"Enlightened Shareholder Value": Corporate Governance Beyond the Shareholder-Stakeholder Divide

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**"ENLIGHTENED SHAREHOLDER VALUE": CORPORATE GOVERNANCE BEYOND THE SHAREHOLDER-STAKEHOLDER DIVIDE**

**Abstract:**

The global financial crisis has led to calls for greater corporate accountability and heightened controls over public corporations. As a result, the past year has seen a marked increase in regulatory initiatives that give shareholders a greater voice in corporate affairs. While debate continues to rage in the academy and beyond over the promise and pitfalls of shareholder empowerment, an important undercurrent in the controversy is the potential impact of "shareholder democracy" on corporate stakeholders.

This Article urges a vision of the corporation and its purpose that transcends the shareholder-stakeholder divide. Under this "enlightened shareholder value" approach, which has been introduced statutorily in the United Kingdom, attention to corporate stakeholders, including the environment, employees, and local communities, is seen as critical to generating long-term shareholder wealth.

This Article observes that a similar paradigm is now being advanced in the U.S. by leading institutional investors who also identify stakeholder interests as key to long-term firm financial performance and effective risk management. It moves beyond prior literature by articulating a statement of the corporate purpose that is consistent with an investor-driven enlightened shareholder value approach and presents normative arguments in its favor. The Article then considers how enlightened shareholder value intersects with existing corporate governance rules in the U.S. context and the extent to which it in fact represents a departure from the standard shareholder wealth maximization norm. In so doing, it offers a response to some of the concerns surrounding corporate stakeholders that have been raised by skeptics of greater shareholder voice.

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I. INTRODUCTION

Over the past several years, a rise in shareholder activism has sparked wide-ranging academic debate about the optimal role of shareholders in U.S. corporate governance and the benefits (or perils) of shareholder democracy.1 These debates have become of greater relevance to policymakers and the public, as the global financial crisis has led to calls for greater corporate accountability and prompted renewed interest in the power of shareholders to police corporate management. Although debate continues to rage over whether shareholders can and will restrain corporate mismanagement, the past year has seen a marked increase in regulatory initiatives that give shareholders a greater voice in corporate affairs.2

1 See infra notes 27-47 and accompanying text.

2 See infra notes 23-37 and accompanying text. Shareholder activism has been defined broadly as "the use of power by an investor either to influence the [behavior and impact] of a given portfolio firm [or
An important undercurrent in the academic and popular controversy is the potential impact of shareholder democracy on corporate stakeholders, such as employees, creditors, the environment, and local communities. Director primacy proponents, who argue that control of the corporation is the proper purview of the board, not shareholders, note that corporate directors and officers already enjoy broad discretion under existing law to consider stakeholder interests. Shareholder empowerment might then disadvantage stakeholders by compelling management to focus solely on shareholder wealth maximization. Powerful shareholders might also pressure management to transfer value from stakeholders to shareholders.

Opposite concerns are voiced as strongly that powerful shareholders will use their power to advance special interests, realize short-term gains, or promote narrow causes to the detriment of the firm, even though some of the "causes" and "interests" so advanced are in fact the causes and interests of employees and other firm constituencies. In short, the problem with stakeholders is both that they might get too little attention and that they might get too much.

This Article engages with this aspect of the shareholder democracy debate by advocating an "enlightened shareholder value" vision of the corporate purpose that transcends the shareholder-stakeholder divide. Under this conception, attention to traditional "stakeholder" interests, such as the effect of corporate operations on the environment, employees, or local communities, is seen as a means of generating long-term shareholder wealth and improving portfolio- and firm-level risk assessment. "Enlightened shareholder value" thus emphasizes the benefits to shareholders that can result from focusing corporate management on areas of shared shareholder and stakeholder concern, while recognizing the very real challenges posed by the diversity of shareholder and stakeholder interests. At the same time, by asserting that shareholder wealth should not be achieved through disregard for the impact of corporate decision-making on stakeholders, enlightened shareholder value in fact parts course from the standard shareholder wealth maximization conception of the corporate purpose.

3 In this Article, I use the term "stakeholder" to refer solely to nonshareholders who bear risk of harm or loss as a result of the firm's activities, following Max Clarkson's risk-based stakeholder model. See STUART COOPER, CORPORATE SOCIAL PERFORMANCE: A STAKEHOLDER APPROACH 39 (2004) (describing Clarkson's model) (citations omitted). As used here then, "stakeholder" is identical in scope to the alternative, but more cumbersome term, "nonshareholder constituencies" preferred by Stephen Bainbridge. See e.g. Stephen Bainbridge, Director Primacy: The Means and Ends of Corporate Governance, 97 NW. U. L. REV. 547 (2003). Other alternatives might include all actors who "affect or are affected by" the corporation, but such definitions are too broad to be meaningful. See COOPER, id. at 38-41 (introducing various alternatives).

4 See infra notes 44-46 and accompanying text.

5 See infra note 47 and accompanying text.

6 See infra notes 39-42 and accompanying text.
Enlightened shareholder value is not a novel concept, but has in fact already been introduced in the United Kingdom statutorily under the U.K. Company Act of 2006. Theoretical precedent for the approach can be found in the narrower "enlightened stakeholder value" theory advanced by economist Michael Jensen. It also has parallels in the United Nations' Principles for Responsible Investment (PRI), which urge analysis of stakeholder interests as part of firm- and portfolio-level risk management. Although there are good reasons to doubt that regulatory reform in the U.S. will follow the path of the United Kingdom, this Article points to indications that an “enlightened shareholder value” model is emerging in the United States, in part at the behest of major institutional investors.

A substantial literature now spanning two decades has critically examined the role of institutional investors in promoting good corporate governance and supporting “responsible” business practices. Much of this literature concluded that institutional investor activism was unlikely to fulfill its hoped-for potential as a catalyst of corporate change, and cause for skepticism remains today. But the market and regulatory context has changed substantially since many of these studies of institutional investor activism were first undertaken. In particular, the rise of shareholder democracy has shifted the balance of corporate power toward shareholders, making their priorities more important to corporate boards. At the same time, movements across the economy favoring long-term investment strategies, "sustainable" business practices, and broader conceptions of corporate accountability and risk management have created an environment in which shareholder and stakeholder interests are more likely to align.

Clear signs of a pro-stakeholder orientation among leading institutional investors can already be seen in initiatives to incorporate environmental, social, and governance (ESG) measures in firm and portfolio risk analysis, supported by investor-led efforts to encourage sustainability reporting and by trends in shareholder activism. To date, CalPERS and other prominent public and union pension funds are at the forefront of many of these trends, with less movement from mutual funds, which make up a slightly greater percentage of U.S. equity markets. Nonetheless, because of its potential to generate long-term economic value to shareholders, facilitate more effective firm and portfolio-level risk management, and improve the quality of information available to the markets, enlightened shareholder value, as defined in this Article, has appeal for mainstream investors and investment intermediaries that is already deepening its impact.

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8 See infra note 178.

9 See infra Part IV(B).

10 See infra notes 15-16 and accompanying text.

11 See infra Section IV(B). On the scale of institutional investor holdings, see note 19.
Although a limited number of prior studies have explored the possibility of an investor-driven enlightened shareholder value model in the U.S. context, this Article offers a new look at the potential of enlightened shareholder value to motivate market-driven corporate reform in light of shifts in investor practices and regulatory measures that now amplify shareholder voice. It is also the first to consider the implications of enlightened shareholder value for dominant conceptions of the corporate purpose. Moving beyond prior literature, the Article squarely considers how enlightened shareholder value intersects with existing corporate governance rules in the United States and the extent to which the paradigm represents a challenge to the standard shareholder wealth maximization norm. It also advances normative arguments in favor of the approach.

Part II sets a foundation for this investigation by reviewing the literature on institutional investor activism and outlining the nature of the "stakeholder problem" within the shareholder empowerment debate. Part III considers the space for stakeholders under current corporate law rules. Part IV introduces the alternative perspective offered by an enlightened shareholder value (ESV) paradigm, its underlying rationales, and evidence of its growing influence among mainstream investors and financial intermediaries. Part V assesses the extent to which ESV fits within and also, paradoxically, challenges fundamental aspects of shareholder wealth maximization. In so doing, this Article responds to some of the concerns surrounding corporate stakeholders that have been raised by critics of greater shareholder voice.

II. INSTITUTIONAL INVESTOR ACTIVISM: PANDORA'S BOX?

In the Berle-Means corporation, the separation of ownership and control produces powerful corporate managers who are largely unrestrained by the dispersed and rationally apathetic shareholders on whose behalf they are obligated to act. For much of the past century, this classic model was a fairly accurate description of the American public corporation and one that has been credited for the economic successes of the United States and other shareholder-oriented jurisdictions.

By the early 1990s, however, it had become apparent that U.S. equity shareholdings were increasingly concentrated among large institutional investors, that is, public and private pension funds, mutual funds, insurance companies and banks. This sparked strong academic interest in the potential of these large investors to serve as quasi-regulators and true monitors of corporations and their boards. Much of this attention focused on the

12 See Williams & Conley, supra note 7; David Hess, Public Pensions and the Promise of Shareholder Activism for the Next Frontier of Corporate Governance: Sustainable Economic Development, 2 VA. L. & BUS. REV. 221 (2007).


15 See Douglas M. Branson, Corporate Governance "Reform" and the New Corporate Social Responsibility, 62 U. PITT. L. REV. 605, 630-35 (2001) (summarizing the literature and describing institutional investor activism as "the academic's panacea" for corporate governance reform).
role of public pension funds because of the long-term investment perspective of their fund beneficiaries and the belief that these funds had fewer conflicts of interest, as compared to other institutional investors. Early optimism ultimately gave way in the face of considerable evidence of institutional investor passivity, short-termism, complex and indeed, conflicting interests, and the limited impact of investor activism on corporate behavior.\(^{16}\)

However, one of the most striking developments impacting corporate America in recent years has been a dramatic shift in the balance of corporate power in the direction of shareholders, a shift which has reinvigorated interest in the questions surrounding institutional investor influence.\(^{17}\) Here, I trace the rise of shareholder democracy and identify the ways in which concerns over stakeholders continue to impact the shareholder empowerment debate.

A. INSTITUTIONAL INVESTOR POWER AND THE RISE OF SHAREHOLDER DEMOCRACY

Since the turn of the century, the concentration of U.S. equity shares held by institutional investors has accelerated to the point that their holdings now represent two-thirds of the value of all U.S. public equities.\(^{18}\) As of year-end, 2006, public and private pension funds controlled over 28 percent of the U.S. public equity market. Major mutual fund families, such as Fidelity and Vanguard, controlled another 27 percent.\(^{19}\) Although diversification requirements prevent most institutional investors from owning 10 percent or more of any single portfolio company and most hold fewer than 3 percent,\(^ {20}\) as of

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\(^{19}\) BRANCATO & RABIMO, id., at 22, tbl. 13. Public pension funds, such as CalPERS, which invest for the benefit of state and local public employees, accounted for 10 percent of the total equity market, nearly half of the pension fund aggregate figure. The 10 percent figure is, however, less than half of the aggregate equity holdings by mutual funds.

\(^{20}\) See BAUMAN, supra note 18, at 509 (discussing diversification restrictions).
2007, institutional investors together owned 76.9 percent of the largest 1000 companies. This concentration of ownership increases the likelihood that management will attend to shareholder concerns and lowers collective action barriers to active investment strategies, creating leverage that makes the benefits of activism more worth the costs to any one investor. In addition, regulatory changes in recent years have stimulated greater activism among institutional investors by reducing proxy solicitation and voting costs and lowering other obstacles to investor coordination, enabling more strategic investor influence of corporate decision-making.

As a result, pension funds, hedge funds, and even major mutual funds now engage in various forms of shareholder activism, often in coordination with one another, ranging from voting corporate proxies to informal negotiations with management, to shareholder proposals, proxy contests and shareholder litigation. Empirical studies, while not uniform in their findings, indicate that investors’ active monitoring can reduce agency costs and improve corporate financial performance.

Nonetheless, investors’ propensity for shareholder activism varies widely. For institutional investors, the fund size, degree of diversification, relative size of holdings in a given portfolio company, degree of investment in equity, investment time horizon, the

21 Brancato & Rabimov, supra note 18, at 27-28, tbs. 19, 21. Institutional ownership is also highly concentrated for many companies. For example, ten institutional investors account for roughly 56% of the equity ownership of WalMart and 18% of Exxon Mobil and Procter and Gamble. Id.


23 For example, in 1992, the SEC amended the definition of “proxy solicitation” to remove most shareholder communications made without a formal proxy solicitation from the scope of federal regulation, and in 2007, amended the proxy solicitation rules to authorize e-proxy solicitations, lowering cost barriers for activist investors. Release No. 34-31326 (Oct. 16, 1992), 52 Fed. Reg. 48276; Release No. 34-56135, (July 26, 2007) 72 Fed. Reg. 42222. See Anabtawi & Stout, id. at 1276, 1281 fn. 98 (describing the proxy solicitation changes and the e-proxy rules as among the most significant reforms that have increased shareholder power). Rules introduced by the SEC in 2002 require mutual funds to disclose how they vote corporate proxies were also intended to encourage mutual funds to exercise voting rights independent of management, although studies to date have not identified a significant impact on mutual fund activism. See David Yermack, Shareholder Voting and Corporate Governance, __ ANN. REV. OF FIN. [21-22] (forthcoming 2009) (reviewing empirical evidence). Further rules to improve proxy notice and access have been proposed. Release Nos. 33-9073; 34-60825 (Oct. 14, 2009).

24 See supra note 17.

investor’s commitment to non-financial performance, whether the fund is managed externally or internally, and the fund’s compensation structure all have an impact.\textsuperscript{26} Moreover, despite the strong shareholder-orientation of the American market and the market dominance of institutional investors, scholars on both sides of the shareholder democracy debate acknowledge that legal and practical limits have impeded the exercise of shareholder control, so that corporate boards have generally exercised nearly exclusive control over corporate affairs.\textsuperscript{27} These constraints have led to calls for deeper reforms that would expand shareholder voting rights and otherwise make corporate boards more directly accountable to shareholders.\textsuperscript{28}

Though academic and public debate about the wisdom of such proposals has not subsided,\textsuperscript{29} shareholders have already begun to make considerable headway on their own. Through shareholder proposals under Rule 14a-8 of the Securities Exchange Act of 1934\textsuperscript{30} and various forms of engagement with corporate management, shareholders are pushing increasingly for greater control over corporate boards.\textsuperscript{31} Proposals replacing plurality with majority voting for director elections, eliminating classified

\begin{itemize}
\item \textsuperscript{26}See \textit{Roderick Martin; Peter D. Casson & Tahir M. Nisar, Investor Engagement} 36-59 (2007); Lori Verstegen Ryan & Marguerite Schneider, \textit{The Antecedents of Institutional Investor Activism,} 27 ACAD. MGMT. REV. 554, 558 (2002); Choi & Fisch, \textit{supra} note 17, at 352 (identifying institutional investor size, in terms of total assets under management, as the factor most highly correlated with activism).

