp.*, 73 A.3d 934, 956 (Del. Ch. 2013) (“[T]he statutory regime provides protections for the stockholders, through the indefeasible right of the stockholders to adopt and amend bylaws themselves.”). *But see* Jill Fisch, *Governance by Contract: The Implications for Corporate Bylaws*, 106 CAL. L. REV. 373, 373 (2017) (recognizing shareholders’ power to modify a charter or bylaws while noting that in practice this power is more limited than the board’s).

¹¹³ Alon Brav, Wei Jang, Tao Li & James Pinnington, *Shareholder Monitoring Through Voting: New Evidence from Proxy Contests*, 37 Rev. Fin. Stud. 591, 592 (2024).

¹¹⁴ See 17 C.F.R. §240.14a-8. See also James D. Cox and Randall S. Thomas, *The SEC’s Shareholder Proposal Rule: Creating a Corporate Public Square*, 2021 COLUM. BUS. L. REV. 1147. Notably, shareholder proposals are precatory, and companies may exercise their discretion in excluding proposals according to certain enumerated criteria. See *infra* notes 140–45.

¹¹⁵ See, e.g., Daisuke Wakabayashi and Scott Shane, *Google Will Not Renew Pentagon Contract That Upset Employees*, N.Y. TIMES (Jun. 1, 2018), <https://www.nytimes.com/2018/06/01/technology/google-pentagon-project-maven.html> [<https://perma.cc/G4NF-74WW>] (describing Google abandoning its contract with the Pentagon after employees protested Project Maven).

stakeholders with adequate precision to make their interests administrable. Ann Lipton has advanced stakeholder disclosures as one form of oversight and accountability.¹¹⁶ Where they have been attempted in the example of voluntary sustainability reports, however, they are rife with greenwashing and inaccuracies.¹¹⁷

Second is a problem of conflicting agendas advanced by different shareholders. Even those who agree on the objective of mitigating climate change, for example, will disagree about the desirable strategies and decisions required to achieve that end. Where corporate ends are simply profit, discretion is categorically delegated to management. Where corporate ends are nonpecuniary, however, the boundary between shareholder expression and micro-management is more contestable.

Third is the problem of reconciling between shareholder interests and stakeholder welfare when these come into conflict. Fiduciary duties create a clear agency relationship that grants shareholder principals standing to seek remedies when managerial agents do not account for their interests. However, expanding the class of principals without a corresponding revision of managers' fiduciary duties to principals creates an opportunity for rent-seeking. For the well-meaning manager, this arrangement fails to provide guidance for how to negotiate tradeoffs between stakeholders when choosing between radically different strategies, timelines of performance, and nonpecuniary benefits.

To date, managerialism has been legally codified in two specific examples: stakeholder constituency statutes and public benefit corporation (PBC) statutes. Stakeholder

¹¹⁶ Ann Lipton, *Not Everything is About Investors: The Case for Mandatory Stakeholder Disclosure*, 37 YALE J. REG. 499 (2020).

¹¹⁷ Kenneth P. Pucker, *Overselling Sustainability Reporting*, HARV. BUS. REV., May–Jun. 2021, <https://hbr.org/2021/05/overselling-sustainability-reporting> [<https://perma.cc/GSP4-6J2K>] (“It turns out that reporting is not a proxy for progress. Measurement is often nonstandard, incomplete, imprecise, and misleading.”).

constituency statutes have been adopted by more than thirty states¹¹⁸ and allow corporate managers to take stakeholder interests into account in the context of a takeover.¹¹⁹ PBC statutes in 36 states provide a governance framework that grants managers an explicit mandate to incorporate stakeholder interests into their decision-making.¹²⁰ They allow shareholders a greater role in setting out specific purposes at the founding stage, but delegate operationalization to managers as consistent with the conventional corporate form.

In practice thus far, managerialist stakeholderism has not ceded any power to stakeholders. An empirical critique has been elaborated by Lucian Bebchuk and colleagues from many angles, including stakeholderists' failure to reflect their commitment to stakeholderism in their governance guidelines and the misalignment between executive compensation metrics and ESG objectives, among others.¹²¹ They have characterized stakeholderism as an "illusory promise" that is not administrable given the limits of managerial agency. If executive compensation is not linked to profit, what is it linked to? If disclosures are not limited to materiality, what sets parameters for oversight?

Understood through an agency lens, both stakeholder constituency statutes and PBC statutes rhetorically refer to

¹¹⁸ Thirty-three states have at some point had shareholder constituency statutes; twenty-nine of these do not have opt-in or opt-out mechanisms. *See* Bebchuk et al., *supra* note 88, at 1489–90.

¹¹⁹ These statutes are often heralded by stakeholder governance advocates as an example of how stakeholder interests may be incorporated into corporate law. However, their practical effect has been dismissed in scholarship by Lucian Bebchuk, Kobi Kastiel, and Roberto Tallarita who find that, as a matter of practice, managers seldom bargain for stakeholder interests. *Id.* at 1490.

¹²⁰ *See, e.g.*, 8 Del. C. 362(a) (A public benefit corporation "is intended to produce a public benefit or public benefits and to operate in a responsible and sustainable manner" and "shall be managed in a manner that balances the stockholders' pecuniary interests, the best interests of those materially affected by the corporation's conduct, and the public benefit or public benefits identified in its certificate of incorporation.").

¹²¹ *See, e.g.*, Bebchuk & Tallarita, *supra* note 54; Bebchuk et al., *supra* note 88; Bebchuk & Tallarita, *supra* note 22.

managers as the agents of stakeholder principals. Practically, however, they expand managerial discretion without providing any corresponding oversight or accountability mechanism under the control of stakeholder principals.

2. Enlightened Shareholder Primacy

Enlightened shareholder primacy can be applied to some ESG objectives more easily than others. For some ESG objectives, related decisions have an obviously rational business purpose, like a Human Capital Management (HCM) agenda that considers workers as corporate “assets” that should be managed like its physical and capital assets.¹²² Other decisions are more expressive and present a tenuous pecuniary connection. One example is Disney lobbying against a Florida education bill prohibiting instruction on sexual orientation or gender identity in public elementary schools.¹²³ The bill doesn’t have a direct operational nexus to Disney, focusing on Florida public school curricula. However, sufficient employee discontent in response to Disney’s agnostic position or a consumer boycott reacting to Disney’s symbolic position on the controversial political matter could result in Disney’s activism acquiring a rational business connection. Another example is Walmart and Dick’s Sporting Goods’ decisions to remove assault rifles from their retail inventory. This decision has a direct business nexus, concerning the stocking of specific products, but is justified with the principled objective of advancing social welfare rather than maximizing profit.¹²⁴ A third

¹²² George S. Georgiev, *The Human Capital Management Movement in U.S. Corporate Law*, 95 TULANE L. REV. 639, 644, 660 (2021).

¹²³ Robbie Whelan & Joe Flint, *Disney Chief Bob Chapek Takes Stand on Florida’s Parental Rights in Education Bill*, WALL ST. J. (Mar. 9, 2022), <https://www.wsj.com/articles/disney-chief-bob-chapek-takes-stand-on-floridas-parental-rights-in-education-bill-11646866002> [<https://perma.cc/TDA4-3QFL>].