\item \textsuperscript{27}The primary disagreement between advocates and skeptics of shareholder power is whether this state of affairs is desirable or not. These limits include (i) state corporate law rules that limit shareholder voting rights to director elections, approval of charter and bylaw amendments, and veto of extraordinary corporate actions, (ii) limits on access to the corporate proxy, (iii) disincentives to formation of large blocks of stock, (iv) limits on shareholder coordination and communication, and (v) a lack of mechanisms for shareholders to exercise direct influence over either operational decisions or what Lucian Bebchuk has termed "rules of the game" decisions. See Lucian A. Bebchuk, \textit{The Case for Shareholder Access to the Ballot,} 59 BUS. L. 43 (Nov. 2003); Lucian A. Bebchuk, \textit{The Myth of the Shareholder Franchise,} 93 VA. L. REV. 675 (2007); Black, \textit{supra} note 22 (highlighting legal obstacles to shareholder activism). See also Bainbridge, \textit{Director Primacy, supra} note 3, at 569-72 (2003) (stating that "shareholder control rights are so weak they scarcely qualify as part of corporate governance."); Margaret M. Blair & Lynn A. Stout, \textit{A Team Production Theory of the Corporation}, 85 VA. L. REV. 247, 310-12 (1999).

\item \textsuperscript{28}See Bebchuk, \textit{Shareholder Access, id.; Lucian A. Bebchuk, The Case for Increasing Shareholder Power,} 118 HARV. L. REV. 833 (2005); Bebchuk, \textit{Myth of the Shareholder Franchise,} id.


boards, and expanding shareholder rights to call special meetings have all received high levels of shareholder support in recent years. In 2009, shareholders at over 80 companies sought more direct leverage with management by supporting "say on pay" requirements that executive compensation be submitted to an advisory vote of the shareholders. Many of these reforms are expected to become standard practice in public corporations in the near future, and all of them expand shareholder voice.

Changing investment practices are also magnifying shareholder voice. In their account of these trends, Anabtawi and Stout identify the rise of aggressive, lightly regulated hedge funds, the emergence of shareholder proxy advisory services that concentrate investor voice, and the creation of complex financial instruments capable of separating voting rights and economic interests as key developments that have strengthened shareholder power. The importance of strong "investor relations" is itself driving many companies to open new channels to engage with shareholders, including direct shareholder surveys and web-based communications.

Heightened demand for greater corporate accountability in the wake of the economic crisis and the failure of leading financial institutions has led to a slew of recent legislative initiatives that further empower shareholders. Most notably, pending SEC rules on proxy access would require companies to include shareholder nominees for director elections in proxy materials at company expense and would authorize shareholder proposals seeking charter or bylaw amendments related to shareholder nominations. Other new rules

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33 2009 Proxy Scorecard, id.

34 Under plurality voting rules, which are the default under current state corporate laws, the directors with the most votes win, even though less than a majority of the shareholders have voted. Under a majority rule, in contrast, "withheld" votes are in effect votes against the candidate, which weakens management control over election outcomes. Most Fortune 500 firms have now adopted some form of majority voting. See Anabtawi & Stout, supra note 17, at 1283 & fn. 106 (citing a 2007 report on such policies). Some of these proposals, such as mandatory majority voting and "say on pay" became part of federal legislative proposals in 2009. See U.S. Sen. Schumer Unveils Shareholder Bill of Rights, REUTERS (online), May 19, 2009, available at http://www.reuters.com/ (last visited Aug. 15, 2009). Corporate and Financial Institution Compensation Fairness Act of 2009, H.R. 3269, July 31, 2009.

35 See Anabtawi & Stout, supra note 17, at 1280-81 (observing that "advisory services coordinate the voting policies of many institutional investors, effectively aggregating their shares into one large voting block, controlled, as a practical matter by the advisory service itself. . . . In short, the widely dispersed individual shareholders of Berle & Means' day, who routinely voted with corporate management, have been replaced to a great extent by a single and far more independent-minded "voter" – ISS."). See also Yermack, supra note 23, at [10-12] (surveying empirical evidence on shareholder activism, including the influence of proxy advisors and the effect of delinking voting and economic rights on shareholder power).

36 See Report of the Task Force of the ABA Section of Business Law Corporate Governance Committee on Delineation of Governance Roles and Responsibilities, Aug. 1, 2009, at 14 (citations omitted).

37 Recent changes to Delaware's corporate code also permit companies to adopt bylaws that give shareholders proxy access at the corporation's expense. DGCL §§ 112-113, effective Aug. 1, 2009. The proposed SEC rules limit these rights to certain shareholders holding at least 5 percent, and for the largest
effective this year further empower investors by eliminating “broker voting” for director elections and increasing investors’ ability to weigh in on executive compensation and monitor corporate risk management.\[^{38}\]

In sum, changing market conditions, regulatory changes, and shareholder activism itself have ushered in a new shareholder-oriented world for public corporations in which more investors are able and willing to take a greater role in shaping corporate decision-making and where corporations are more likely to take notice. However, whether this is a good thing for American corporations, their shareholders, and society as a whole depends in large part on how shareholders use their power. For some critics of shareholder democracy, the answer to these questions depends to at least some degree on whether shareholder voice benefits stakeholders or not.

### B. THE PROBLEM OF STAKEHOLDERS

Concerns about stakeholders have been raised from all sides of the shareholder democracy debate. The basic objection to greater shareholder control raised by Stephen Bainbridge and other director primacy proponents is that the heterogeneity of stakeholder and shareholder interests makes centralized decision-making by the board of directors more, not less, essential to efficient management of the firm,\[^{39}\] whereas expanding shareholder influence over corporate decision-making and decision-makers is likely to undermine board discretion.

More strident critics of shareholder democracy fear that shareholder advocacy of stakeholder interests will balkanize boards, producing *de facto* "constituency directors" who speak for the interests of certain shareholders or stakeholders rather than for shareholders as a class.\[^{40}\] With directors accountable to everyone, they would become accountable to no one.\[^{41}\] At the very least, it is argued, shareholder advocacy of corporations, 1 percent, of the outstanding shares. See Release No. 33-9086, 74 Fed. Reg. 67144 (Dec. 18, 2009); Release No. 33-9046, 74 Fed. Reg. 29024 (June 18, 2009), available at http://www.sec.gov/rules/proposed/2009.shtml. Similar proposals were considered and tabled in 2003, but not before touching off heated debate. For a summary of the debate and its origins, see John H. Biggs, *Shareholder Democracy: The Roots of Activism and the Selection of Directors*, 39 LOY. U. CHIC. L. J. 493 (2008). See also Release No. 33-9046, id. at 29030-31 (regarding related SEC guidance issued in 2007 allowing companies to exclude shareholder nomination bylaw proposals).


\[^{40}\] See Lipton & Rosenblum, *supra* note 29.

\[^{41}\] See *infra* notes 213-212 and accompanying text. The arguments for and against multi-stakeholder
stakeholder interests and other "private" concerns will distract corporate managers from their duty to maximize shareholder wealth. This view was voiced most strongly perhaps by Henry Manne, Dean Emeritus of the George Mason School of Law, in an op-ed on the dangers of shareholder proxy access, where he argued that "the laws of corporate governance should not countenance interference by those activists" who put "social causes, political movements or the reallocation of wealth" above profit maximization with the "contractually established expectations of the vast number of investors [who] are interested exclusively in maximizing their return on investment." To the extent institutional investors might use their influence to "advance personal or political agendas ahead of the [economic] interests of [their fund] beneficiaries," director control becomes even more essential to preserving the economic value of the firm and avoiding costly wrangling over competing and potentially value-reducing investor priorities. In essence, too much attention to stakeholder interests is wealth-reducing and is therefore bad for the firm and bad for shareholders.

Other skeptics of greater shareholder power affirm the importance of attention to stakeholders but observe that corporate directors and officers are already well-positioned to attend to stakeholders under existing law. Thus, there is less need for shareholders to advocate for stakeholders. Management insulation from shareholder control, it is argued, is in fact favorable to stakeholders in that it "ties the hands" of shareholders ex ante to encourage stakeholders to make firm-specific investments without fear that shareholders will transfer value from the firm ex post. These benefits may be lost if shareholders gain real control over management. This view also resonates with progressive corporate law scholars, such as Lawrence Mitchell, who see board control as a better safeguard of firm interests as a whole, and who fear that shareholder pressure for higher profits will keep management from giving proper attention to employees and other corporate stakeholders. In short, shareholder empowerment might actually exacerbate market pressures toward single-minded profit generation, at the expense of stakeholder interests.

More pernicious perhaps are the dangers noted by other scholars that powerful investors will use their power to exact concessions from other corporate constituencies (the "holdup" problem), siphon off firm value toward opportunistic shareholders or fiduciary duties and other rules that would give nonshareholders direct voice in corporate affairs are the subject of a vast literature beyond the scope of this Article. For responses in the context of the shareholder democracy debate, see Bainbridge, supra note 29, at 608-15.


43 See Bainbridge, Limited Shareholder Voting Rights, supra note 29, at fn. 89. See also Lipton & Rosenblum, supra note 29, at 82-85 (arguing that greater shareholder involvement will bog down the corporation in inefficient, value-reducing negotiations with various shareholder groups).

44 See Blair & Stout, supra note 27. Lynn Stout suggests in her later work that she has no objection to shareholder advocacy of stakeholder interests, so long as it is not driven by an economic conflict of interest. See Anabtawi & Stout, supra note 17, at 1284.

45 See Blair & Stout, supra note 27, at 304-05; Bainbridge, Director Primacy, supra note 3, at 579.

46 See, e.g. Lawrence Mitchell, The Board as a Path to Corporate Social Responsibility, in THE NEW CORPORATE ACCOUNTABILITY 207, 283 (Doreen McBarnet et al., eds. 2007).
shareholder coalitions ("rent-seeking"), or align with management to the detriment of nonshareholders ("co-optation" or "gang up"). These concerns echo criticisms first raised in the 1990s about public pension funds' susceptibility to political capture by "special interests" and the potential for their influence to be used to the detriment of other shareholders and of the corporation. Assessing the strength of these competing concerns will require further empirical investigation. What they show clearly, however, is that claims about the merits and limits of shareholder empowerment are entwined with the question of the proper space for stakeholders in corporate decision-making. Largely overlooked in these debates, however, is the possibility that shareholders may define their own long-term economic interests in terms of stakeholders. The "enlightened shareholder value" vision of the corporation described in Part IV is one such approach. It is also one which suggests new responses to some of the concerns surrounding shareholder power. However, before considering this alternative vision and evidence of its emergence, it is important to first review the position of stakeholders under prevailing corporate law rules.

III. STAKEHOLDERS UNDER CORPORATE LAW

Over the course of the past century, the famous debate between Adolph Berle and Merrick Dodd in the Harvard Law Review over the nature and purpose of the corporation has been traced and retraced in a pendulum swing between two fundamental positions: (i) the shareholder-oriented view, that the corporation is formed from the nexus of private contracts (or is, alternatively, a private entity) whose primary purpose is to maximize shareholder wealth, and (ii) the stakeholder view, that the corporation has both public and private roles and must therefore be managed in the interests of a broader range of stakeholders, including employees, consumers, and even the public at large. Corporate

47 See Martin Gelter, The Dark Side of Shareholder Influence, 50 HARV. INT’L L. J. 129 (2009) (arguing that "shareholder oligarchy" creates greater risks of shareholder "holdup" of employees and other nonshareholder groups, even as it creates better conditions for shareholder engagement); Iman Anabtawi, Some Skepticism About Increasing Shareholder Power, 53 UCLA L. REV. 561 (2006), at 575-77, 589-90 (highlighting the dangers of rent-seeking behavior); Anabtawi & Stout, supra note 17, at 1261 (stating that trends in shareholder activism "poin[t] to an inevitable increase in the risk of shareholder opportunism"); Lipton & Rosenblum, supra note 29, at 67 (noting that "there is serious doubt as to whether institutional shareholders, public pension funds, and labor unions – the parties most likely [to engage in shareholder activism] – are well-suited to [monitor directors]" because each "has duties to its own constituencies [and] its own agenda."); Jennifer Hill, Visions and Revisions of the Shareholder, 48 AM. J. COMP. L. 39, 62-63 (2000) (stressing the dangers of alliances between management and powerful institutional shareholders at a time when organized labor is weak).


49 See Adolfe Berle, Corporate Powers as Powers in Trust, 44 HARV. L. REV. 1049 (1931); Merrick Dodd, For Whom are Corporate Managers Trustees?, 45 HARV. L. REV. 1145 (1932). Berle emphasized the fiduciary duties of managers toward shareholder-beneficiaries, while Dodd argued for broader obligations
law in most of the rest of the world follows a stakeholder approach, while dominant understandings of the corporation's role and purpose in the United States remain decidedly shareholder-oriented.

The "standard shareholder-oriented model" of the corporation has generally been viewed to encompass essentially three elements: (i) the view that the corporate objective is to maximize shareholder wealth, as measured by the market value of the corporation’s shares; (ii) the principle that control over the corporation lies ultimately with shareholders; and (iii) the principle that shareholders are the primary beneficiaries of judicially enforceable fiduciary duties owed by management and of special monitoring rights, such as voting rights and the right to bring derivative actions, that are generally not afforded to other corporate constituencies.

The first element, the shareholder wealth maximization norm, establishes both the "ends" of corporate decision-making and the decision-making rule for corporate managers (i.e. the "means") – namely, that managers advance the best interests of the corporation by acting exclusively in the economic interests of shareholders. The second and third principles address the balance of power between shareholders and management, and between shareholders and stakeholders, respectively. Scholarly positions on these dimensions can be traced along the axes introduced by Bainbridge, as shown below. Figure 1

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51 See, e.g. Chen & Hanson, supra note 49 (referring to shareholder primacy as the "macro script of corporate law"); Michael C. Jensen, Value Maximization, Stakeholder Theory, and the Corporate Objective Function, 14 J. APPL. CORP. FIN. 8, 8-9 (2001) (hailing the strong support for the shareholder primacy norm in "200 years of research in economics and finance"). For a history of shareholder primacy, see D. Gordon Smith, The Shareholder Primacy Norm, 23 J. CORP. L. 277 (1998).

52 See Hansmaan & Kraakman, supra note 14, at 440-43.

53 The classic case of Dodge v. Ford Motor Co., which endorsed this proposition, states: "A business corporation is organized and carried on primarily for the profit of the stockholders... 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... in order to devote them to other purposes." Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919).

54 Bainbridge, Director Primacy, supra note 3, at 547-48.
Source: Adapted from Stephen Bainbridge, Director Primacy, supra note 3, at 547-48.

In Figure 1, the vertical axis represents the range of positions with regard to the corporate purpose (the "ends"), and the horizontal axis represents views on the proper center of corporate decision-making power (the "means"). It should be noted that some ambiguity surrounds use of the term "shareholder primacy," which can refer to both the shareholder wealth maximization norm (the vertical axis) and to the view that the balance of power in corporate governance should be set in favor of greater shareholder control (the horizontal axis). Interestingly, with only limited exceptions, neither aspect of shareholder primacy is in fact mandated by corporate law.

A. SHAREHOLDER WEALTH MAXIMIZATION

Despite the divergent uses of the term “shareholder primacy,” it is most often equated simply with the view that the purpose of the corporation is to maximize shareholder wealth. In the oft-quoted words of Milton Friedman, "there is one and only one social responsibility of business – to . . . increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition, without deception or fraud." By establishing the "ends" of corporate decision-making, the shareholder wealth maximization norm also sets a decision-making rule for corporate managers -- namely that the best interests of the corporation are advanced when managers act exclusively in the economic interests of shareholders. Under shareholder primacy in its strongest form, attention to nonshareholders, corporate philanthropy, or any other "socially responsible" activity that is profit-reducing is generally impermissible, because such activities necessarily impair the company's ability to achieve maximum shareholder profits. To the extent that these activities generate profits, at least in the long run, they are simply good business, nothing more.

This is not to say that stakeholders have no place in a shareholder primacy world. Indeed, as Jill Fisch notes, "both Berle and Dodd distinguished the legal obligations of managers to shareholders from their obligations to other stakeholders, but at the same time, acknowledged the legitimacy of other stakeholder interests." Under the standard law and economics argument, the surest way to produce the greatest aggregate social


57 See FRIEDMAN, id. at 136.

58 Fisch, supra note 63, at 646-48.
welfare is to "make corporate managers strongly accountable to shareholder interests, and, at least in direct terms, only to those interests."^{59} By focusing squarely on shareholder wealth maximization, businesses can best contribute to the public good by paying taxes, hiring employees, and providing goods and services.^{60}

In addition, law is part of Friedman’s “rules of the game” within which firms operate and properly constrains the corporation’s freedom to pursue profit maximization.\(^{61}\) Thus, it is generally argued that stakeholder interests matter very much, but are adequately (and best) protected and advanced outside of corporate law by separate bodies of regulation, such as labor, environmental, or consumer protection regulations, and by explicit private contracts, which are the proper tools to address social welfare, equity, and distributional concerns.\(^{62}\)

However, it is generally acknowledged that shareholder wealth maximization is itself a norm of corporate behavior, rather than a legal tenet.\(^{63}\) Indeed, neither caselaw nor corporate statutes impose on directors and officers an obligation to maximize shareholder wealth. Even in Delaware, whose corporate code is less receptive to stakeholder interests than many other state corporate statutes, there is no requirement that management decision-making maximize shareholder wealth or even be justified solely in terms of shareholder interests.\(^{64}\) Moreover, as interpreted by the Delaware courts, directors and officers have a fiduciary duty to act "in the best interests of the company," not solely in the interests of shareholders.\(^{65}\) Accordingly, courts will not second-guess directors’ "business judgment" that is based on concerns about employees, communities,

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59 Hansmaan & Kraakman, supra note 14, at 441. See also FRIEDMAN, supra note 56, at 133-34.
60 Id.
61 See supra note 56.
63 See Jill E. Fisch, Measuring Efficiency in Corporate Law: The Role of Shareholder Primacy, 31 J. CORP. L. 637, 650 (2005) and sources cited therein. See also Smith, supra note 52, at 278 n.1. The Delaware Chancery Court stated in Katz v. Oak Industries, Inc., 508 A.2d 873, 879 (Del. Ch. 1986) that "[i]t is the obligation of directors to attempt, within the law, to maximize the long-run interests of the corporation's stockholders," but later rulings have rejected this view. See Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140, 1145, 1155 (Del. 1990) (holding squarely that the board is under no duty to maximize short-term shareholder value and emphasizing the board's duty is to act in the corporation's best interest and to select the appropriate timeframe for consideration).
64 See Fisch, id. at 652 & fn. 88 (observing that Delaware's corporate statute is noticeably silent "both with respect to the standard by which board decisions are to be evaluated, and with respect to the stakeholders whose interests may legitimately be taken into account.") (citations omitted).
65 Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984), overruled on other grounds by Brehm v. Eisner, 746 A.2d 244, 254 (Del. 2000). Other cases articulate this duty as one owed to "the corporation and its shareholders," though not to "shareholders" alone. See, e.g. Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985), overruled in part on other grounds, Gantler v. Stephens, 965 A.2d 695, 713, fn 54 (Del. 2009). The dominant view among corporate scholars is that little should be read into the emphasis on the interests of the "corporation" as independent from the interests of shareholders, since courts have assumed that the two are synonymous and since any distinction improperly "reifies" the corporation as an independent identity. See Smith, supra note 52, at 285.
and other non-shareholder constituencies, absent any finding of a clear breach of fiduciary duty. In fact, the broad discretion afforded directors under the business judgment rule applies even to profit-sacrificing decisions that benefit nonshareholders.

To be sure, the Delaware Supreme Court in Revlon held that there is a narrow range of cases where the board is required to maximize share price to the exclusion of all other criteria or interests. Specifically, "concern for non-stockholder interests is inappropriate when an auction among active bidders is in progress, and the object no longer is to protect or maintain the corporate enterprise, but to sell it to the highest bidder." However, in Paramount v. Time Warner, the court subsequently limited Revlon to the narrow circumstance of that case, that is, where the board had decided to put the company up for sale. Outside of Revlon mode, "a board of directors . . . is not under any per se duty to maximize shareholder value," and directors are expressly permitted to consider the interests of "creditors, customers, employees, and perhaps even the community generally." Thus, even in the hostile takeover context, directors are generally permitted to reject shareholder-wealth-maximizing bids in the interests of stakeholders, so long as the decision can pass muster under a heightened change of control standard of review.

Beyond the general affirmations of director discretion outlined above, other aspects of current corporate law expressly permit decision-makers to preference stakeholder interests over shareholder wealth maximization. For example, the majority of states (Delaware not included) have adopted constituency statutes, which allow directors to consider the impact of corporate decisions on a broad range of stakeholders – not just on shareholders – and sanction decisions "in the best interests of the corporation" even if they are not justified on the basis of shareholders' economic interests. State corporate statutes also uniformly authorize corporations to make charitable contributions without

66 The exercise of discretion by corporate management is further shielded by standard charter provisions that exculpate and/or indemnify directors and officers for breach of the duty of care. See Gordon Smith, supra note 52 (arguing that because of the expansive scope of the business judgment rule, the true role of shareholder primacy in corporate law has been highly over-rated).

67 Blair & Stout, supra note 27, at 306. The leading case on profit-sacrificing decisions is Shlensky v. Wrigley, 237 N.E.2d 776, 780 (Ill. App. Ct. 1968), where the court upheld the directors' decision to permit only daytime use of the stadium, which favored community interests at the expense of shareholder profits.


69 Paramount Communications, Inc. v. Time Warner, Inc., 571 A.2d 1140, 1145, 1155 (Del. 1990) (upholding board rejection of takeover offer that was based on a desire to protect Time's corporate culture).

70 See Unocal v. Mesa, 493 A.2d 946 (Del. Sup. 1985). Unocal introduced an intermediate standard of review in change of control transactions, requiring the board to show that their defensive action was a proportionate response to a reasonably perceived threat to the corporation.

71 See, e.g. IND CODE 23-1-35-1 (2008). These statutes were adopted in response to the hostile takeover wave of the 1980s and early 1990s. In practice, courts have relied on them only rarely since the business judgment rule and other anti-takeover statutes already protect directors who reject takeover bids out of concern for other stakeholders. See Brett H. McDonnell, Corporate Constituency Statutes and Employee Governance, 30 WM. & MITCHELL L. REV. 1227 (2004).
any showing that the contribution will improve profitability.\textsuperscript{72}

\section*{B. \CONTROL OF THE FIRM: SHAREHOLDER V. DIRECTOR PRIMACY}

With regard to control rights in the firm (the horizontal axis), American corporate law rules are in fact predominantly director-centric, not shareholder-centric. As then-Chancellor Allen once put it, the law "seems to have ringingly endorsed a managerialist or entity orientation," rather than shareholder-centric control rules.\textsuperscript{73} Indeed, both the Model Business Corporation Act and the corporate code in Delaware, the jurisdiction of choice for most publicly traded companies incorporated in the United States, confer upon the board of directors the authority and responsibility to manage the business and affairs of the corporation.\textsuperscript{74} The expanse of the business judgment rule makes this authority quite broad.\textsuperscript{75}

These director-centric rules are in fact quite compatible with a stakeholder orientation, as Professors Blair and Stout demonstrated in their work on a "team production" theory of the firm, in which the public corporation depends upon the firm-specific investments of numerous stakeholders, including shareholders, employees, creditors, and communities. Their interests are mediated by the board of directors in order to maximize the value of the firm to all stakeholders.\textsuperscript{76} With recent trends expanding shareholder influence, American corporate governance appears to be moving toward a model of corporate control where influence over corporate decision-making is shared by shareholders and corporate boards. Nonetheless, the balance remains weighted toward director primacy and gives corporate directors wide latitude to consider, or even preference, the interests of nonshareholders.

\section*{C. \SHAREHOLDER PREEMINENCE OVER STAKEHOLDERS}

However, state corporate laws, as a rule, generally do not give nonshareholders any

\textsuperscript{72} See, e.g. Kahn v. Sullivan, 594 A.2d 48 (Del. 1961) (interpreting DGCL § 122(9), the Delaware authority for corporate charitable contributions, to be limited only by a reasonableness test).


\textsuperscript{74} MBCA § 8.01 (2008) (stating that "[a]ll corporate powers shall be exercised by or under the authority of, and the business and affairs of the corporation be managed under the direction of, its board of directors." \textit{See also} DGCL § 141(a) (2009) (providing that "[t]he business and affairs of every corporation . . . shall be managed by or under the direction of a board of directors.") Lynn Stout also points out that the default rules giving greater discretion to directors also appear to be the initial rules preferred by investors themselves at the IPO stage. See Lynn A. Stout, \textit{New Thinking on "Shareholder Primacy."} [unpublished manuscript, Jan. 10, 2005], available at http://cdn.law.ucla.edu/SiteCollectionDocuments/ucla-sloan\%20foundation\%20conference/new\%20thinking\%20on\%20shareholder\%20primacy.pdf., at 16 (surveying the literature and calling the default rules and these findings on investor preferences the "twin anomalies" of director primacy in U.S. law).

\textsuperscript{75} The broad scope of the business judgment rule continues to be reaffirmed by the courts. \textit{See, e.g. supra} text accompanying note 154.

\textsuperscript{76} See generally Blair & Stout, \textit{supra} note 27.
means of directly influencing corporate affairs, nor do they mandate management attention to stakeholder interests. In particular, the rights of shareholders to elect directors, vote on major corporate transactions, ratify interested transactions, submit proposals for inclusion in the corporate proxy, sue derivatively and benefit from court-enforced director and officer fiduciary duties, are with few exceptions, not extended to other corporate stakeholders. Giving monitoring and enforcement power to shareholders makes corporate managers directly accountable only to shareholders, an arrangement that is deemed to be normatively optimal for reasons discussed further in Section V.

Still, the fact that shareholders alone are the primary beneficiaries of these rights need not be viewed as a legal requirement that management attend only to shareholders’ (economic) interests. Even assuming that shareholders as a class will prioritize wealth maximization, corporate law may grant monitoring and oversight rights to shareholders because they are in the best position to oversee management for the benefit of the firm as a whole. Thus, established corporate governance structures that preference shareholders can be coherently explained from both a shareholder primacy and a stakeholder-oriented standpoint.

IV. DEFINING AND DRIVING ENLIGHTENED SHAREHOLDER VALUE: PATHWAYS BEYOND THE SHAREHOLDER-STAKEHOLDER DIVIDE

As we have seen, cross-currents of the shareholder-stakeholder debate lie beneath some of the core objections surrounding increased shareholder power. We have also seen, however, that corporate law does not prevent, and in fact expressly permits, directors and officers of public corporations to take the interests of nonshareholders into account. In this Part, I introduce "enlightened shareholder value" as an alternative vision of the corporate purpose and present evidence that it is being embraced by a growing number of influential institutional investors. Part V draws on this foundation to assess enlightened shareholder value as a corporate decision rule and explore the response it offers to the stakeholder "problems" that have animated much of the controversy over shareholder empowerment.

A. ENLIGHTENED SHAREHOLDER VALUE UNDER THE U.K. COMPANIES ACT

American corporate law scholars and policy makers have not infrequently drawn

77 Progressive scholars have argued that there is insufficient justification to limit these preferential rights to shareholders. See generally, KENT GREENFIELD, THE FAILURE OF CORPORATE LAW (2007); PROGRESSIVE CORPORATE LAW, supra note 46. However, current Delaware caselaw does not recognize any fiduciary obligations to nonshareholders. Even when the corporation is approaching insolvency, creditors have standing to sue derivatively but are owed no direct fiduciary duties. See N. Am. Catholic Educ. Programming Found., Inc. v. Gheewalla, 930 A.2d 92, 103 (Del. 2007)

78 See infra notes 190-191, 213-212 and accompanying text.

79 See Blair & Stout, supra note 27, at 312-14 (arguing that share price offers a proxy for firm value, albeit an imperfect one, on the assumption that shareholders will vote largely to maximize wealth).
inspiration from regulatory innovations in the United Kingdom. Indeed, the British experience has served as a source for some of Lucian Bebchuk’s recommendations in favor of increased shareholder voice.  

This comparative approach has much to recommend it, since the U.S. and the U.K. share a common legal heritage and because their markets share important similarities – both have been historically characterized by a base of dispersed investors, in contrast to Japan and Europe, where family-owned companies and concentrated ownership structures dominated by banks and conglomerates predominate.

Like the United States, corporate governance in the United Kingdom has historically been grounded on shareholder primacy. However, in 2006, when the United Kingdom enacted its new Companies Act, it took a small step in the direction of the European stakeholder model by introducing an "enlightened shareholder value" paradigm of corporate governance that merges elements of the shareholder primacy and stakeholder models.

The core of the enlightened shareholder value principle is embodied in Section 172 of the Companies Act, which defines the fiduciary duties of corporate directors as follows:

"A director . . must act . . in good faith . . to promote the success of the company for the benefit of its members as a whole, and in doing so have regard to . . (a) the likely consequences of any decision in the long term, (b) the interest of the company's employees, (c) the need to foster the company's business relationships with suppliers, customers and others, (d) the impact of the company's operations on the community and the environment, (e) the desirability of the company maintaining a reputation for high standards of business conduct, and (f) the need to act fairly as between members of the company." (emphasis added)

As under prior law, these duties are monitored and enforced by shareholders through litigation.

The Act also requires listed companies to recognize and report on stakeholder matters as

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80 See Bebchuk, Shareholder Power, supra note 28, at 847-50.
81 See Jacoby, supra note 30, at 5 and sources cited therein.
84 The limited caselaw applying Section 172 has simply confirmed that it is to be interpreted in accordance with existing common law rules, equitable principles, and existing laws that require directors to give priority to the interests of creditors in certain instances. Id. at § 170, Part 11 (member (i.e. shareholder) litigation rights). See Andrew Keay, Moving Towards Stakeholderism? Constituency Statutes, Enlightened Shareholder Value, and All That: Much Ado About Little? (unpublished manuscript on file with author), Jan. 2010, at 21-22.
part of providing comprehensive disclosures to investors. Specifically, the mandatory directors’ report, a business review of both financial and non-financial performance indicators, must include either information about the company’s environmental impact, employees, social and community issues, and "essential" contractual arrangements, or a statement detailing which type of information is not being provided. These disclosures are required unless the information is not "necessary for an understanding of . . . the company's business."85 Per Section 417(2) of the Companies Act, this report is explicitly intended to permit members to evaluate directors’ compliance with their fiduciary duties under Section 172.