¹²⁴ Edward W. Stack, *Dick’s CEO to high school gun protesters: We have heard you*, THE DALLAS MORNING NEWS (Feb. 28, 2018), <https://www.dallasnews.com/opinion/commentary/2018/02/28/dick-s-ceo-to-high-school-gun-protesters-we-have-heard-you/> [<https://perma.cc/UM7E-4743>] (“We hope others join us in this effort to let our kids know that their pleas are

example is Lyft and Uber’s advocacy against a Texas abortion law. The ridesharing companies presented their advocacy as a matter of political freedom and human rights, while simultaneously protecting the interests of their drivers who might face potential legal liability under the new law.¹²⁵ In these examples, ESG complicates the “rational business purpose” that limits the business judgment rule, and, with it, the appropriate scope of managerial discretion under an enlightened shareholder primacy paradigm.

Under current doctrine, hybrid pecuniary and expressive ESG decisions leave managers vulnerable to shareholder oversight unless they can attribute such decisions to a rational business purpose. Managers can and generally do avoid this risk by couching their social and political decisions in terms of long-term profit. Supposing that even the long-term objective of wealth-creation were removed as a limiting factor to “rational” business purposes, as managerialists advocate, the agency costs of such discretion are potentially very high. With such a liberal standard, managers could advance their own idiosyncratic values at the expense of shareholder welfare or use the pursuit of social objectives as cover for self-enrichment.

Where decisions are made under the pretense of principle but have a strategic objective, such as generating employee loyalty or consumer goodwill, disclosing the true objective undermines the instrumental function of such *woke washing* and undermines its *rational business* value. These instrumental motives are not, on their face, distinguishable from those made for a sincerely expressive purpose. The entanglement of

being taken seriously. Some will say these steps can’t guarantee tragedies like Parkland will never happen again. They may be correct - but if common sense reform is enacted and even one life is saved, it will have been worth it. We deeply believe that this country’s most precious gift is our children. They are our future. We must keep them safe.”).

¹²⁵ See, e.g., Logan Green (@logangreen), X, <https://twitter.com/logangreen/status/1433872535288827911> [<https://perma.cc/48DE-QUZR>] (“This is an attack on women’s access to healthcare and on their right to choose. @Lyft is donating \$1 million to Planned Parenthood to ensure that transportation is never a barrier to healthcare access. We encourage other companies to join us.”).

social and business motivations that characterizes most ESG decisions problematizes the boundaries of the business judgment rule and increases the risk that ESG will be used as cover for managerial rent-seeking.

IV. AN ALTERNATIVE: CORPORATE TECHNOCRACY

At its inception nearly two decades ago, ESG promised to reconcile profit with purpose by linking environmental, social, and corporate governance objectives with corporate financial performance.¹²⁶ The success of this proposition hinged on the premise that social welfare is financially material. Accordingly, good governance could reconcile between profit and purpose by translating valent and contested stakeholder matters into material and measurable elements amenable to routine management. The durability of this premise, however, entails considerable epistemic oversimplification. This has become apparent in the resulting democratic deficit that arises when politically valent ESG judgments are delegated to shareholder democrats or to managerial autocrats. In this section, I argue that a technocratic paradigm offers a framework that is more conducive to meeting the unique governance challenges of ESG, while reckoning with its political and administrative facets.

As elaborated in Part III, both shareholder democracy and managerialism fail, in theory and in practice, to account for the novel agency challenges presented by ESG. In this Part, I argue that a technocratic model overcomes the structural shortcomings of both paradigms and that it accounts for the agency relationships that characterize ESG governance while offering practical reforms to strengthen institutional accountability.¹²⁷ Technocracy accommodates the liminal and

¹²⁶ UNITED NATIONS ENVIRONMENT PROGRAMME, *THE MATERIALITY OF SOCIAL, ENVIRONMENTAL AND CORPORATE GOVERNANCE ISSUES TO EQUITY PRICING* 3 (2004), https://www.unepfi.org/fileadmin/documents/amwg_materiality_equity_pricing_report_2004.pdf [<https://perma.cc/UA9F-Q4LC>].

¹²⁷ The epistemic complexity complicating governance concerned democratic theorists of the early 20th century. A famous debate between Walter Lippmann and John Dewey grappled with the challenges of governing a

controversial nature of ESG’s “materiality” and provides a normatively and practically defensible solution to the complexities of ESG governance.

This Part begins in Section A by elaborating the merits of a corporate technocracy when dealing with the unique governance challenges of ESG. It goes on in Section B to identify three main structural features of a corporate technocratic regime. Finally, in Section C it elaborates three applications of the corporate technocracy in the examples of ESG goals of climate risk; corporate political speech; and diversity, equity, and inclusion (DEI).

A. The Case for Corporate Technocracy

Technocracy, or rule by experts, translates political objectives into measurable criteria that correspond with a governing body’s animating mandate. In place of charismatic political leadership or a deliberative democratic process, it advances a form of managerialism encumbered by a technical rationality, measurement, and administration by expertise. Technocracy offers a framework for operationalizing the ends of ESG while emphasizing procedural accountability and measurability, and curbing managerial rent-seeking. It limits the parameters of managerial discretion and rationalizes shareholder involvement as serving an informational rather than political function. Technocratic governance offers an alternative to ideologically driven pro-shareholder or pro-manager agendas and a framework that recognizes principal costs and agent costs with the objective of balancing power between the two groups.

Technocratic governance emphasizes technically capable administrators implementing a pre-determined mandate. In the corporate context, this can be found in the corporate purpose drafted by a corporation’s founders in its charter (“Purpose”). Corporate Purpose refers to long-term corporate

complex, modern society where even those who agree roughly on the meaning of the public good disagree on how to achieve it. *See* WALTER LIPPMANN, *THE PHANTOM PUBLIC* 67–68 (1925); JOHN DEWEY, *THE PUBLIC AND ITS PROBLEMS* 216 (1927).

welfare distinguished from short-term shareholder returns, direct shareholder expression, or management's political activism.¹²⁸ Unless specified otherwise, a corporation's presumptive Purpose under Delaware doctrine is shareholder value creation. This can be considered the default doctrinal rule that shareholders are assuming when they buy into a company. Accordingly, a corporate technocracy assumes corporate principals to be those recognized in the charter, namely shareholders, unless otherwise provided for by a codetermination clause, for example. Managers are their agents and managerial discretion, viewed through a technocratic lens, serves to operationalize corporate Purpose. It accounts for stakeholder interests only in so far as they are material to that Purpose.

ESG, then, can be characterized as a subsidiary set of "purposes" that are essentially judgments about the means used to achieve Purpose. Shareholders can revise Purpose,¹²⁹ but as a routine matter their contribution to defining ESG is one input among others that inform material considerations and risks as they pertain to corporate Purpose. This limitation to the shareholders' role, far short of a "shareholder democracy," preserves minority shareholder rights and prevents micromanagement. From this perspective, the costs of shareholder activism with an overtly nonpecuniary motive, like Carl Icahn's ESG-motivated proxy campaigns against Kroger and McDonald's,¹³⁰ should be borne by the activist rather than taxed to other shareholders. This is distinguishable from Engine No. 1's ESG-motivated proxy campaign against

¹²⁸ See, e.g., Millon, *supra* note 18, at 1014 (consistent with "traditional shareholder primacy" that is oriented towards long-term corporate value, and distinguished from "radical shareholder primacy" that is oriented towards short term shareholder wealth maximization). A lower case reference to corporate purposes denotes the more specific objectives that contribute to achieving its overall Purpose.

¹²⁹ Shareholders always have the option of redefining Purpose through charter amendments and bylaw provisions that go through a complete ratification procedure. See 8 Del. C. §242 (procedure by which a certificate of incorporation may be amended after receipt of payment for stock); 8 Del. C. §109 (procedure by which bylaws may be amended).

¹³⁰ *Supra* notes 92-95 and accompanying text.

ExxonMobil, which was professedly motivated by a pecuniary rationale and which characterized its climate objectives in material terms.¹³¹ Managerial authority is restrained by fiduciary duties to shareholders, limited by the terms of materiality to furthering rational business purposes, and enhanced by institutional features that increase managerial capacity, improve legibility of their decisions, and provide for corresponding oversight by those who wield the franchise.

By reframing ESG governance as a technocratic project I am not eliding the fundamentally political nature of this epistemic endeavor, particularly in defining and contesting “materiality.”¹³² Rather, I’m advancing the benefits of technocracy for encumbering an unfettered managerialism with the rationale of materiality and imposing on political judgments the logic of Purpose. This relies on identifying the attributes of technical expertise required to achieve the ends of ESG, problematizing and identifying mechanisms to contest and define materiality, and identifying the proper scope and space for shareholder and stakeholder participation as a channel for informing technocracy.

B. Key Features of the Corporate Technocracy

In this section, I identify three main features of a corporate technocracy intended to promote efficient and accountable ESG governance: 1) encouraging ESG specific skills and experiences among managers and board members, 2) adopting materiality as a limit to managerial discretion, and 3) creating channels for stakeholders and shareholders to inform ESG materiality.

1. A Skills Matrix for Technocrats

Technocracy depends on the decision-making of competent administrators with relevant skills and expertise. Where a corporation’s purpose is the pursuit of profit, the skills and

¹³¹ *Supra* notes 82-84 and accompanying text.

¹³² For a critical account of technocracy and technocratic measurement, see JEFFREY FRIEDMAN, *POWER WITHOUT KNOWLEDGE: A CRITIQUE OF TECHNOCRACY* 1–31 (2019).

attributes required of its executives differ from the expertise that might be required by a more socially oriented entity. One way to enhance institutional ESG competence is to adopt a version of the “skills matrix” disclosed by some companies in their annual filings, in the form of an ESG skills matrix. An ESG skills matrix should reflect not just specific ESG objectives that a company prioritizes, but also attributes and experiences it seeks to promote among its decision-makers.¹³³

In the current version of a skills matrix, the names of incumbent directors are plotted against attributes like specific industry experience, government/public policy expertise, or marketing/sales skills.¹³⁴ This information provides a better understanding of directors’ specific skills and attributes and increases the board’s accountability with respect to the criteria listed while also demonstrating collective skills gaps. Linking skills disclosure to director nominations, for example, allows shareholders to understand why a candidate was chosen for election or to nominate candidates who complement the skills mix where gaps are unfilled. For companies promoting ESG, a skills matrix would allow them to institutionalize these priorities as part of an administrative rationale. Skills and experiences included in a matrix can reflect a company’s strategy and the ESG priorities of its respective industry. For example, companies in the oil and gas sector might include expertise in environmental science or climate risk as target skills. Companies can also account for relevant expertise that is not represented at the board level by supplementing it with

¹³³ GLASS LEWIS, DISCLOSURE OF BOARD SKILLS AND EXPERIENCE—EMERGING BEST PRACTICE 5 (2018), https://www.glasslewis.com/wp-content/uploads/2019/02/BoardSkillsand_Experience.pdf [<https://perma.cc/7Z9S-EZAK>]; Charles-Etienne Borduas, Thierry Dorval, Audrey Bernasconi & Sophie Doyle, *ESG: What boards of directors should do now*, NORTON ROSE FULBRIGHT (Aug. 16, 2021), <https://www.nortonrosefulbright.com/en-ca/knowledge/publications/bed17bb0/esg-what-boards-of-directors-should-do-now> [<https://perma.cc/CKL4-ETQ9>].

¹³⁴ Following a 2014 recommendation from the ASX Corporate Governance Council. *See* ASX CORPORATE GOVERNANCE COUNCIL, CORPORATE GOVERNANCE PRINCIPLES AND RECOMMENDATIONS 13 (4th ed. Feb. 2019), <https://www.asx.com.au/documents/asx-compliance/cgc-principles-and-recommendations-fourth-edn.pdf> [<https://perma.cc/YE56-LE4F>].

information about how the board has access to these skills or expertise through internal or external experts, for example, or with ways that the board is kept informed of relevant developments through reporting by a relevant management committee. The ESG skills profile might be subject to regular assessment and revised to reflect priorities and strategies and evolving interpretations of ESG.¹³⁵

2. Materiality as a Limit to Managerial Discretion

The notion of “materiality” is fundamental to a corporate technocracy and serves as both the space of contestation concerning which pro-social objectives are institutionalized in corporate decision-making, and the boundaries of managerial discretion protected by the business judgment rule. Under current doctrine, information is “material” if it is relevant to a “reasonable investor”¹³⁶ when deciding to purchase or sell securities.¹³⁷ Under a technocratic governance regime,

¹³⁵ See GLASS LEWIS, *supra* note 133, at 8.

¹³⁶ TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 445 (1976) (“The question of materiality, it is universally agreed, is an objective one, involving the significance of an omitted or misrepresented fact to a reasonable investor. Variations in the formulation of a general test of materiality occur in the articulation of just how significant a fact must be or, put another way, how certain it must be that the fact would affect a reasonable investor’s judgment.”).

¹³⁷ Several corporate and securities law doctrines distinguish between material and immaterial information when determining the type of information that shareholders should have access to and that managers and directors should consider in keeping with their fiduciary duties. These include the scope of mandatory SEC disclosures, the types of corporate statements or omissions deemed actionable under Section 10-b litigation, the types of risks requiring managerial oversight under *Caremark*, and information that directors must consider in fulfilling their fiduciary duty of care. See, e.g., BUS. ROUNDTABLE, THE MATERIALITY STANDARD FOR PUBLIC COMPANY DISCLOSURE: MAINTAIN WHAT WORKS (Oct. 2015), <https://s3.amazonaws.com/brt.org/archive/reports/Materiality%20White%20Paper%20FINAL%2009-29-15.pdf> [<https://perma.cc/P2PT-ZXKM>]; Becker, Exchange Act Release No. 44460, 2001 WL 698370 (Jun. 21, 2001); Smith v. Van Gorkom, 488 A.2d 858, 872 (1985) (quoting Aronson v. Lewis, 473 A.2d 805, 812 (1984)) (holding that directors must inform themselves “prior to making

political and value-laden objectives are made *legible* through a translation process that casts them in terms that are material and measurable.