Nonetheless under the Companies Act, directors remain directly accountable only to shareholders. The Act maintains the (unitary) board of directors as the decision-making authority of the firm, with space for some degree of member (i.e. shareholder) control. It also rejects the European Union's approach to takeover law and labor issues, such as German codetermination or other requirements that labor be represented on corporate boards.86 Consistent with prior law, the Companies Act also places shareholders as the sole corporate constituent permitted to elect directors, bring a derivative suit, and authorize interested transactions.87

The central elements of this "enlightened shareholder value" model then are (i) an explicit focus on long-term shareholder value as the goal of the corporation; (ii) a requirement that corporate directors and officers consider the effects of their decisions on the "extended stakeholder constituencies," financial and non-financial, that are referenced in Section 172, and (iii) a rejection of changes to the corporate decision-maker (i.e. the board with shareholder oversight) or the rules that give shareholders monitoring and enforcement rights not afforded other stakeholders.

To no small degree, then, "enlightened shareholder value" looks like the standard Anglo-American corporate governance model. As its name suggests, it is grounded squarely within a shareholder-primacy paradigm that emphasizes economic efficiency and returns on shareholder investments. It might also be argued that this "enlightened shareholder value" approach differs little from the current state of affairs under state nonshareholder constituency statutes, which permit corporate management to consider the interests of the various stakeholders contemplated by the U.K. Companies Act reforms.88 But in contrast to both traditional shareholder primacy (and the approach of most constituency statutes), the U.K. reforms require boards to justify their decisions in

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85 UK Companies Act, § 417. These provisions represent a much watered-down version of the mandatory social reporting requirements that were initially introduced in the United Kingdom in 2005 for the largest public companies as the Operating and Financial Review (OFR). The OFR was later abolished and ultimately replaced by Section 417 of the Companies Act. For a description of the OFR, see Williams & Conley, supra note 7, at 516-522. On the Companies Act version, see generally Clark & Knight, supra note 82.

86 Williams & Conley, supra note 7, at 550.

87 See, e.g. U.K. Companies Act, supra note 85, at arts. 188-223, 239 (various interested transactions requiring member approval), Part 11 (derivative claims by members).

88 See supra note 71 and accompanying text.
terms of stakeholder interests and to disclose risks impacting stakeholders. By doing so, the U.K. endorses a multi-stakeholder decision-making rule and makes management at least indirectly accountable to stakeholders. In short, the goal of the U.K. approach is to "maintain [corporations'] financial accountability to a constituency of dispersed, independent shareholders while simultaneously using market forces to nudge companies in the direction of greater social responsibility." 89 (emphasis added).

To date, there has been no movement in the United States to follow the U.K. and mandate "enlightened shareholder value" through state or federal corporate legislation. Indeed, there are many reasons why such a stakeholder-oriented regulatory shift is unlikely. First, of the states that have already enacted constituency statutes, only one makes consideration of stakeholder interests mandatory. 90 Key differences between the dominant institutional investors in the U.K. (pension funds/insurers) and the U.S. (mutual funds), as well as the two countries' regulatory environments, make stakeholder-oriented corporate reform less likely in the U.S. 91 But given the strong and growing shareholder-orientation of the U.S. market, it is more likely that "enlightened shareholder value" will instead make inroads through shifts in the power and priorities of shareholders themselves.

B. INVESTOR-DRIVEN ENLIGHTENED SHAREHOLDER VALUE

More than two decades of scholarship has considered (and largely dismissed) the possibility that large institutional investors and other shareholders could drive greater corporate accountability to shareholders, much less bring about a new era of corporate social responsibility. 92 However, the rise of shareholder democracy, the growing market power of institutional investors, and changes in the economic and regulatory climate all give cause for a second look. Indeed, as I explore below, many influential institutional investors now view attention to stakeholder concerns, such as environmental protection, labor and human rights, and related corporate governance reforms, as key to long-term financial gain, at a time when they are also well-positioned to bring this "enlightened shareholder value" vision into mainstream U.S. corporate practice.

In this Section, I consider indicators of these trends, as well as the avenues through which these investors are seeking to advance greater stakeholder-orientation among investment

89 Williams & Conley, supra note 7, at 500.

90 Connecticut is the sole state where consideration of stakeholder interests is mandatory. See CONN. GEN. STAT. § 33-756(d). The literature defending and attacking constituency statutes is too vast to cite fully here. See, e.g. Stephen Bainbridge, Interpreting Nonshareholder Constituency Statutes, 19 PEPP. L. REV. 971 (1992) (summarizing the literature).

91 See Williams & Conley, supra note 7, at 499, 529 (speculating that movements toward shareholder power might in future give rise to the phenomenon explored here – that "shareholders [might] define shareholder value to include stakeholder concerns" (emphasis in original). See also supra notes 18-23 (regarding institutional investor characteristics). Although some of these gaps are narrowing, the British government remains much more strongly committed to advancing corporate social responsibility than U.S. state and federal governments, and societal support for these goals is arguably still stronger in the U.K.

92 See supra note 16 and accompanying text.
intermediaries and in corporate practice. My purpose here is not to demonstrate that shareholders are better positioned to advance stakeholder interests than, for example, boards or stakeholders themselves. Rather, I aim to show first that investors are both able and willing to do so, and for reasons that are in fact quite conventional – the prospect of higher long-term returns and more comprehensive information on investment risks.


One of the most important expressions of an emerging "enlightened shareholder value" paradigm is growing attention to stakeholder issues as a critical element of firm and portfolio risk management. Much of the current energy in this direction has been focused on developing tools to help firms, investors, and fund managers identify, measure, and manage "environmental, social, and governance" (ESG) risks in order to improve the quality of information available to investors and potentially increase overall portfolio returns and firm competitiveness.

The scope of "ESG" risks is in fact not limited to "environmental, social, and governance" measures, but extends to all "extra-financial" fundamentals that can impact financial performance, such as climate change, corporate governance, employment standards, human resources, executive compensation, environmental impact, and reputational risk. Such issues are not reflected in standard accounting measures because they are typically qualitative in nature, are related to externalities not well captured by standard accounting measures, are forward-looking, and/or have effect largely in the medium- to long-term. Some ESG risks, particularly environmental risks, are increasingly material for many companies because they are the subject of public concern and/or are areas of heightened regulatory attention. Although the precise issues and measures that matter to particular investors or firms may vary, it is clear that ESG investment strategies require investors, financial intermediaries, and corporate management to account for the effects of corporate operations on a wide range of nonshareholder constituencies.

Among the broadest efforts to mobilize mainstream institutional investors around an ESG-oriented approach are the United Nations' Principles for Responsible Investment (PRI). The PRI were developed by the joint efforts of 20 leading institutional investors under the auspices of the United Nations Environmental Programme Finance Initiative (UNEP FI) and the United Nations Global Compact in 2006.

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93 Alternative terms have been suggested for what I refer to here as ESV. See, e.g. Hess, supra note 12 (proposing "sustainable long-term responsible investment" or simply "LTRI" and noting that no uniform terminology has yet emerged).

94 "Social risks" are risks arising from practices affecting the workforce, such as liability risk, or reputational risk associated from poor employment practices.


96 The PRI initiative is governed by an elected Board of 11 representatives from asset owner signatory organisations and two representatives from the United Nations. The Secretariat reports to the PRI Board.
signatories commit to voluntarily support and implement the following six core principles in a manner consistent with their fiduciary duties toward their beneficiaries: (i) Incorporate ESG issues into investment analysis and decision-making; (ii) Adopt an active ownership strategy and engage portfolio companies around ESG issues (iii) Seek appropriate ESG disclosures from portfolio companies; (iv) Promote acceptance and implementation of the PRI among service providers and others within the investment industry; (v) Collaborate with other signatories to implement the PRI; and (vi) Disclose to beneficiaries and the public how ESG issues are integrated within investment practices, policies toward service providers, and active ownership activities.97

The primary goal of the PRI is to channel institutional investor power toward promoting the integration of ESG issues within internal investment practices, by financial intermediaries, and down the investment chain to portfolio companies.98 Secondarily, the PRI creates a framework for institutional investor accountability to industry peers and to the public for progress toward these goals. The PRI is significant because its intended scope is not limited to isolated issues, portfolio companies, or investors, but rather extends horizontally across the investment industry, vertically throughout the investment (and ultimately, supply) chain, and broadly across a range of corporate social responsibility and stakeholder concerns.

2. The ESG Rationale

Historically, stakeholder-oriented investment has been identified almost exclusively with "socially responsible investment" (SRI) strategies that identify particular industries or firms to exclude from (or include in) an investment portfolio based on certain ethical or "values-based" screens and may prioritize ethical, religious, social, and/or environmental concerns equally or above financial risk and return.99 Many institutional investors shy away from social screening because of regulatory diversification mandates,100 because of the perception that ethical or moral investment criteria cannot be adopted by ERISA fiduciaries,101 or because of the belief that a restrictive investment approach will result in systematically below-market returns and overall higher risk exposure.102 The limits of

98 Id.
99 This definition is adapted from Lloyd Kurtz, Socially Responsible Investment and Shareholder Activism, in THE OXFORD HANDBOOK OF CORPORATE SOCIAL RESPONSIBILITY 250 (Andrew Crane, et al., eds. 2008) 250.
100 For a survey of these limits, see sources cited at note 28.
101 Many pension fund managers are of the view that ERISA's prudent investor standard requires a unitary focus on maximizing returns to beneficiaries and thus prevents them from basing investment decisions on ethical or other non-financial factors. See RONALD B. DAVIS, DEMOCRATIZING PENSION FUNDS: CORPORATE GOVERNANCE AND ACCOUNTABILITY 56-62 (2008) (discussing pension fund fiduciary duties).
102 There is some evidence that over the long term SRI screened funds may perform at least as well as unscreened peers (but not better); however, there is some evidence based on SRI indices that SRI
the screening model are among the key factors that have kept SRI from being embraced by the mainstream investment community and from having a deeper impact on corporate practice.\textsuperscript{103}

ESG-oriented investing and activism, however, is grounded on traditional economic rationales. The two primary rationales that together form the "business case" for this form of "responsible investment" are (i) the prospect of higher long-term returns, and (ii) improved firm-level risk management and portfolio-level risk analysis. For example, the PRI affirms that a focus on ESG matters "may better align investors with the broader objectives of society," but its fundamental rationale is solidly grounded in shareholder primacy – namely, that "consideration of [ESG] issues is part of delivering superior risk-adjusted returns" to investors over the long run.\textsuperscript{104} Given the potentially controversial nature of an effort to define shareholder value explicitly with reference to stakeholders, it is important to unpack the relationship between ESG risk management and financial performance.

\textbf{a. Firm-Level Risk Management and Financial Performance}

Considering first the firm-level perspective, the rationale is that management failure to understand and respond to ESG risks can hurt the company's long-term financial performance, while monitoring ESG issues can help management identify such risks as well as new opportunities to generate long-term shareholder wealth.\textsuperscript{105} Reducing firm-level risk can confer direct benefits on managers, employees, creditors, and other stakeholders who have made firm-specific investments in the company and thus have vested interests in the firm's survival. Better ESG risk management may also benefit the firm by lowering the cost of capital.\textsuperscript{106} If attention to ESG matters translates into a broader commitment to corporate social responsibility, it may also produce economic benefits by improving brand loyalty, employee retention and motivation, resource allocation, and overall competitive advantage.\textsuperscript{107}

A number of studies by the United Nations Environmental Programme Finance Initiative investments may not exhibit a lower risk profile than comparable non-SRI investments. \textit{See} Kurtz, \textit{supra} note 99, at 269-71.


\textsuperscript{104} PRI FAQs, available at http://www.unpri.org/faqs/ (last visited Feb. 15, 2010).

\textsuperscript{105} \textit{See}, e.g. Enhanced Analytics Initiative, "What are EFIs [extra-financial issues]?", www.enhanced-analytics.com (follow "What is EAI?") (last visited Sept. 1, 2009). \textit{See also infra} note 108.

\textsuperscript{106} \textit{See} Mark Sharfman & Chitrur S. Fernando, \textit{Environmental Risk Management and the Cost of Capital, _ STRAT. MGMT. J. _} (forthcoming 2009) (presenting empirical evidence that environmental risk management reduces the cost of equity capital and allows firms to more easily obtain debt financing).

(UNEP-FI) and other researchers testing these claims have found either a neutral effect or a positive correlation between ESG factors and corporate financial performance (CFP).\textsuperscript{108} While further research is needed, these early results lend support to the substantial empirical literature finding, on balance, that there is weak but positive correlation between corporate social performance (CSP) and CFP.\textsuperscript{109}

b. Portfolio-Level Risk Management and Financial Performance

At the portfolio level, the argument that better ESG risk assessment will improve risk-adjusted returns across a portfolio is more complex. First, ESG risks can be either systematic (i.e. "undiversifiable") risks affecting the market as a whole (measured by $\beta$) or unsystematic, "diversifiable" risks that are firm-specific. Systematic risks include the risk of regulatory, socioeconomic, or political changes, such as a change in the rate of inflation. Examples of firm-specific (i.e. diversifiable) risk, on the other hand, might include risk related to potential product liability claims or a change in corporate management. According to the standard capital asset pricing model (CAPM), to the extent that investors are able to diversify away firm-specific risk (even if they fail to do so), they are not compensated with a higher risk premium on the asset.\textsuperscript{110} Thus, there should be no economic gain to the investor from reducing firm-specific risk.

However, modern portfolio theory offers an explanation for why large institutional investors might want to reduce even firm-specific risk -- namely, that unique, firm-specific risks, such as the risk created by poor environmental practices, are in fact internalized by the portfolio investor, since the cost of the harms, or negative externalities, produced by one portfolio firm may in fact be borne by other portfolio firms.\textsuperscript{111} These costs might arise directly -- for example, if environmental harms impact real estate owned or insured by another entity in the portfolio -- or may be indirect costs assessed against the economy as a whole, for example, higher tax rates imposed in a


\textsuperscript{109} See David P. Baron, Mareton A. Harjoto, & Hoje Jo, The Economics and Politics of Corporate Social Performance, unpublished manuscript, April 21, 2009, available at http://ssrn.com/abstract=1202390 at 4 (surveying the empirical literature). See also Marc Orlitsky, Corporate Social Performance and Financial Performance: A Research Synthesis, in THE OXFORD HANDBOOK OF CORPORATE SOCIAL RESPONSIBILITY, supra note 99, at 113 (conducting a meta-analysis of the literature and concluding that "there is a positive, but highly variable, relationship between [the two] and that they are mutually reinforcing and positively correlated). But see Amann, et al., supra note 24, at 343-44 (concluding from a similar meta-analysis that "numerous" empirical studies on the links between corporate social performance and corporate financial performance have been done "without arriving at truly proven results one way or the other").


\textsuperscript{111} See HAWLEY & WILLIAMS, supra note 18, at 5-18, 98-99 (noting that such investors will for similar reasons have interest in encouraging firms to produce positive externalities, such as through research and development).
Given locality to cover environmental cleanup. Therefore, highly diversified investors have a direct incentive to seek more comprehensive information on the externalities produced by portfolio firms and to respond to such information through exit or engagement.

Moreover, some highly diversified investors, including ESG’s main proponents, are so-called "universal owners," a term which refers to public and private pension funds, mutual funds, labor union funds and other large institutional investors that are diversified to the point that they are in essence invested across the entire economy. Because of the breadth of their holdings, such investors have particular incentives to attend to the long-term health of the broader economy and to address issues, such as the environment, labor practices, health care, and anti-competitive behavior, that impact entire industries and the economy as a whole.