Shareholders and stakeholders seeking to make the case for ESG materiality have several available avenues. First, they might lobby to expand the types of issues considered financially material based on specific industry features. Second, they might push a legal interpretation of materiality that captures nonfinancial aspects of corporate performance in the form of “double materiality” or “dynamic materiality.”¹³⁸ Third, they might problematize the “reasonable investor” standard by showing that “reasonable investors” are increasingly concerned with ESG and therefore require mandatory disclosures corresponding with their respective prosocial objectives and agendas. As ESG materiality is contested and redefined, this has implications for information that managers are under a duty to disclose, the risks they must oversee, and the statements and commitments that are actionable under shareholder suits.

3. Informing Materiality Through Shareholders and Stakeholders

Technocracy overcomes the challenge of indeterminate principals that stakeholderism has persistently encountered. It characterizes shareholders’ and stakeholders’ role in ESG governance as informational rather than political. Both shareholders and stakeholders are a vital source of information for understanding ESG materiality. In the example of the COVID pandemic, Stavros Gadinis and Amelia Miazad elaborated managers’ reliance on stakeholders to gather information about work practices.¹³⁹ A review of managers’ decision-

a business decision, of all material information reasonably available to them”).

¹³⁸ See Donato Calace, *Double and Dynamic: Understanding the Changing Perspectives on Materiality*, SASB (Sept. 2, 2020), <https://sasb.org/blog/double-and-dynamic-understanding-the-changing-perspectives-on-materiality/> [https://perma.cc/JN8M-GNAH].

¹³⁹ Stavros Gadinis & Amelia Miazad, *A Test of Stakeholder Governance*, 47 J. CORP. L. 47, 56 (2021).

making during the COVID-19 pandemic found that companies relied on stakeholders to derive information concerning social issues that fell outside the scope of ordinary monitoring systems. While Gadinis and Miazad convincingly advance the value of stakeholders as a source of risk-management, their claim that this systematized stakeholder governance creates mechanisms of accountability between managers and stakeholders is unsubstantiated. Under controlling doctrine and established governance procedures, shareholders remain managers' sole principals and the only stakeholders wielding levers of accountability over them. Stakeholders (shareholders included) may be more accurately characterized as a source of information, while shareholders alone hold protected powers to keep managerial rent-seeking at bay.

From this perspective, procedures that are typically considered instruments of "shareholder democracy," such as shareholder proposals, might instead be understood and leveraged as a channel of information for managers to interpret what is "material" to corporate purpose.¹⁴⁰ Shareholder proposals¹⁴¹ provide information concerning shareholder expectations which might signal matters of emerging materiality.¹⁴² Instead of liberalizing Rule 14a-8's "ordinary business

¹⁴⁰ The current version of SEC Rule 14a-8 allows shareholders meeting certain requirements to include concise proposals on a variety of issues in a company's proxy statement. Shareholders then vote on proxy proposals at a company's annual meeting. 17 C.F.R. § 240.14a-8. Various interpretations of Rule 14a-8 have limited or expanded who may submit a proposal and what subjects may be included. Eligibility to submit a proposal is based on a minimum equity stake and holding duration. 17 C.F.R. § 240.14a-8(b).

¹⁴¹ See, e.g., Sanford Lewis, *Analysis and Recommendations on Shareholder Proposal Decision-Making under the SEC No-Action Process*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Jul. 26, 2018), <https://corpgov.law.harvard.edu/2018/07/26/analysis-and-recommendations-on-shareholder-proposal-decision-making-under-the-sec-no-action-process/> [<https://perma.cc/NCQ4-99NE>].

¹⁴² See, e.g., "Just Vote No" Campaigns in Uncontested Director Elections – Renewed Vitality for the 2010 Proxy Season, WILLKIE FARR & GALLAGHER LLP, https://www.willkie.com/-/media/files/publications/2009/09/just-vote-no-campaigns-in-uncontested-director-e_/files/just-vote-no-campaignspdf/fileattachment/just-vote-no-campaigns.pdf [<https://perma.cc/XT84-G45Y>] (last visited Nov. 3, 2023).

exclusion,” as the SEC recently did in SLB 14L,¹⁴³ the exclusion should be preserved as an important lever in the balance of power between shareholders and managers¹⁴⁴ by keeping ordinary business decisions in the hands of managers and the board of directors, while allowing shareholders to provide high-level strategic direction while avoiding micromanagement.¹⁴⁵

The Rule’s previous ordinary business exclusion prevented shareholders from submitting proposals pertaining to a company’s “ordinary business” and included a nexus requirement that considered the significance of a social policy issue to a specific company.¹⁴⁶ In place of the nexus requirement, SLB 14L stipulated that SEC staff would instead focus on “the social policy significance of the issue that is the subject of the shareholder proposal.”¹⁴⁷ Current SEC interpretation recognizes “that proposals seeking detail or seeking to promote timeframes or methods do not per se constitute micromanagement” and instead focuses on “the level of granularity sought in the proposal and whether and to what extent it inappropriately limits discretion of the board or management.”¹⁴⁸ The

¹⁴³ SEC Legal Bulletin, *supra* note 66.

¹⁴⁴ See, e.g., Stephen M. Bainbridge, *Revitalizing SEC Rule 14a-8’s Ordinary Business Exclusion: Preventing Shareholder Micromanagement by Proposal*, 85 *FORDHAM L. REV.* 705, 718–19 (2016).

¹⁴⁵ *Trinity Wall St. v. Wal-Mart Stores* set out a two-step analysis for determining whether managers can exclude a shareholder proposal from a proxy statement. First, a court considers whether a proposal “deals with a matter relating to the company’s ordinary business operations.” *Trinity Wall St. v. Wal-Mart Stores, Inc.*, 792 F.3d 323, 341 (3d Cir. 2015) (quotation omitted). If yes, the Court must determine whether the proposal “transcends the day-to-day business matters of the company and raises policy issues so significant that it would be appropriate for a shareholder vote.” *Id.* at 345 (quotation omitted).

¹⁴⁶ SLB 14L further dismissed the “economic relevance” exception that allowed companies to exclude proposals pertaining to operations accounting for less than five percent of a company’s total assets or earnings and gross sales. SEC Legal Bulletin, *supra* note 66.

¹⁴⁷ *Id.*

¹⁴⁸ *Id.* The SEC’s current approach to micromanagement is illustrated in its letter to ConocoPhillips denying a no-action relief for a proposal requesting greenhouse gas reduction targets for its operations and products.

liberalized standard has led to a spike in shareholder environmental and social proposals.¹⁴⁹ This development might be successful in furthering a shareholder democracy agenda but it does not serve ESG governance efficacy. The former micromanagement exclusion served an important purpose in forcing shareholders to maintain a sufficient level of abstraction in their strategic and value-based expression without stifling managers' discretion. For example, McDonald's shareholders might choose to promote the humane treatment of animals as a broad, strategic objective. However, they might also focus on a narrower issue like the conditions of group housing for pigs. Narrower still, they might focus on the use of gestation crates for pregnant sows. Because the guiding objective of these agendas is a humanitarian rather than strictly pecuniary one, the generality or specificity of the issue is not anchored by a profit motive. Instead, the objective of "animal welfare" is a subjective one, and shareholder proponents might conceive of it in different terms from managers, or from one another, requiring micromanagement to achieve their preferences. The ordinary business exclusion was an important lever in preventing such micromanagement.

Characterizing stakeholders (including shareholders) as an information source rather than as principals avoids the shareholder minority concerns of shareholder democracy and the agency concerns of stakeholder governance. Under a technocratic model, shareholders must justify their ESG objectives in terms of long-term value or otherwise go through by-law or charter amendment procedures and allow for a buyout option for minorities who do not share the same non-pecuniary objectives.

The proposal did not impose a specific method of reduction and SEC staff concluded that it was not excludable under Rule 14a-8(i)(7). ConocoPhillips, SEC Staff No-Action Letter (Mar. 19, 2021), <https://www.sec.gov/divisions/corpfin/cf-noaction/14a-8/2021/followconocophilips031921-14a8.pdf> [on file with the Columbia Business Law Review].

¹⁴⁹ Suzanne McGee, *Shareholders Push an Array of ESG Proposals*, WALL ST. J. (Apr. 28, 2022), <https://www.wsj.com/articles/shareholders-push-array-of-esg-proposals-11651004156> [on file with the Columbia Business Law Review].

C. Corporate Technocracy in Practice

In this section I elaborate the payout of adopting a technocratic approach to ESG governance through the examples of three popular ESG objectives: climate risk, corporate political speech, and DEI.

1. Climate Risk

In the absence of political will and regulatory intervention responding to the urgency of the global climate change crisis, corporate leaders have taken private initiative to pursue climate risk management,¹⁵⁰ greenhouse gas emissions disclosures,¹⁵¹ and net zero commitments.¹⁵² The case for climate change materiality has been well-established by the work of organizations like the Task Force on Climate-Related

¹⁵⁰ See, e.g., Mathew Nelson, *Global Climate Risk Disclosure Barometer*, EY (Jun. 2021), https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/assurance/ey-if-the-climate-disclosures-are-improving-why-isnt-decarbonization-accerlerating.pdf [<https://perma.cc/VK6N-RFAE>] (“The US has seen a surge in companies issuing their first climate risk disclosure and TCFD reporting in the wake of the BlackRock and State Street CEO letters urging portfolio companies to report on climate risk. Investor and stakeholder pressure to manage and disclose material environmental, social and governance (ESG) and climate risks and opportunities has spread beyond the most carbon-intensive sectors, leading to advances in the quality of reporting in sectors such as agriculture, food and forest products, manufacturing, retail, health and consumer goods, and telecommunications and technology.”).

¹⁵¹ See, e.g., Lynn M. LoPucki, *Corporate Greenhouse Gas Disclosures*, 56 U.C. DAVIS L. REV. 405, 435 (2022) (providing empirical analysis of 2020 greenhouse gas disclosures from S&P 500 companies, observing an 81% reporting rate for Scope 1 and Scope 2 emissions).

¹⁵² See, e.g., *The Corporate Net-Zero Standard*, SCIENCE BASED TARGETS, <https://sciencebasedtargets.org/net-zero> [<https://perma.cc/YK8A-G395>] (last visited Nov. 3, 2023); but see Peter Eavis & Clifford Krauss, *What’s Really Behind Corporate Promises on Climate Change?*, N.Y. TIMES (Feb. 22, 2021), <https://www.nytimes.com/2021/02/22/business/energy-environment/corporations-climate-change.html> [on file with the Columbia Business Law Review] (noting the discrepancy between commitments and substantive practice).

Financial Disclosures (TCFD),¹⁵³ the Integrated Reporting and Connectivity Council,¹⁵⁴ and the Partnership for Carbon Accounting Financials (PCAF).¹⁵⁵ Climate materiality is interpreted based on industry sector, as elaborated by the Sustainability Accounting Standards Board (SASB), for example.¹⁵⁶ However, the boundaries of climate change materiality remain contested. Today, scope 1 emissions, which refer to a firm's direct greenhouse gas emissions from sources that it owns, are readily measurable and largely uncontested as a direct corporate impact.¹⁵⁷ Scope 2 emissions, which refer to indirect emissions associated with an organization's energy use, are also readily measurable and widely accepted.¹⁵⁸ Both scope 1 and scope 2 emissions are included in carbon neutral commitments, for example, and in carbon footprint metrics used by the MSCI index.¹⁵⁹ The materiality of scope 3

¹⁵³ The TCFD was created by the Financial Stability Board, an international body monitoring and making recommendations about the global financial system, in December 2015, to "improve and increase reporting of climate-related financial information." See TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES, <https://www.fsb-tcfid.org/> [<https://perma.cc/S4FM-T2MN>] (last visited Nov. 3, 2023).

¹⁵⁴ Council, IFRS FOUND., <https://integratedreporting.ifrs.org/the-iirc-2/council/> [<https://perma.cc/YED4-MSSQ>] (last visited Feb. 28, 2024).

¹⁵⁵ PCAF, <https://carbonaccountingfinancials.com/> [<https://perma.cc/5W9H-4MQV>] (last visited Feb. 28, 2024). Citing such efforts, the SEC proposed rule-making that would standardize climate risk disclosure. Press Release, Sec. and Exch. Comm'n, SEC Proposes Rules to Enhance and Standardize Climate-Related Disclosures for Investors (Mar. 21, 2022), <https://www.sec.gov/news/press-release/2022-46> [<https://perma.cc/K6EU-JCYD>].

¹⁵⁶ SASB, CLIMATE RISK TECHNICAL BULLETIN 6 (Aug. 2022), <https://sasb.org/wp-content/uploads/2023/11/SASB-Climate-Risk-Technical-Bulletin-2023-0823.pdf> [<https://perma.cc/FR4Z-3NF6>].

¹⁵⁷ *Scope 1 and Scope 2 Inventory Guidance*, U.S. ENV'T PROT. AGENCY (Aug. 21, 2023), <https://www.epa.gov/climateleadership/scope-1-and-scope-2-inventory-guidance> [<https://perma.cc/9SSX-M928>].

¹⁵⁸ *Id.*

¹⁵⁹ MSCI, MSCI CARBON FOOTPRINT INDEX RATIOS METHODOLOGY 3 (Jan. 2018), <https://www.msci.com/documents/1296102/6174917/MSCI+Carbon+Footprint+Index+Ratio+Methodology.pdf/6b10f849-da51-4db6-8892-e8d46721e991> [<https://perma.cc/MFX2-RRX9>] ("Based on both reported and estimated

emissions,¹⁶⁰ referring to emissions resulting from activities not directly owned or controlled by the reporting organization, however, remains widely disputed.¹⁶¹ Scope 3 materiality depends on an assumption about the boundaries of the corporate enterprise, a fact that is itself subject to considerable contestation.