One of the most important reasons why prominent institutional investors and financial intermediaries are behind much of the movement to account for ESG risks is that more comprehensive information regarding firm-level ESG risks might increase the quantity and quality of non-financial information available to the markets and better enable diversified owners to more accurately structure their portfolio in accordance with their risk preferences. Institutional investors rely strongly on the information reflected in market prices and on financial agents’ responses to those prices. If, as is now widely recognized, there are limits to market efficiency, then the market may only imperfectly account for risk.

Moreover, since comparable, verifiable information related to certain stakeholder interests, such as environmental and social matters, is essential if markets are to accurately evaluate firms’ market prices, its absence means that the entire market (and thus the investors’ portfolio) is subject to systemic distortions. If this is so, incorporating ESG factors into investment analysis may also offer a way for investors to achieve higher risk-adjusted returns (measured by alpha) – that is, to "beat the market" – by exploiting these informational inefficiencies, at least until other investors trade on the same information and the market adjusts. Ultimately, the creation and dissemination of data on ESG and non-financial corporate performance measures should also improve the

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112 These examples are drawn from Hawley & Williams, id. at 4-5.

113 According to Hawley and Williams, a "universal owner" is "an institutional owner whose holdings are highly diversified and, typically, held long term," such that they essentially represent a cross-section of the entire economy. Hawley & Williams, supra note 18, at 3.


115 Clark & Knight, supra note 82, at 269.

116 See Stout, supra note 74, at 21 (citing empirical studies challenging the ECMH, including research on heterogeneous expectations asset pricing models, the limits of arbitrage, and behavioral finance). See also Lynn A. Stout, The Mechanisms of Market Inefficiency: An Introduction to the New Finance, 28 J. CORP. L. 635 (2003).

117 Clark & Knight, supra note 82, at 269.
efficiency and accuracy of pricing signals in the market as a whole, although again reducing the likelihood of unique gains to ESG-informed investors. These informational benefits can be realized even if the ultimate allocation of portfolio funds remains unchanged.

As with firm-level analyses, empirical studies to date have generally found that incorporation of ESG measures into portfolio allocation decisions has either a neutral or positive effect on portfolio returns relative to standard benchmarks. These studies lend some support to the view that investors may reap financial rewards (i.e. alpha) relative to the market by being the "first movers" investing with the benefit of ESG-related information.

3. Implementation & Diffusion

Despite the rise of shareholder empowerment, questions remain about whether public pension funds and other institutional investors will use their power to promote long-term "responsible investing" or ESG-oriented investing strategies, and if so, whether their voices will outweigh counter-pressure from investors who do not share this view. Indeed, it is widely recognized that for much of the past decade, market pressures and the behavior of institutional investors themselves encouraged aggressive risk-taking and an over-emphasis on short-term profits. Past studies also suggest that given the reality of high portfolio turnover and the costs of activism, the vast majority of public pension

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119 See, e.g. Goldman Sachs Global Investment Research, “Introducing GS SUSTAIN,” June 22, 2007, at 6-10, available at http://www.unglobalcompact.org/docs/summit2007/gs_esg_embargoed_until030707pdf (finding no correlation between ESG performance and stock market performance, but that incorporating ESG factors into long-term industry and returns-based analysis identified companies that outperformed relevant indices by 25 percent between 2005 and 2007 and outperformed peers by 75 percent over the same period). It should be noted that the findings were based on Goldman Sachs’ proprietary ESG analytics.

120 See Aspen Institute, Overcoming Short-termism: A Call for a More Responsible Approach to Investment and Business Management, Sept. 9, 2009; Sanford M. Jacoby, Finance and Labor: Perspectives on Risk, Inequality, and Democracy, 30 COMP. LAB. LAW & POL’Y J. 17, 24-25, 57-61 (2008). Even public pension funds, those often viewed most likely to promote corporate accountability, fueled short-termism by shifting more holdings toward higher-risk, higher-return investments, such as private equity and hedge funds, and by compensating fund managers on the basis of short-term industry returns. See Hess, supra note 12. See also Robert C. Illig, The Promise of Hedge Fund Governance: How Incentive Compensation can Enhance Institutional Investor Monitoring, 60 ALA. L. REV. 41 (2008) (proposing an alternative compensation structure based on approaches common in private equity investments). Investor short-termism may reduce incentives for firms to focus on stakeholders by, for example, reducing environmental degradation or funding worker health and safety programs, since the costs of such measures are incurred in the short term while the benefits (or the risks of failing to do so) are often material, if at all, only in the long term.
funds and other institutional investors will remain rationally apathetic and leave the challenge of translating ESV into corporate practice in the hands of a relatively limited number of institutional activists. 121 And even if these barriers are overcome, "enlightened" investor activism might simply create more sustainability "talk" and less "walk" among public companies. 122

However, for a new stakeholder-oriented norm to compete with traditional shareholder wealth maximization, it is not necessary that all market participants sign on so long as market leaders (both investors and corporate management) have a shared interest in promoting change. Indeed, many of the successes of investor activism highlighted below are the result of a limited number of activists focusing their efforts on select targets, generally the largest, most visible public companies in order to spur market-wide changes. 123 As the following discussion shows, ESV principles are already being adopted by leading institutional investors and other mainstream financial institutions, many of whom have a history of active engagement with the firms they invest in.

a. Institutional Investors & Enlightened Shareholder Value

At an initial level, investor adoption of an enlightened shareholder value approach can be seen from the UN PRI itself. As of the first quarter of 2010, nearly 700 institutional investors, asset managers, and industry service providers, representing $18 trillion in assets under management, had signed onto the PRI. U.S. signatories now account for over 15 percent of all PRI signatories and include 20 public, private, and union pension funds, including CalPERS, CalSTRS, AFL-CIO funds, and Connecticut, Illinois, and New York state pension funds, as well as over 60 prominent asset managers, such as TIAA-CREF. 124 These signatories are among the most prominent activist investors.

PRI signatories and other investors are also implementing ESG principles in their investment practices. 125 For example, CalPERS and other major public pension plan’s investment guidelines already mandate consideration of ESG factors in addition to standard financial analysis. 126 While ESG practices have made slower headway among

121 See, e.g. Choi & Fisch, supra note 17; Hess, supra note 12; Bainbridge, Limited Shareholder Voting Rights, supra note 29, at 628-36 (questioning the ability and will of institutional investors to engage in activism).

122 See, e.g. Conley & Williams, supra note 103. But see Lisa M. Fairfax, Easier Said Than Done? A Corporate Law Theory for Actualizing Social Responsibility Rhetoric, 59 FLA. L. REV. 771 (2007) (emphasizing the force of rhetoric in shaping corporate behavior). I defer here for the moment the further challenge that activists investor "enlightenment" may simply reflect political pressure, conflicts of interest, self-interest and other value-reducing motivations. These are considered in Part V.

123 See Yermack, supra note 23, at [21].


126 See, e.g. Robert G. Eccles and Aldo Sesia, CalPERS' Emerging Equity in the Markets Principle (March
mainstream mutual funds, Vanguard, a leader in passively managed investments, recently adopted investment policies on human rights practices of portfolio firms that may pave the way for other passively managed funds to incorporate ESG analysis.\textsuperscript{127} Recent analyst reports of the mutual fund industry also point to a growing recognition of ESG indicators as integral to identifying strong performers.\textsuperscript{128} New analytical tools and investor advisory services are being developed to help investors and financial intermediaries overcome the practical obstacles defining, quantifying, and monitoring extra-financial factors, such as "sustainability," a commitment to labor standards, or a positive human rights record, in a comparable and consistent manner.\textsuperscript{129}

Support for emerging conceptions of enlightened shareholder value is further amplified by its natural overlap with much of the SRI movement,\textsuperscript{130} which shares ESV’s emphasis on non-financial risks and long-term returns and accounts for $2.7 trillion assets under management.\textsuperscript{131} The list of PRI investment advisor signatories is indicative of this, as it


\textsuperscript{130} Although most ESV investors do not rely on screening strategies, screening-based SRI is compatible with ESV insofar as its ultimate objective is generating long-term shareholder wealth. \textsuperscript{131} See Kurtz, supra note 99, at 249, 251-53 (noting that SRI is no longer solely the domain of religious orders and other altruistic or "values-based" investors, but now includes “value-seeking” investors as well). The primary difference is that ESV investors would not generally share some SRI investors’ tolerance for investments that generate below-benchmark returns but are stronger on ethical measures.

\textsuperscript{131} As of 2007, 11 percent of professionally managed assets in the U.S., then valued at $2.7 trillion, were engaged in some form of SRI, according to the Social Investment Forum, the U.S. trade association for SRI investment and research. These figures include over 260 socially screened mutual fund products in the US, with assets totaling $201.8 billion. 2007 Report on Socially Responsible Investing Trends in the United States, Social Investment Forum Biannual Report, available at http://www.socialinvest.org/resources/pubs/documents/FINALExecSummary_2007_SIF_Trends_wlinks.pdf (last visited Feb. 2, 2010). \textsuperscript{131} See also 2008 ESG Background Report, supra note 31 (reporting that this represents a growth in SRI assets of over 18%, compared to 3% for non-SRI managed assets.)
includes both “responsible investment” leaders like Domini Social Investments and mainstays of the financial services industry such as JPMorgan Asset Management and Risk Metrics Group/ISS.

Financial intermediaries are also beginning to focus on ESG risk measures in making investment allocations. These changes are particularly important because the vast majority of institutional investors rely on external fund managers to make investment decisions and many also delegate proxy voting authority to fund managers. As of 2008, public pension funds in New York, Connecticut, Maryland, and California already required ESG disclosure by managers and were including ESG matters in standards for fund manager evaluations. One recent survey of 319 fund managers, only 23 percent of whom self-identified as “socially responsible investors”, found that 99 percent include ESG factors in their investment analysis and over 70 percent view ESG as a tool to identify investment opportunities as well as to manage risk. Mainstream financial institutions, such as Citigroup, HSBC, Goldman Sachs, and State Street Global Advisers are also contributing to or endorsing research on ESG implementation and integration.

The global economic crisis has moved public opinion and public policy further in the direction of ESV by calling attention to the dangers of short-term investment strategies and encouraging a better balance between risk-taking and risk management. As a result, public pension funds and other asset owners are beginning to review their compensation practices in order to better focus fund managers on long-term performance. Recently adopted SEC disclosure rules now encourage tighter board (and investor) monitoring of corporate risk management functions at a time when many investors recognize the importance of broader measures of risk, including ESG risks, in evaluating long-term firm performance and in portfolio risk analysis.

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132 See Choi & Fisch, supra note 17, at 324 (reporting that over 84 percent of assets of the pension funds surveyed were externally managed).
135 In addition to those named above, studies by the UNEP Finance Initiative have been endorsed or supported by ABN Amro, the Conference Board, Credit Suisse Group, the IFC, Innovest (now a part of RiskMetrics), UBS, and the World Bank Group, among others. See supra note 108.
137 See 2008 ESG Background Report, supra note 31. On the problem of short-term-oriented fee structures, see supra note 120.
138 See, e.g. Release No. 33-9089, supra note 38 (proxy disclosure enhancements on board oversight of risk
developments suggest that the emergence of ESV and broader economic trends may be mutually reinforcing and may together contribute to a fundamental reassessment of what corporate accountability to shareholders requires.

b. Translating Enlightened Shareholder Value to Firms

For investor-driven ESV to impact corporate decision-making, a broader vision of corporate accountability must ultimately be transmitted to corporate boards and managers. But how does this occur? And if ESV is advanced through market forces rather than through regulatory mandate, to what extent, if at all, does it "have teeth"?

At base, ESG-oriented investors influence firms by communicating that recognizing, reporting, and responding to ESG risks matter. This occurs as institutional investors use the tools of shareholder activism to seek more comprehensive reporting from portfolio firms on stakeholder impacts, require investment intermediaries to take this information into account in allocating investments, and urge intermediaries to communicate to firms that investors are basing investment decisions in part on ESG measures.

Disclosure requirements under U.S. federal securities regulations, including those under Regulation S-K and Regulation S-X, already mandate that firms disclose ESG risks or other information if there is a substantial likelihood that a reasonable investor would consider it important in deciding how to vote or make an investment decision, or if it would alter the total mix of available information. For example, as the SEC reaffirmed in January of this year, the legislative, regulatory, business, market, and physical impacts of climate change are increasingly material to public companies and investors and must therefore be addressed in regular public filings.

For example, in 1999 the U.K. amended its pension regulations to require trustees of local public pension funds to disclose the extent to which "social, environmental or ethical considerations are taken into account in the selection, retention, and realization of investments" as well as any policies concerning the exercise of voting rights associated with their investments. For example, in 1999 the U.K. amended its pension regulations to require trustees of local public pension funds to disclose the extent to which "social, environmental or ethical considerations are taken into account in the selection, retention, and realization of investments" as well as any policies concerning the exercise of voting rights associated with their investments. See Williams & Conley, supra note 7, at 504 (referencing the 1999 amendments to the U.K. Pensions Act of 1995). But see Clark & Knight, supra note 82, 270-71 (2009) (finding that the 1999 regulations had little impact because the primary obligations fell on fund managers rather than on institutional investors).
and Europe.  

Investor advocacy of stakeholders also comes in the context of a resurgent corporate social responsibility movement that in both Britain and the U.S. has proven to be a powerful driver toward broader measures of accountability. Many corporations face market pressure from consumers, employees, and civil society to consider their impact on stakeholders. As a result, the vast majority of U.S. public corporations already voluntarily issue "sustainability", "triple-bottom-line" (financial, social, and environmental), ESG, or annual reports describing their commitment to stakeholders, generally based on indicators developed by the Global Reporting Initiative (GRI). Sustainability reporting in any of these forms is also increasingly seen by investment analysts as an important risk assessment tool.

However, investor demand is still critical to driving improved ESG reporting and performance. ESG disclosures under the securities laws have on the whole been limited in quantity and scope, whether because these risks have not been identified by firms, because they have not previously been viewed to be material, or because of firms' conservative approach toward qualitative and forward-looking disclosures. Voluntary disclosures, while more widespread, are inherently selective and are for many institutional investors, inadequate to ensure transparency and accountability with respect to ESG issues. Investors are therefore increasingly engaging with companies to advance corporate governance reform that includes closer attention to ESG issues and

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144 On the U.K. requirements, see supra note 85. See Williams & Conley, supra note 7, at 502-10 (describing requirements in Europe).

145 See generally ECONOMIST, Jan. 19, 2008 (special issue on corporate social responsibility).


147 See generally, Lisa M. Fairfax, The Rhetoric of Corporate Law: The Impact of Stakeholder Rhetoric on Corporate Norms, 31 J. CORP. L. 675, 691-94 (2006) (finding that over 50 percent of Fortune 50 companies produce sustainability reports and that nearly 90 percent of Fortune 500 companies' annual reports address stakeholder issues). See also Williams and Conley, supra note 7, at 496 (observing that the "identification and disclosure of corporate information concerning social and environmental risks" is itself a prime indicator of pro-stakeholder convergence).

148 See www.globalreporting.org. For comparisons of widely used indicators and standards, see generally COOPER, supra note 3, at 32-38.

149 Id.

150 The PRI itself is intended to improve the level and quality of non-financial reporting, particularly under the UN Global Compact. See www.unpri.org; www.unglobalcompact.org.