From a technocratic governance perspective, managers have protected discretion to make decisions concerning scope 1 and scope 2 emissions. An associated ESG board matrix promoting relevant technocratic expertise might include attributes reflecting climate competency,¹⁶² particularly in high emissions sectors like fossil fuels, energy, construction, cement, and animal farming. Managers are empowered to operationalize climate change as an ESG objective by mitigating a company's climate impacts with the discretion to determine strategy, operational decisions, and timeline for implementation.

Scope 3 emissions, however, present an opportunity for input from shareholders and stakeholders to inform materiality. Shareholder proposals might, for example, request reporting

Scope 1 & 2 carbon emissions, MSCI measures the carbon responsibility, efficiency, and exposure attributed to the MSCI Indexes.”).

¹⁶⁰ *Scope 3 Inventory Guidance*, U.S. ENV'T PROT. AGENCY (May 12, 2022), <https://www.epa.gov/climateleadership/scope-3-inventory-guidance> [<https://perma.cc/NJC4-NDUU>] (“Scope 3 emissions are the result of activities from assets not owned or controlled by the reporting organization, but that the organization indirectly impacts in its value chain. Scope 3 emissions include all sources not within an organization’s scope 1 and 2 boundary.”).

¹⁶¹ *See, e.g.*, Robert S. Kaplanand & Karthik Ramanna, *Accounting for Climate Change*, HARV. BUS. REV. 120, 123 (“Scope 3 emissions are the fatal flaw in GHG reporting. The [GHG Protocol]’s creators included them to encourage companies to exert influence over emissions that they don’t control directly. For example, they could buy from or sell to companies with lower Scope 1 emissions, and collaborate with their suppliers and customers to reduce GHG emissions along their value chains. But the difficulty of tracking emissions from multiple suppliers and customers across multitier value chains makes it virtually impossible for a company to reliably estimate its Scope 3 numbers.”).

¹⁶² Borduas et al., *supra* note 133.

on emissions resulting from a company's supply chain.¹⁶³ While shareholder participation might serve an advisory function that informs management of material climate risks, proposals or proxy campaigns concerning specific strategies for how a company should achieve scope 3 targets would constitute micromanagement¹⁶⁴ making them excludable under former 14-8 guidelines and objectionable from a shareholder minority standpoint. Outside of corporate governance, organizations like SASB might issue guidelines standardizing scope 3 as it pertains to particular industry sectors. Viewed through a technocratic lens, Engine No. 1's much maligned decision to vote against climate-related resolutions at Citi, Bank of America, and Wells Fargo in 2022 can be reconciled with its climate-focused ESG orientation. The resolutions in question called on the banks to adopt policies by the end of 2022 ensuring that their financing does not contribute to new fossil fuel supplies in keeping with International Agency Association's recommendations.¹⁶⁵ Engine No. 1's managing director explained that the proposals had too much micromanagement and "as written they did not provide adequate flexibility for banks to finance the fossil fuel and energy transition."¹⁶⁶

¹⁶³ Karin Rives, *Climate Resolutions Top 'Unprecedented' Number of Shareholder Proposals in 2022*, S&P GLOBAL (Apr. 4, 2022), <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/climate-resolutions-top-unprecedented-number-of-shareholder-proposals-in-2022-69641049> [<https://perma.cc/L8SD-AGMN>].

¹⁶⁴ A recent controversy concerning activist fund Engine No. 1 demonstrates diverging understandings of the degree of discretion that should be ceded to managerial agents, even among shareholders who, apparently, align on substantive ESG objectives. See McDonnell, *supra* note 82.

¹⁶⁵ See *supra* notes 83-85 and accompanying text.

¹⁶⁶ McDonnell, *supra* note 82. BlackRock adopted a similar position: a recent memo observed that shareholder proposals concerning climate disclosures have been too "constraining" and "prescriptive" in the most recent proxy season. See BLACKROCK, *supra* note 85 ("Having supported 47% of environmental and social shareholder proposals in 2021, BIS notes that many of the climate-related shareholder proposals coming to a vote in 2022 are more prescriptive or constraining on companies and may not promote long-term shareholder value.").

2. Political Speech

Since the Supreme Court issued its controversial *Citizens United* opinion in 2010,¹⁶⁷ political speech has been a leading subject of shareholder proposals.¹⁶⁸ Partisan political spending garnered further scrutiny in the wake of the 2021 capitol riots,¹⁶⁹ when contradictions between corporate political contributions and professed values became a subject of media and public critique.¹⁷⁰ Shareholders reflected this concern with corporate spending in the 2021 proxy season, which featured

¹⁶⁷ *Citizens United v. Fed. Election Comm'n*, 558 U.S. 310 (2010).

¹⁶⁸ See, e.g., Ki P. Hong, Melissa L. Miles & Karina Bakhshi-Azar, *Companies Face New Pressure from Shareholders and Regulators to Disclose Political Policies and Contributions*, SKADDEN (Jan. 19, 2022), <https://www.skadden.com/insights/publications/2022/01/2022-insights/regulation-enforcement-and-investigations/companies-face-new-pressure-from-shareholders> [<https://perma.cc/7RMH-AJYJ>] (“[D]uring the 2021 proxy season, shareholder proposals requesting disclosure of corporate political spending passed at the highest rate ever recorded . . . [S]ome shareholders have been pushing for increased disclosure of corporate political spending for almost two decades In 2020, a record 20% of these political shareholder proposals were adopted, a number eclipsed in 2021 with a new high of 40%[.]”); Andrew Ramonas & Lydia Beyoud, *Activist Shareholders Score Wins on Election Spending After Riot*, BLOOMBERG L. (July 14, 2021), <https://news.bloomberglaw.com/securities-law/activist-shareholders-score-wins-on-election-spending-after-riot> [<https://perma.cc/W79T-NR59>].

¹⁶⁹ See, e.g., Dorothy S. Lund & Leo E. Strine, Jr., *Corporate Political Spending Is Bad Business*, HARV. BUS. REV. (Jan.–Feb. 2022), <https://hbr.org/2022/01/corporate-political-spending-is-bad-business> [<https://perma.cc/8WXN-W88X>].