152 Id. See also Commission Guidance, supra note 129, at 7-10 (describing level of current disclosures related to climate change).
increasingly vocal about the types of information they regard as material to their investment decisions.

i. Litigation

In the U.K., Section 172 of the Companies Act is enforceable through shareholder litigation. However, early implementation experience there suggests that the anticipated flood of shareholder suits has not materialized, and that the primary effect of the law have been to urge companies to more carefully document their consideration of the impact of corporate decisions on stakeholders.\(^{153}\)

In the U.S., litigation is not likely to be a significant means of promoting an enlightened shareholder value decision rule, with the possible exception of claims challenging inadequate or misleading disclosures under the securities laws. The Delaware Court of Chancery's decision in \textit{In re Citigroup} has reaffirmed the strength of the business judgment rule, making clear that shareholder litigation alleging director failure to adequately oversee risk management or mitigate potentially high-impact risks will be unlikely to prevail. There the court held that Citigroup's directors and officers could not be found liable for a breach of the duty of oversight articulated in \textit{In re Caremark} for allegedly failing to mitigate "excessive" business risk, notwithstanding catastrophic losses to shareholders resulting from the subprime mortgage crisis.\(^{154}\)

ii. Voting & Engagement

Another option is for investors to simply divest from firms with poor ESG performance (i.e. the "Wall Street Walk"). However, exit will in most cases be "invisible" to the firm absent any other communications from the investor and may not be a viable option for many investors with large holdings. In contrast, the exercise of voting power and direct negotiation with management are increasingly powerful tools for investors to influence corporate practice.

Investors are authorized to vote for the election of directors (or withhold votes from candidates they disapprove of), initiate or support shareholder proposals, and under "say on pay" voting measures may "comment" on executive compensation. Empirical studies indicate that even when unsuccessful, a strong vote for a shareholder proposal, or weak support for a management proposal or director nominee, often sparks changes in the board, management, or corporate practices in the aftermath of the vote.\(^{155}\) ESV-oriented investors may therefore be able to leverage their support for director candidates,

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\(^{153}\) See Loughrey et al., \textit{supra} note 7, at 96-101, 110-11. \textit{See also supra} note 84.


\(^{155}\) See Yermack, \textit{supra} note 23, at [6-10] and sources cited therein (examining the impact of shareholder voting on boards and corporate strategy).
executive compensation, or governance measures in a way that rewards directors who are well-aligned with an enlightened shareholder value approach.

Shareholders can also directly advocate for stakeholder interests through "social activism", that is, shareholder activism around labor, environmental, or human rights issues. To date, shareholder social proposals and related shareholder campaigns have tended to be ad hoc, issue-specific, and driven by ethically-motivated and interest group investors rather than by mainstream institutional investors.\(^{156}\) Few have actually passed.\(^{157}\)

However, recent years have witnessed a growing level of shareholder (and proxy advisor) support for social or environmental proposals, approaching levels more typical of governance-related initiatives.\(^{158}\) Even some mutual funds, including those managed by TIAA-CREF, Charles Schwab and Credit Suisse, are increasing their support for shareholder proposals on climate change.\(^{159}\) In addition, a large number of the social and environmental proposals submitted annually are withdrawn, which generally indicates that management has been willing to adopt some portion of the action requested by the shareholders.\(^{160}\) For example, the fact that over two-thirds of shareholder proposals requesting corporate sustainability reporting are now routinely withdrawn has been seen as confirmation that sustainability reporting is gaining acceptance among mainstream investors, advisors, financial analysts, and managers.\(^{161}\)

\(^{156}\) A prime example is the anti-apartheid divestment campaign surrounding the Sullivan Principles, which was the first major "responsible investment" shareholder-driven movement. It lost momentum and dissolved once apartheid ended. See generally S. PRAKASH SETHI & OLIVER F. WILLIAMS, ECONOMIC IMPERATIVES AND ETHICAL VALUES IN GLOBAL BUSINESS: THE SOUTH AFRICAN EXPERIENCE AND INTERNATIONAL CODES TODAY (2000). Current campaigns targeting investment in Burma and Sudan appear to be following the same issue-centric approach.

\(^{157}\) See 2008 ESG Background Report, supra note 31 (reviewing empirical studies). For example, in recent years, resolutions on human-rights have gained less than five percent support from shareholders. Id.


\(^{159}\) One recent study reviewing the proxy votes of 74 mutual fund families, together representing $3.8 trillion, on shareholder-sponsored climate change resolutions from the 2004 to the 2008 proxy season found that these and other major mutual funds are increasing their support for shareholder proposals on climate change. See www.ceres.org/mutualfunds09.

\(^{160}\) See 2008 ESG Background Report, supra note 31. The number of shareholder proposals urging boards to adopt voluntary corporate sustainability reporting has also risen in recent years. Id. (reporting such proposals have generally attracted over 25 percent shareholder support in recent years).

\(^{161}\) Id. (reporting that over two-thirds of such proposals were withdrawn without a vote in 2008 and 2009). The number of shareholder proposals withdrawn is often read as an indicator of success, since it generally indicates that management has been willing to adopt some portion of the action requested by the shareholders. See, e.g. 2008 ESG Background Report, supra note 31, at 3-4.
In October 2009, the SEC opened the door further to shareholder engagement around ESG issues by adopting a new policy that will allow more shareholder proposals pertaining directly to risk management or requiring a risk analysis to go forward. This will give investors the ability to directly urge firms to focus on risks previously disregarded by the firm but which investors consider material (both governance (“G”) and environmental/social (“E/S”)–related). In addition, the increasing convergence between the identity, goals, and strategies of corporate governance and social activism is likely to make stakeholder issues more prominent as a focus of mainstream investor engagement.

A final development that is contributing to the emergence of ESV are networks for coordinated investor (and NGO) engagement, often around an ESG or social responsibility mission. Coordination amplifies investor voice by facilitating direct information exchange, collaboration, and goal identification, much of which can now be done without falling afoul of the SEC rules for proxy solicitations. This reduces the collective action barriers and free rider problems of shareholder activism.

The PRI itself is a prime example. Coordinated engagement under the PRI extends beyond traditional core corporate governance concerns to direct advocacy of stakeholder interests, including some beyond a strict environmental or social/labor focus. Other institutional investor collaborations include the Carbon Disclosure Project, an international coalition of institutional investors that pushes the largest global corporations to disclose their level of greenhouse gas emissions. Yet another, the Coalition for Environmentally Responsible Economics (CERES), has initiated the global Investor Network on Climate Risk (INCR), bringing together leading institutional investors, investment funds, and environmental public interest organizations. The SEC’s recent guidance on climate change reporting is one example of the potential impact of such collaborations.

163 On the intersections between corporate governance and corporate social responsibility, see generally Amiram Gill, Corporate Governance as Social Responsibility: A Research Agenda, 26 BERKELEY J. INT’L. L. 452 (2008); Ann K. Buchholtz, et al., Corporate Governance and Corporate Social Responsibility, in THE OXFORD HANDBOOK OF CORPORATE SOCIAL RESPONSIBILITY, supra note 99, at 327 (surveying the literature).
164 The rules do not cover communications by investors that do not seek voting authority, and exclude announcements of how an investor intends to vote. See BAUMAN ET AL., supra note 18, at 528-29 (explaining the 1992 reforms to the SEC proxy solicitation rules).
166 Hess, supra note 12, at 221, 328.
167 See http://www.ceres.org/.
coalitions, as it was issued in response to requests from CERES and a number of individual public pension funds, among others.\textsuperscript{168} These global coordination mechanisms can also be viewed as a type of "meta-regulation," leveraging participants' reputational interests to give "teeth" to otherwise voluntary commitments and translate them down the investment chain to financial intermediaries and corporations.\textsuperscript{169}

V. SHAREHOLDER ENLIGHTENMENT AND THE CORPORATE OBJECTIVE FUNCTION

This Article has thus far presented a basic descriptive claim -- that an "enlightened shareholder value" perspective is emerging as an increasingly relevant paradigm for mainstream institutional investors and many U.S. public corporations. It has also examined the basic rationales advanced in support of ESV from the standpoint of institutional investors.

These developments raise a number of fundamental questions that have not been addressed by previous studies. For example, what precisely does enlightened shareholder value mean in the U.S. context, and what in fact might enlightened shareholder value offer as an alternative to shareholder wealth maximization? Or is ESV no more than shareholder wealth maximization in a new "responsible" guise? If ESV in fact suggests an alternative vision of the corporate purpose, what does it mean as a standard for managerial decision-making, and how well does it fit within existing corporate governance rules?

In this Part, I offer an initial response to these questions by clarifying some of the contours of an investor-driven ESV paradigm. I then present normative arguments in favor of an ESV model and consider how ESV addresses some of the questions surrounding shareholder advocacy of stakeholders.

A. ENLIGHTENED SHAREHOLDER VALUE: REVISING THE CORPORATE OBJECTIVE FUNCTION

As described in Part II, the standard shareholder primacy paradigm incorporates: (i) the view that the purpose of the corporation is to maximize shareholder wealth; (ii) the principle that ultimate control of the corporation rests with shareholders; and (iii) the identification of shareholders as the corporate constituency that may exercise monitoring and oversight rights over corporate boards. As we have seen, investor-driven ESV has, as in the U.K., not been directed toward transforming current corporate governance structures to make corporate boards directly accountable to nonshareholders. I will also show below that ESV does not mandate any shift in current corporate governance rules. Instead, ESV is at base a revision of the first element – the corporate objective function –

\textsuperscript{168} See Commission Guidance, supra note 129, at fn 20. For petition signatories, see, e.g. Supplemental Petition, supra note 151.

that is, the standard against which "success" of the corporate enterprise is measured.

In altering only this first dimension, ESV is only a moderate step from the "standard" shareholder primacy paradigm. For reasons discussed below, it fits, perhaps paradoxically, even more comfortably within current corporate law, which as we have seen, is fundamentally director-centric and gives directors and officers broad discretion to take stakeholder interests into account.

1. The Enlightened Shareholder Value Alternative: Distilling Decision Rules

From Part IV, we can readily identify a number of the defining elements of investor-driven ESV. First and foremost, the expressions of investor-driven ESV explored here are motivated by the view that stakeholder issues have an economic impact on firms’ long-term profitability and risk profile and therefore, on the long-term value of investor portfolios. Accordingly, ESV is neither altruistic nor wealth-sacrificing (except in anticipation of long-term gains). Second, while investors are only in some cases directly advancing the interests of stakeholders, for example, through social activism, they are in all these cases at least indirect advocates of stakeholders. Finally, this vision of ESV depends on market pressure from investors and affirms the priority of shareholder value in managerial decision-making. In short, investor-driven ESV shares with the U.K. approach a focus on generating long-term shareholder wealth through investor and management attention to the firm's impact on extended stakeholder constituencies.

a. ESV & Shareholder Wealth Maximization

The conventional understanding of shareholder wealth maximization has always been that corporations should maximize long-term returns to shareholders.\footnote{See, e.g., Hansmaan & Kraakman, supra note 14, at 439 (describing the goal of the corporation, and of corporate law, as "principally striv[ing] to increase long-term shareholder value") (emphasis added).} Since ESV too sets long-term shareholder wealth as the fundamental standard for evaluating corporate success, then perhaps, as some have argued, ESV is no more than "shareholder primacy with an ESG cherry on top".\footnote{Branson, supra note 15.} But is this in fact the case?

Consider first cases where shareholders’ long-term interests are coextensive with stakeholder interests, for example, a decision to build an alternative energy plant that will generate jobs, clean energy, and profits. Similarly, in some sectors, consumer demand for "sustainable" business practices may generally reward companies who deliver with increased profitability and market share. In these cases, the results of an ESV and a shareholder wealth maximization approach might well be the same.

Likewise, if management is considering several courses of action with comparable expected financial benefits, but some options confer a greater net benefit on stakeholders, then an ESV decision rule would preference the latter, essentially encouraging the firm to produce positive externalities. An analysis based on shareholder wealth maximization,
in contrast, would not suggest a basis for selecting between two courses of action that are expected to be equally profitable.

Under the more common scenario, management must make tradeoffs among competing stakeholders. Customer demand for low prices, employee demand for secure employment and competitive compensation, and shareholder demand for market or above-market returns will often be at odds. In a pure profit-maximization approach, the only relatively clear constraints on managerial decision-making are limits explicitly imposed by law. While neither shareholder wealth maximization nor an ESV approach offer a hard and fast rule for quantifying and weighing competing interests and their respective costs and risks, an ESV approach makes ESG and stakeholder-related risks increasingly salient to corporate management as part of the decision calculus.

Under the stakeholder salience model developed by Mitchell, Agle, and Wood, the importance of a stakeholder group to management depends on its relative "salience". Mitchell et al. define "salience" with reference to the stakeholder's power to produce desired outcomes, the legitimacy or appropriateness of their claims, and the urgency of the issue to the stakeholder. If, for example, a firm is weighing whether to adopt new technologies to reduce pollutant emissions or to maintain a competitive edge by continuing to pollute, and if we assume further that the pollution level is within legal limits and there are no reasons beyond environmental benefits to install the new technologies, then a firm might rationally decide to do nothing. If, however, investors are expressing concern about environmental impact or regulatory risks confronting the firm (or are demanding more comprehensive public reporting of such issues), their influence is likely to increase the perceived legitimacy and urgency of environmental and community concerns for the firm. By lending their "power" to stakeholder concerns, investors' voice also increases the likelihood that the firm will respond.

However, it is in the cases where market forces pressure firms away from social responsibility that the contrast between shareholder wealth maximization and ESV is clearest. These are cases where a course of action that maximizes (long-term) profits and boost (short-term) share prices imposes negative externalities on stakeholders, for example, by disregarding human rights or paying minimal heed to environmental impact. If permitted by law, such decisions are fully compatible with a shareholder wealth maximization approach. Under an ESV decision rule, in contrast, the potential impact on stakeholders must be assessed, and if a course of action is profitable only when the costs to stakeholders are ignored, then it should not be taken or some of the costs must be absorbed by the firm. Of course, in some cases, absorbing these costs will likely have

172 Indeed, we might also question the assumption implicit in my first example above that the financial implications of any decision (i.e. ultimately, shareholder value) can be disaggregated from consideration of stakeholder issues so that the relative costs and benefits can be meaningfully compared.


174 The primary mechanism to compel firms to internalize some of the costs in this circumstance would include any obligation to report to shareholders on the firm's impact on shareholders or the threat of
an impact on at least short-term profits. For example, adoption of a greenhouse gas (GHG) mitigation strategy might require significant expenditures with benefits that are realized only in the long term, or a firm may elect not to undertake a potentially profitable investment in a country where it is unable to cost-effectively minimize the risk of human rights violations by corporate actors.

b. ESV Decision Standards

Under an ESV paradigm, then, generating long-term shareholder wealth is the fundamental objective for corporate decision-making, but multiple financial and non-financial stakeholders must be taken into account in the pursuit of financial success. Accordingly, any decision rule must look beyond quarterly earnings or other traditional measures of shareholder value.

Although ESV has yet to be consistently operationalized as a yardstick for management success, there are a number of possible measures of “successful” decision-making that are consistent with this basic ESV decision rule. I consider two here by way of example. Because ESV is investor-driven, these are proposed primarily as a standard for operational decision-making, not for change of control or game-ending corporate decisions where there is no "long-term" investment horizon. In those cases, existing corporate codes and caselaw governing change of control transactions, which again, generally permit consideration of stakeholder interests, would of course apply.\textsuperscript{175}

i. Long-term firm value or "joint output".