¹⁷⁰ See, e.g., Ephrat Livni, *On Voting Rights, It Can Cost Companies to Take Both Sides*, N.Y. TIMES (June 5, 2021), <https://www.nytimes.com/2021/06/05/business/dealbook/voting-rights-companies.html> [<https://perma.cc/2E63-XRJZ>]; Maxine Joselow & Vanessa Montalbano, *Top Companies Are Undermining Their Climate Pledges with Political Donations, Report Says*, WASH. POST (Feb. 23, 2022), <https://www.washingtonpost.com/politics/2022/02/23/top-companies-are-undermining-their-climate-pledges-with-political-donations-report-says/> [<https://perma.cc/MD3B-X49D>]; Brody Mullins & Ann Zimmerman, *Target Discovers Downside to Political Contributions*, WALL ST. J. (Aug. 7, 2010), <https://www.wsj.com/articles/SB10001424052748703988304575413650676561696> [<https://perma.cc/RE9M-ZN4R>].

record voting in support of corporate political disclosure.¹⁷¹ As a governance matter, political speech presents some unique challenges due to its intertwined expressive and instrumental functions.¹⁷² Recognizing this, some governance reform agendas have proposed banning corporate political speech outright¹⁷³ or relying on the regulatory functions of disclosure.¹⁷⁴

Addressing corporate political speech through a technocratic paradigm provides some guidance for distinguishing between different types of speech activities and differentiating those that are administrable from an agency perspective from those that engender unmanageable agency costs. For

¹⁷¹ See, e.g., Sue Reisinger, *Corporate Political Disclosure Votes Hit Record High in 2021*, LAW360 (Dec. 20, 2021), <https://www.law360.com/pulse/articles/1450343/corporate-political-disclosure-votes-hit-record-high-in-2021> [<https://perma.cc/A7PJ-UNPS>].

¹⁷² Lucian Bebchuk and Robert Jackson argue that political speech decisions are “substantially different from” ordinary business decisions and that they should be subject to different rules that grant control to shareholders instead of managers. Their argument offers a blunt solution to the complexities of overlapping instrumental and expressive aspects of corporate political activity and seeks to expand shareholder control as the remedy to potential managerial rent-seeking. They propose rules to “(i) provide shareholders with a role in determining the amount and targets of corporate political spending; (ii) require that independent directors oversee corporate political speech decisions; (iii) allow shareholders to opt out of . . . each of these first two rules; and (iv) mandate detailed and robust disclosure to shareholders of the amounts and beneficiaries of a corporation’s political spending, whether made directly by the company or indirectly through intermediaries.” See Bebchuk & Jackson, Jr., *supra* note 34, at 84.

¹⁷³ See, e.g., Lund and Strine, Jr., *supra* note 169. This solution has limited political traction. The SEC currently faces a ban on issuing corporate political spending disclosure rules. The fiscal 2022 appropriations deal announced on March 9, 2022 maintains the ban. See Bill Flook, *Budget Deal Preserves Ban on SEC Political Spending Disclosure Rule*, THOMSON REUTERS (Mar. 10, 2022), <https://tax.thomsonreuters.com/news/budget-deal-preserves-ban-on-sec-political-spending-disclosure-rule/> [<https://perma.cc/AP24-49JM>].

¹⁷⁴ Though legal obstacles currently prevent the SEC from issuing rules concerning political spending, the efficacy of a disclosure regime may be limited for other reasons. If we accept a shareholder primacy orientation, then disclosure undermines the instrumental function of expressive activities by putting on display corporate hypocrisy and extinguishing its value in generating popular or employee goodwill.

example, political lobbying activities are instrumentally beneficial to corporate Purpose if they produce policies favorable to a specific company or industry. Publicly directed political statements and activities might also be instrumental to corporate Purpose if they enhance a company's social or political license to operate. Purely instrumental political speech falls squarely within managers' mandate under a conventional shareholder primacy paradigm. Where there is an overriding shareholder interest and a utilitarian strategy, corporate political speech is defensible as rational, ordinary business decision-making. For instrumental political speech, oversight requires disclosure, and substantiation through a bureaucratic and institutionalized procedural pathway. Managerial rent-seeking can be disciplined through levers available to shareholders through *Caremark*, Section-10B, and books and records claims. However, where political speech is purely expressive and corporate executives claim to advance their own visions of the common good, apart from corporate value, then the interests of shareholder principals have been effectively substituted with the public welfare. These types of decisions create the structurally unaccountable managerial discretion that critics point to.

3. DEI

Diversity has been an emerging ESG objective for over 30 years.¹⁷⁵ More recently, a broad set of actors and activities

¹⁷⁵ Shareholders have promoted a corporate diversity agenda and lobbied for integrating it into decision-making since the early 1990s, when a national focus on the gender gap in corporate leadership inspired the "Glass Ceiling Commission." Shareholder proposals on gender diversity followed the 1991 bipartisan "Glass Ceiling Commission" appointed by President H.W. Bush to identify "barriers based on attitudinal or organizational bias that prevent qualified individuals from advancing upward in their organization into management-level positions." U.S. DEP'T OF LAB., THE GLASS CEILING INITIATIVE. A REPORT. (1991), <https://files.eric.ed.gov/fulltext/ED340653.pdf> [<https://perma.cc/TA7B-779W>]. Shortly after the Commission issued its report, a coalition of investors began filing shareholder proposals requesting that companies publicly disclose federal diversity data submitted annually to the Equal Employment Opportunity Commission and the Department of Labor. For example,

have brought diversity to the forefront of corporate ESG priorities, with advocates citing material implications for corporate performance.¹⁷⁶ Financial services firms and consultants have made the case for a positive relationship between

Trillium Asset Management filed a proposal with Home Depot for three years in a row beginning in 1998 and garnered more than 10% support each year. Susan Baker & Randy Rice, *Two Decades Later, Trillium Still Engaging Companies on Diversity*, TRILLIUM (Jun. 16, 2014), <https://archive.trilliuminvest.com/2014/06/16/two-decades-later-trillium-still-engaging-companies-on-diversity/> [<https://perma.cc/KS5R-XJ4T>]. Beginning in 2005, investors were reaching agreements on EEO-1 disclosure at American Express, IBM, Merck, Hewlett Packard, Walmart, and Intel.

¹⁷⁶ In January 2020 Goldman Sachs announced that it would stop underwriting IPOs for U.S. and European companies that don't have diverse boards that include representation from traditionally underrepresented groups. Jena McGregor, *Goldman Sachs CEO Says It Won't Take a Company Public Without Diversity on Its Board*, WASH. POST (Jan. 23, 2020), <https://www.washingtonpost.com/business/2020/01/23/goldman-sachs-ceo-says-it-wont-take-companies-public-without-diverse-board-member/> [<https://perma.cc/GN9Y-PB32>]. At the start of the 2021 proxy season, the Big Three institutional investors updated their guidance and expectations on diversity and inclusion for portfolio companies. In his 2021 letter to investors, BlackRock's Larry Fink asked CEOs to disclose their long-term plans to improve diversity, equity, and inclusion. Larry Fink, *Larry Fink's 2021 Letter to CEOs*, BLACKROCK, <https://www.blackrock.com/us/individual/2021-larry-fink-ceo-letter> [<https://perma.cc/AE2S-SKZB>] (last visited Dec. 22, 2023) ("As you issue sustainability reports, we ask that your disclosures on talent strategy fully reflect your long-term plans to improve diversity, equity, and inclusion, as appropriate by region."). State Street Global Advisors similarly said it expected all companies in its portfolio to publicly "articulate the role diversity plays in the firm's broader human capital management practices and long-term strategy." Cyrus Taraporevala, *Guidance on Enhancing Racial & Ethnic Diversity Disclosures*, STATE STREET GLOBAL ADVISORS (Jan. 11, 2021), <https://www.ssga.com/library-content/pdfs/asset-stewardship/combined-proxy-guidance-letters.pdf> [<https://perma.cc/9VD6-9C92>]. In its Investment Stewardship Insights, Vanguard noted that "[r]isks to shareholder value associated with diversity, equity, and inclusion (DEI) remain a top engagement priority" and that the growing focus on racial and ethnic discrimination has increased scrutiny of companies' DEI risks and opportunities. *Shareholder Proposals: Diversity, Equity, and Inclusion*, VANGUARD INV. STEWARDSHIP INSIGHTS (May 2021), https://corporate.vanguard.com/content/dam/corp/advocate/investment-stewardship/pdf/perspectives-and-commentary/INVDEIS_052021.pdf [<https://perma.cc/4BSB-HMTX>].