Although ESV advocates tend to stress its impact in terms of traditional shareholder value measures, broader measures of firm value are in fact a better fit with an ESV approach, for the reasons set forth above. Measures of firm value reflect the "joint output" of shareholders, employees, lenders, communities, and all other contributors to the corporate enterprise.\textsuperscript{176}

In this regard, ESV is largely consistent with Blair and Stout's team production model of the firm,\textsuperscript{177} the "enlightened stakeholder value" model proposed by economist Michael Jensen,\textsuperscript{178} and other approaches that specify long-term \textit{firm} value maximization as the

\begin{footnotesize}
\begin{enumerate}
\item[175] \textit{Supra} Part III.
\item[176] See Blair & Stout, \textit{supra} note 27, at 310.
\item[177] See Blair & Stout, \textit{id}.
\item[178] See Jensen, \textit{supra} note 51, at 13 (arguing that joint output can only be measured by a comprehensive assessment of firm value that internalizes the costs and returns to all residual financial claimants). Jensen excludes non-financial claimants from the definition of "stakeholders" because, in his view, the interests of these claimants fall within the scope of externalities that are properly dealt with through regulation.
\end{enumerate}
\end{footnotesize}
firm's objective rather than shareholder value. However, an ESV-oriented measure of firm value would potentially incorporate a broader range of stakeholders than financial claimants of the firm, as Jensen and Thomas Smith have proposed, or those with firm-specific investments, as in the Blair and Stout model. Instead, the limiting factor in investor-driven ESV is simply what investors identify as having a potentially material effect on firm performance, which may include measures of costs borne by the environment, local communities, and other non-financial claimants as well. Economists and corporate finance scholars have developed alternative measures of firm value that attempt to provide a more comprehensive picture of the corporation and might therefore offer better metrics to ground an ESV analysis.

ii. Two-tier constrained optimization.

Other possible rules, while not generally advanced by ESV advocates, are also consistent with an ESV approach. One possibility is a two-tier model where decisions that are expected to maximize long-term value to shareholders are first identified and then from those, zero-sum options, that is, decisions that are viable only if high costs to stakeholders are presumed, are excluded. This rule might apply, for example, when weighing the business, political, and reputational risks associated with a planned foreign investment. Again, this approach would not, however, be appropriate in either the Revlon context or where the firm is "in the vicinity of insolvency" and shareholders cease to have long-term interests in the firm's survival. Conceptually, a two-tier rule would essentially embody the principle that the corporation should "do no harm." The challenge with this


180 At the same time, because ESV is driven by investors, financial stakeholders whose interests may overlap less closely with those of shareholders (such as creditors) are not generally represented.

181 See, e.g. Bennett Stewart, EVA Momentum: The One Ratio that Tells the Whole Story, 21 J. Appl. Corp. Fin. 74-86 (Spring 2009) (defining EVA Momentum); Terrance Jalbert; Brian L. Boscaljon; Chenchuramaish Bathala; & Ramesh P. Rao, EVA as a Predictor of Firm Performance, 8 J. Acct. & Fin. Resrch., No. 3, 83-92 (Winter 2000) (reporting EVA as a better measure of firm performance than traditional measures of earnings and cash flow). But see John M. Griffith, The True Value of EVA, 14 J. of Appl. Fin. ___ (Fall/Winter 2004). See also Fisch, supra note 63 (surveying this literature and efforts to quantify costs and gains to stakeholder groups).

182 A rule which requires management to simultaneously maximize the welfare of all stakeholders (i.e. a Pareto optimal result) is not included, since even if it could be achieved, it would not be consistent with the ESV model's emphasis on shareholder value. See, e.g. Bebchuk, Shareholder Power, supra note 28, at 910 (noting that "in theory, one could require management to maximize the overall welfare of all corporate constituencies. Courts, however, would be unable to enforce effectively compliance with such a principle.") Shareholders would likely face similar difficulty. The "balanced scorecard" approach, developed by Kaplan and Norton, might also be used to implement an ESV decision rule. See Robert S. Kaplan & David P. Norton, The Balanced Scorecard – Measures That Drive Performance, Harv. Bus. Rev., Jan.-Feb. 1992, at 71-79. However, as Jensen points out, the Balanced Scorecard likewise does not provide a single objective standard for guiding how to weigh financial, customer, internal business process, learning and growth and other dimensions that together make up the "scorecard." Jensen, supra note 51, at 17-21.

183 See supra text accompanying notes 68-70.
type of standard is that determining the long-term effect of any decision and then resolving inevitable conflicts between stakeholders (and shareholders) affected by the decision is inherently difficult. However, this approach could at least be used as an initial decision tool to exclude those options that are reasonably likely to impose severe or widespread costs on one or more direct stakeholders of the firm.

2. Enlightened Shareholder Value Decision Rules Under Corporate Law

All of these decision rules would pass muster under current Delaware corporate law and under most state corporate statutes. Moreover, investor-driven ESV requires no change in existing corporate governance rules. First, as we have seen, corporate directors and officers are not obligated by law to maximize shareholder wealth outside the narrow circumstances of a change in control under Revlon. Second, with regard to the control rules of corporate governance, ESV does not presuppose either a shareholder-primacy or director-primacy approach and is also consistent with existing director-centric governance rules.

Certainly, in both the U.S. and the U.K., ESV has emerged in a context that gives prominence to shareholder interests. An investor-oriented vision of ESV is also supported by trends toward greater board accountability to shareholders. However, investor activism around ESG risk and other stakeholder issues presumes that directors have the broad discretion afforded by current law to consider stakeholder interests. Moreover, disclosure of ESG risks and implementation of an ESV vision at the firm level depends on the initiative and leadership of corporate boards. As Elhauge observes, directors are well-positioned to bear direct responsibility for the corporations' impact on stakeholders, since they possess inside information on corporate operations and directly bear the shame of public relations "sanctions." Now they also face the prospect of stronger sanctions from investors. Finally, in an era where more voices are weighing in on the direction of the corporation, there is clear value in preserving the board's traditional role as a central decisionmaker with the power of "fiat," as Bainbridge urges. While shareholder empowerment gives shareholders greater space to define corporate accountability, the fundamental balance of current corporate governance rules give corporate boards the necessary freedom to balance competing interests and make decisions for the long-term benefit of the firm as a whole.

ESV also poses no challenge to the current choice of the shareholder as the constituency

184 See generally supra Part III.

185 Advocates of director-centric rather than shareholder-centric control rules note that such theories appear to comport more closely with how companies actually behave, that is, that managers do take into account a range of competing interests and priorities in reaching decisions on behalf of the corporation. See, e.g. Stephen M. Bainbridge, Director Primacy and Shareholder Disempowerment, 119 HARV. L. REV. 1735 (2006); Blair & Stout, supra note 27, at 329.


187 See Bainbridge, Director Primacy, supra note 3.
that enjoys monitoring and enforcement rights under corporate law. Notwithstanding fears of some that proxy access will open the door for "constituency" directors, institutional investors have not pushed for stakeholders to have a direct voice in corporate affairs, for example, by giving employees a seat on the board, nor are they likely to urge that fiduciary duties, voting rights, or other shareholder privileges be extended to other stakeholders even if state corporate codes and corporate boards authorized them to do so. Unless this changes, stakeholders will not gain direct voice in firm governance. The primary impact of ESV, then, is to harness investor power to lend indirect force to stakeholder concerns.

B. NORMATIVE ADVANTAGES OF ESV AS A STATEMENT OF THE CORPORATE OBJECTIVE FUNCTION

Not only does ESV point to decision rules that differ from shareholder wealth maximization, but it also offers normative advantages as a statement of the corporate purpose. Although the implications of enlightened shareholder value are likely far broader than those presented here, the following are potential areas where these contributions are most apparent.

1. Of Law and Markets

Normative arguments in favor of shareholder wealth maximization rest on two primary economic rationales: that maximizing shareholder wealth increases the entire corporate pie, redounding to the benefit of all stakeholders; and that that the corporation's single-minded pursuit of profits generates the greatest welfare gains to society as a whole. ESV decision rules revise these standard arguments in ways that address some

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188 This is in contrast to communitarian visions of corporate governance that would give multiple stakeholders direct voice in corporate affairs. Progressive corporate scholars have called for multi-stakeholder fiduciary duties that would obligate managers to weigh stakeholder and shareholder concerns in corporate decision-making. See generally MITCHELL, PROGRESSIVE CORPORATE LAW (Lawrence E. Mitchell ed., 1995). See supra, notes 77-79 and accompanying text.

189 Any such change could only be accomplished through a charter amendment initiated by the board. Such an amendment would also be contrary to current state corporate code provisions, which limit these rights to shareholders, or in the exceptional case, to creditors. See, e.g. DGCL at §§ 211-221. Note also that the U.K. Companies Act of 2006 does not extend direct monitoring or enforcement rights to stakeholders either. See supra note 87.

190 In brief, the theory states that shareholder primacy compensates shareholders for bearing greater risk than fixed claimants with a priority claim, and thus gives ultimate control to those with the strongest interest in maximizing the surplus and thus the entire economic pie. Employees, creditors, and other stakeholders are generally assumed to be fixed claimants. See Hansmaan & Kraakman, supra note 14, at 449.

191 See EASTERBROOK & FISCHEL, supra note 62, at 38; Jensen, supra note 51, at 16. Other arguments rest on the identification of shareholders as the legal owners of the corporation. Although the shareholder-owner's strong rhetorical appeal has brought it back into circulation in support of shareholder democracy, this view has already been assailed on a number of practical and theoretical grounds. See, e.g. Lynn Stout, Bad and Not-So-Bad Arguments for Shareholder Primacy, 75 S. CAL. L. REV. 1189, 1190 (2002) (citing the shareholder ownership theory as "the worst[] of the standard arguments for shareholder primacy"); Fisch, supra note 63, at 648-50 (summarizing the ownership argument and its limits as a
of the limits of law and of markets better than pure shareholder wealth maximization.

One such limit concerns negative externalities. As Bainbridge explains, if as is typically assumed, nonshareholders have a priority fixed claim on firm assets while shareholders have a residual claim, then shareholder wealth maximization only generates net benefits to nonshareholders in the absence of externalities. However, where the firm takes a course of action that is relatively risky, "[t]he increased return associated with an increase in risk does not benefit nonshareholders because their claim is fixed, whereas the simultaneous increase in the corporation's riskiness makes it less likely that nonshareholder claims will be satisfied." 192 If, on the other hand, as Jensen and others have recognized, shareholders are not in fact the sole residual claimants of the firm – indeed, employees and local communities often are as well – then shareholder economic value alone is not coextensive with firm value. 193 Under either view, the conclusion that shareholder wealth maximization increases firm value, and therefore social value, may not hold true.

ESV offers a response to these challenges. ESV proponents assert that maximizing firm value (or value to stakeholders) maximizes shareholder wealth, not the other way around. 194 As we have seen, such a decision rule is more likely to encourage firms to recognize and internalize risks to stakeholders than pure shareholder wealth maximization. ESV's emphasis on the need to account for broader stakeholder concerns also meshes better with empirical findings that gains to shareholders are often generated simply by wealth transfers from other stakeholders, thus resulting in little or no net gain to the firm. 195 Finally, ESV asserts that even when shareholder and stakeholder interests diverge, the costs which the firm externalizes to multiple stakeholders may reduce long-term shareholder value and increase the level of risk assumed by the firm. Thus, it may not be possible to maximize shareholder economic value when these factors are excluded from the analysis. ESV's emphasis on broader definitions of shareholder value therefore offers useful revisions of some of these standard rationales.

With regard to the argument that profit maximization is best for society as a whole, ESV

justification for shareholder primacy).

192 Bainbridge, Director Primacy, supra note 3, at 585, fn. 182 (but concluding that the externalities argument is overstated).

193 In other words, some stakeholder claims are not fixed but are in fact residual. See supra text accompanying notes 177-180. Jill Fisch observes that if stakeholder interests cannot be assumed to be adequately protected by contract, a point addressed infra, then stakeholders are also residual claimants, and "if nonshareholders can be residual claimants or corporate decisions can transfer value between stakeholders, then maximizing shareholder value is not the equivalent of maximizing firm value.” Fisch, supra note 63, at 659-60 (reviewing empirical support finding these conditions met as a matter of corporate practice).

194 See supra Part IV(B)(2).

195 A number of studies show, for example, that the value to shareholders generated by a takeover is offset by the losses to employees. See, e.g. Andrei Schliefer & Lawrence H. Summers, Breach of Trust in Hostile Takeovers, in FROM CORPORATE TAKEOVERS: CAUSESS AND CONSEQUENCES 33 (Alan J. Auerbach, ed.) (1988).
also implies the inverse of the standard argument: companies that do good for society will do well in the market, a proposition that has some empirical support.\textsuperscript{196} In addition, ESV implies that the public spillover benefits of firm productivity may be offset by costs and risks to stakeholders that are neither adequately addressed under current law nor known to the markets.\textsuperscript{197} In particular, the emphasis of ESV proponents on environmental, social, and even human rights risks highlights the inadequacy of legal and contractual protections for involuntary stakeholders (i.e. employees of foreign suppliers, the environment, and distant tort claimants) and for other stakeholders of global corporations beyond the jurisdictional reach of U.S. law and courts.\textsuperscript{198} Pressure from investors, among others, may help fill these gaps.

2. \textit{The Nature of the Corporate Contract}

A further normative argument in favor of shareholder wealth maximization and other dimensions of shareholder primacy is that it is an implied term of the hypothetical and real contracts between the firm and its various constituencies. Because shareholders lack the legal and contractual protections available to other stakeholders, they would not agree to invest in long-term, capital-intensive projects of the firm if shareholder primacy were not part of the corporate contract (or would do so only at a higher rate of return).\textsuperscript{199}

Without questioning the theoretical utility of a nexus of contracts understanding of the firm, it can at least be said that ESV suggests a revision of the corporate contract argument that is a better fit with emerging realities of global public corporations. That shareholder wealth maximization is an assumed term of the contract is generally justified on grounds that shareholders are relatively powerless to defend their own interests, that nonshareholders are adequately protected by law or contract, and finally, that the rule is the one most likely to maximize firm value and is therefore the rule that the contracting parties would have reached had they explicitly bargained for it.\textsuperscript{200} First, while legal and

\textsuperscript{196} See supra Part IV(B)(2).

\textsuperscript{197} ESV also recognizes, as the standard argument does not, that nonshareholders' interests in increasing firm value may not be coextensive with shareholder interest in profit-maximization and may thus deserve separate consideration. See Chen & Hanson supra note 49, at 47 (noting that "[the claim that increased firm value increases social welfare] assumes that the interests of nonshareholders are aligned with the [profit-maximizing interests] of shareholders."). In this respect, ESV echoes Christopher Stone's well-known observations about the limits of law (and, it should be noted, the limits of markets) in motivating corporate social responsibility. See \textsc{Christopher Stone}, \textit{Where the Law Ends: The Social Control of Corporate Behavior} 88-110 (1975).

\textsuperscript{198} These include foreign communities and workers who cannot be presumed to be protected by law, the democratic process, or even, an implicit contract. Because most corporate law scholarship assumes that corporations operate within a (single) democratic domestic political system that can be relied on to address distributitional and equitable effects generated by the market, the limits of international law in extending such protections globally are rarely considered. For a thorough discussion, see generally Cynthia Williams, \textit{Corporate Social Responsibility in an Era of Economic Globalization}, 35 U.C. \textit{D}avis. \textit{L. Rev.} 705 (2002).