diversity and investment.¹⁷⁷ In 2020, SASB noted that it is continually monitoring “evidence related to the financial materiality of diversity and inclusion across industries.”¹⁷⁸ In the 2021 proxy season, MSCI began offering metrics on Racial and Ethnic Diversity for US companies.¹⁷⁹ Proxy advisory services ISS and Glass Lewis¹⁸⁰ developed voting guidelines tied to diversity.¹⁸¹ These activities have brought the issue of diversity into the fold of financial materiality justifying managerial discretion extending to this objective.

The diversity example reveals an important limitation to the administration of ESG through technocracy. Distilling such an abstract and complex social objective into measurable criteria inevitably means that form can supersede substance. This is a major critique of board diversity quotas, for example. Different diversity metrics approximate various objectives,

¹⁷⁷ Chris Brummer & Leo E. Strine, Jr., *Duty and Diversity*, 75 VAND. L. REV. 1, 28-33 (2022) (indicating research shows that diversity and inclusion increases a company’s chances of financial success).

¹⁷⁸ Kelli Okuji Wilson, *Exploring Diversity & Inclusion in the SASB Standards*, SASB (Sept. 28, 2020), <https://sasb.org/blog/exploring-diversity-inclusion-in-the-sasb-standards/> [<https://perma.cc/GL3K-66CL>].

¹⁷⁹ MSCI, 2022 ANNUAL MEETING OF SHAREHOLDERS AND PROXY STATEMENT 5 (2022), <https://ir.msci.com/static-files/56e6fc9f-c575-4bba-aa86-7c39572e2d30> [<https://perma.cc/HEF2-CW3X>].

¹⁸⁰ James Bee, Paul Davies, Michael Green & Andra Troy, *ISS, Glass Lewis Focus on ESG in 2022 Benchmark Proxy Voting Policies*, JD SUPRA (Jan. 12, 2022), <https://www.jdsupra.com/legalnews/iss-glass-lewis-focus-on-esg-in-2022-8502187/> [<https://perma.cc/98GQ-63UW>].

¹⁸¹ For 2021, ISS voting policy indicated that it would flag in its reports company boards with no apparent racial or ethnic diversity and that beginning in 2022 it would recommend against nominating committee chairs where a company’s board had no apparent racial or ethnic diversity. *Id.* Similarly, Glass Lewis indicated that beginning in 2021 reports for companies in the S&P 500 index would include an assessment of its proxy disclosure relating to board diversity. Later, Glass Lewis updated its policy to note that beginning in 2022, it would possibly recommend “against” or “withhold” votes for the chair of the nominating and governance committee for S&P 500 companies if a company failed to provide disclosure in four categories pertaining to board diversity, and that beginning in 2023 it would generally oppose election of the chair of the nominating and governance committee at those companies if they have not provided any aggregate or individual disclosure about a Board’s racial/ethnic demographics. *Id.*

including measuring demographics across organization levels, retention across employee groups, employee turnover, adverse impact of discriminatory practices, candidate demographics, or employee advancement and promotion rates.¹⁸²

This example highlights that technocracy is limited in its potential as a mechanism for radical social change, but this shortcoming also tempers the possibility of abuse by managers or shareholders. By underscoring the function of materiality as a stabilizing concept and as a limit to managerial discretion, technocracy shifts political attention to multi-nodal, decentralized activity by social movements, consumer campaigns, third-party organizations, politicians, shareholder groups, empirical scholars, and others to build the case for materiality and to challenge and revise the efficacy of selected metrics in capturing an intended outcome. Technocracy forecloses the possibility of more urgent political or social action by corporate leadership, but the opportunity remains for swift political intervention to implement social objectives that do not conform to a financial materiality rationale through directed shareholder activity in the form of charter or bylaw amendments.

V. CONCLUSION

ESG remains a highly politicized notion that inspires hundreds of legislative proposals advancing and obstructing its impact.¹⁸³ While some anti-ESG advocacy is undoubtedly

¹⁸² Volker Lainer, *DEI Measurement of ESG is Beginning to Emerge*, GOLDENSOURCE BLOG (July 15, 2022), <https://www.thegolden-source.com/dei-measurement-esg-beginning-to-emerge/> [<https://perma.cc/5RRB-GR3F>].

¹⁸³ See, e.g., Andrew Ramonas & Clara Hudson, *ESG Top of Mind as New State Attorneys General Flex Powers*, BLOOMBERG L. (Feb. 13, 2023), <https://news.bloomberglaw.com/esg/esg-top-of-mind-as-new-state-attorneys-general-flex-powers> [<https://perma.cc/RP38-MEAA>]; Saijel Kishan & Danielle Moran, *Republicans Ramp Up Anti-ESG Campaign for 2023*, BLOOMBERG (Dec. 29, 2022) <https://www.bloomberg.com/news/articles/2022-12-29/republicans-prepare-to-ramp-up-their-anti-esg-campaign-in-2023> [<https://perma.cc/Z4Z4-C7LB>]; Niquette & Crowley, *supra* note 1.

opportunist,¹⁸⁴ more substantive concern with the agency problems that riddle ESG governance remains unaddressed. Whether it empowers managers or increases shareholder power, ESG governance confronts unresolved principal-agent challenges. For those who seek to redeem the moderate, incremental possibilities of an ESG agenda while avoiding the pitfalls of both shareholder democracy and managerialism, a corporate technocracy that emphasizes institutional capacity, materiality, procedural accountability, and shareholder protections offers a way through the political quagmire.

APPENDIX 1 - A TAXONOMY OF ESG

| | | Corporate Ends | |
|------------------|---------------------|---------------------------------|---------------------------|
| | | Profit | Stakeholder Interest |
| Governance Means | Shareholder Control | X | Shareholder Pluralism |
| | Managerial Control | Enlightened Shareholder Primacy | Managerial Stakeholderism |
| | Stakeholder Control | X | Codetermination |
| | | | |

¹⁸⁴ *You Want Us to Ignore What? A Brief Analysis of Anti-ESG Political Rhetoric*, THE S'HOLDER COMMONS (Oct. 2022), <https://theshareholdercommons.com/you-want-us-to-ignore-what-a-brief-analysis-of-anti-esg-political-rhetoric/> [https://perma.cc/5V26-FS9R].