\textsuperscript{199} See, \textit{e.g.} Bainbridge, \textit{Director Primacy}, supra note 3, at 600; See also EASTERBROOK & FISCHEL, supra note 62, at 12 (asserting that shareholders as residual claimants implicitly contract for the promise that the firm will maximize long term returns to shareholders).

\textsuperscript{200} See Chen & Hanson, \textit{supra} note 49, at 52-66 (noting that "scholars have offered a seemingly watertight
contractual protections may be adequate protection for many stakeholders, we have already seen that they do not generally extend to many stakeholders of global corporations. With the rise of powerful institutional investors and lower barriers to shareholder activism, the claim that shareholders are in need of particular protection under corporate law has also lost some of its rhetorical force.\footnote{\ref{fn:201}}

Moreover, it is no longer certain that pure shareholder wealth maximization that excludes stakeholders is the decision standard that all shareholders would inevitably reach with other corporate stakeholders and firms. Indeed, many investors are, through various forms of activism, explicitly negotiating the terms of their continued investment directly with portfolio firms to ensure that the corporation generates solid returns but also gives due consideration to ESG issues.\footnote{\ref{fn:202}} Traditional theories maintain that investors would demand a risk \textit{premium} on their investment, that is, a higher rate of return, if managers were free to "make tradeoffs" between shareholders and stakeholders.\footnote{\ref{fn:203}} However, the behavior of ESV-oriented investors and their allies among SRI investors suggests that, at least for these investors, the traditional assumption does not fit. Rather, these shareholders have concluded that firm-level risks are actually \textit{reduced} when management takes both voluntary and involuntary stakeholders into account and that it is in fact \textit{failure} to make some tradeoffs preferencing stakeholders that might increase long-term risks to shareholders, justifying a risk premium.

3. \textit{Of Means and Ends}

Finally, traditional shareholder wealth maximization assumes that the \textit{ends} of the corporation (i.e. advancing the private, economic interests of shareholders) can be distinguished from the choice of appropriate \textit{means} to achieve that goal, a task which is left to management discretion, constrained, if necessary, by laws passed by duly elected public officials.\footnote{\ref{fn:204}} However, given the reputational risk of "irresponsible" business practices, shareholder economic interests are increasingly directly linked to the economic and even non-economic interests of stakeholders. ESV better recognizes that it is

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\footnote{\ref{fn:201}} The choice of the shareholder as the stakeholder to whom corporate law grants monitoring and enforcement rights may, however, still be justified on grounds that shareholder’s interests are generally speaking most closely aligned with the interests of all of the firm’s stakeholders.

\footnote{\ref{fn:202}} Others more aligned with traditional SRI activism, negotiate through shareholder proposals and the like to achieve outcomes that may in some cases \textit{not} be wealth maximizing to a portfolio investor. Einer Elhauge has lent theoretical support to this observation by showing that such behavior can be justified in some cases on grounds of efficiency as well as ethics. \textit{See generally} Elhauge, \textit{supra} note 186.

\footnote{\ref{fn:203}} \textit{See} \textit{generally} Friedman, \textit{supra} note 56.
perhaps no longer possible to make useful distinctions between the private and public roles of the firm.

Although views clearly differ on the normative benefits of maintaining the means/ends or public/private distinction, the range of issues raised through various forms of shareholder activism shows clearly that many shareholders are in fact as concerned about the means by which shareholder value is achieved as they are in returns on investment. ESV thus also better comports with the observed reality that shareholders increasingly expect corporations to be directly accountable for how their money is spent.

4. Stakeholder Representation

Although this Article demonstrates the compatibility of many stakeholder interests with the economic interests of shareholders and the corporations they invest in, a normative objection might well be raised about whether investor advocacy of stakeholder interests is in fact good for stakeholders and if so, whether investors are in fact better positioned than regulatory authorities, corporate boards, and stakeholders themselves, to advance and protect stakeholder interests.

While there is not space here to provide a complete response to this question, a few observations are in order. First, it is doubtful that indirect representation by institutional shareholders fully and accurately reflects the true interests of stakeholders. Second, because any voluntary ESV approach inevitably gives institutional investors and corporate directors and officers the power to define, select, and prioritize the stakeholder interests they will advance, investors and boards are inevitably framing how stakeholder interests are perceived by corporate managers and which will be deemed "material". Particularly for financial stakeholders, such as creditors and to a lesser extent employees, investor voice will therefore generally be an imperfect substitute for direct protections that may be provided through legislation or by contract between the stakeholders and the firm. Nonetheless, shareholders can and do advance certain stakeholder interests, and investor advocacy can amplify stakeholder voice where these mechanisms are weak.

This is particularly so in the case of "involuntary" stakeholders, such as the environment, foreign workers, and victims of human rights violations, for whom regulatory and contractual mechanisms may not be available or enforceable. Even if domestic, foreign, and international regulation is strengthened, "one-size-fits-all" approaches may not be optimal. For these stakeholders, investor activism that motivates firms to "self-regulate" by identifying and reducing risks and harms to these constituencies can provide an important supplement to market pressure from NGOs and consumers and reinforce existing contractual and regulatory protections.

C. ESV & THE “PROBLEM” OF STAKEHOLDERS: RESPONDING TO

Shareholder proposals seeking to set limits on executive compensation, and social proposals urging, for example, disinvestment from Sudan, illustrate this point equally.

On corporate self-regulation generally, see generally PARKER, supra note 169.
EFFICIENCY-BASED CONCERNS

Since Berle and Dodd began their famous debate over the nature and purpose of the corporation, any significant movement within academic and popular discourse in the direction of shareholder primacy has caused an equal and opposite movement away from the stakeholder model and its emphasis on corporate obligations to broader constituencies.\textsuperscript{207} Not surprisingly, the ebb and flow of the corporate social responsibility movement itself can be charted along much the same historical trajectory.\textsuperscript{208} Over the past decade, however, the lines between these categories have begun to blur.\textsuperscript{209} ESV promises to dissolve some of the remaining boundaries, paving the way toward more integrated conceptualizations of the corporation and its purpose. Where then does enlightened shareholder value leave us in considering the "problem" of stakeholders that is behind much of the debates over corporate governance reform?

1. "Too Little" Attention to Stakeholders

The first area of concern was that shareholder power might cause management to give too little attention to stakeholders. This Article suggests that such assumptions are no longer well-founded. As Part IV of this Article highlights, "enlightened shareholder value" is in fact already gaining traction among influential mainstream institutional investors and might ultimately motivate leading public corporations in a pro-stakeholder direction. These trends support findings from Lisa Fairfax's survey of investor social activism, which provided ample evidence that many institutional investors can and do advocate for stakeholders.\textsuperscript{210} More comprehensive reporting and disclosure of ESG and other nonfinancial factors may also facilitate broader public oversight of corporate activities that impact stakeholders.

2. "Too Much" Attention to Stakeholders

Expanded shareholder influence is however problematic for those concerned about the potentially efficiency-reducing effects of shareholder representation of stakeholder interests. The ESV model responds in part to these concerns by showing that accounting for stakeholders in investment and ultimately managerial decision-making can generate long-term shareholder wealth. Thus, ESV is actually grounded on efficiency-based rationales at both the investor and the firm levels and has the potential to make headway in the mainstream investment and business communities precisely for that reason.

Still, it might be argued that ESV decision rules, like other stakeholder-oriented decision rules, are nonetheless efficiency-reducing because they give "too much" attention to stakeholders. Essentially, the arguments are that stakeholder-oriented rules: (i) lack the

\textsuperscript{207} See generally Chen & Hanson, supra note 49 (tracing the history and origins of the debate).

\textsuperscript{208} See Branson, supra note 15.

\textsuperscript{209} See, e.g. Stout, supra note 74 (identifying some of these trends).

\textsuperscript{210} See generally Fairfax, Shareholder Democracy, supra note 17.
practical simplicity of a single maximand, exacerbating agency problems (the "two masters" problem); and (ii) directly or indirectly advance “private”, political, or social interests that distract from the mission of the firm. These important criticisms have been reinvigorated in the course of the shareholder empowerment debate, and are ones to which ESV offers a more satisfying response than pure stakeholder models.211

a. A Response to the "Two Masters" Problem

The strongest argument for the shareholder wealth maximization norm is that it keeps corporate managers accountable to shareholders by setting a single clear standard – maximizing shareholder wealth, as reflected in the share price. Conversely, one of the strongest criticisms of pro-stakeholder theories is that they leave managers without a standard for choosing among competing stakeholder interests. This multiplicity of interests provides a cover for management self-interest, which is the essence of the "two masters" problem.212 In the words of Easterbrook and Fischel, "a manager told to serve two masters (a little for the equity holders, a little for the community) has been freed of both and is answerable to neither. Faced with a demand from either group, the manager can appeal to the interests of the other. Agency costs rise and social wealth falls."213

ESV, like shareholder wealth maximization, overcomes these obstacles by placing long-term shareholder value as the single objective standard.214 However, ESV investors expect management decision-making to satisfy an additional criterion – that is, to be justified with reference to stakeholders, whether by avoiding harms to stakeholders that pose a risk of material future losses to the firm, or by seeking opportunities to generate wealth in a way that also benefits stakeholders.215 Such a decision rule raises practical difficulties, but no more than in the current context of corporate decision-making, where managers routinely confront competing shareholder and stakeholder constituencies.

b. A Response to the Problem of Private Interests

The question of "private" or "special" interests poses more difficulty for an enlightened shareholder paradigm. Here, the basic concern is that the most activist shareholders,

211 Stakeholder-oriented theories generally maintain that the interests of shareholders and other stakeholders should be weighed equally in managerial decision-making or that other stakeholder interests, such as those of employees, should take precedence. For a survey of stakeholder theories, see Thomas Donaldson & Lee E. Preston, The Stakeholder Theory of the Corporation: Concepts, Evidence, and Implications, 20 ACAD. MGMT. REV. 65 (1995).

212 Id. See also Bebchuk, Shareholder Power, supra note 28, at 910-11.

213 See EASTERBROOK & FISCHEL, supra note 62, at 38.

214 See Bainbridge, Director Primacy, supra note 3, at 600 (explaining that under shareholder wealth maximization, “if the board considers the interests of nonshareholder constituencies when making decisions, it does so only because shareholder wealth will be maximized in the long run.”). But see Blair & Stout, supra note 27, at 304 (disputing this view based on evidence from the takeover context).

215 This is an advantage of Jensen's "enlightened stakeholder model" as well. See Jensen, supra note 51.
large public pension funds, union funds, and hedge funds, might use their power to advance their own private, political, or constituency interests, transferring value from other shareholders or stakeholders to select shareholders. Shareholders might also align with management against stakeholders for reasons not shared by the shareholder class. Both concerns resonate strongly with critics of greater shareholder power.

At the outset, we should dispel the false notion that these problems do not arise under shareholder wealth maximization. Since shareholder voice is now a part of the landscape in which public corporations must operate, then the artificial uni-dimensional wealth maximizing shareholder has already been replaced by a heterogeneous, dynamic contingent of mostly fiduciary shareholders, who together with their beneficiaries, have real and diverse interests that include, but may extend beyond wealth maximization. Therefore, the assumption that all shareholders are long-term wealth maximizers is now less theoretically and practically useful. While courts may continue to rely on this fiction for its simplicity, shareholder voice clearly means that what real investors want, in all its variety, matters both to management and to other shareholders who likely will have quite different views.

The ESV approach does not itself resolve all of these challenges. It cautions, however, that shareholder activism that aligns with stakeholders or that constrains the means of generating profits should not be suspect as per se "impermissible." Specifically, the fact that public pensions, labor union funds, and other activist institutional investors owe duties to diverse constituencies with both economic and non-economic goals does not necessarily present a threat to long-term value creation. For example, we have seen that in addition to informational benefits, ESV might encourage companies to pursue value-increasing environmental and social goals that they might otherwise neglect, or deter activities that create a high risk of harm to other stakeholders that may ultimately be value-decreasing for the firm. Therefore, discouraging institutional investor voice on "public" or "stakeholder" issues because it may be a cover for self-interest, collusion, or managerial protectionism runs the risk of throwing the baby out with the bathwater, resulting in lost benefits to stakeholders and shareholders as well. Instead, it is possible to leave space for ESV by narrowing the class of "private" interests that pose concern.

216 See, e.g. Anabtawi and Stout, supra note 17, at 1285-86 (citing CalPERS proxy campaign to oust Safeway's president and pressure Safeway in labor negotiations).

217 See supra note 47.

218 The most comprehensive treatment of the fictional wealth-maximizing shareholder is Daniel J.H. Greenwood's Fictional Shareholders: For Whom Are Corporate Managers Trustees, Revisited, 69 S. CAL. L. REV. 1021 (1996). However, the heterogeneity of even the economic interests of shareholders challenges the traditional view that a single maximand can be achieved by relying on trends in share prices. See Anabtawi, supra note 47. The utility of shareholder wealth, generally measured by current share price, as a single maximand rests on an assumption of efficient capital markets in which current share prices reflect the present value of all available (or at least all public) information about the company's present and future operations. However, modern corporate finance theories have challenged the descriptive accuracy of the stronger forms of the efficient capital markets hypothesis (the ECMH). See supra note 116.

219 Cases where institutional investor advocacy of stakeholder interests may be wealth-decreasing do not fall within an ESV paradigm.
There are essentially two forms of "impermissible" (i.e. value-decreasing) private interests: *self-interest* (rent-seeking, opportunism, and "hold-up") and *collusion with management* ("gang-up"). Activism conducted for these purposes is impermissible not because it might advance the interests of labor unions or the agenda of a prominent environmental NGO, but because it confers a unique *economic* benefit on the activist that is not shared by the shareholder class. Because ESV is focused on wealth-enhancing corporate reform and advancing broader definitions of corporate accountability, ESV-oriented investors should generally be opposed to misuse of activist power for solely "private" or "special interest" purposes.

A full analysis of potential solutions is beyond the scope of this Article. However, a number of possibilities have already been proposed that would mitigate these risks and allow firms (and markets) to reap the benefits of investor activism. First, the majority voting rule already offers some protection against impermissible activism. Although majority voting will not necessarily prevent all abuses of shareholder power, it clearly does deter some degree of self-interested activism. The deterrent effect is arguably stronger when investors are engaging in direct social activism, since social proposals historically have attracted less support from non-proponent investor groups. For example, one recent study of “say-on-pay” shareholder proposals found that labor-union-initiated proposals targeting firms where CEO pay was not excessive generally received lower support from other shareholders.

Other proposals that offer strong potential deterrents for impermissible activism would extend controlling shareholder fiduciary duties to all activist shareholders, or strengthen the transparency and accountability of fiduciary institutions, such as pension funds, to fund beneficiaries and other stakeholders. Such measures might include expanding beneficiary roles in pension fund governance and requiring institutional investors to publicly disclose how they are exercising activism.

Further answers also lie in where the boundaries for shareholder activism are set in the

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220 Anabtawi and Stout’s arguments in favor of fiduciary duties for activist shareholders make the same distinction. Anabtawi & Stout, *supra* note 17, at 1284.

221 *See* Anabtawi, *supra* note 47.

222 *See* Fairfax, *Shareholder Democracy, supra* note 17, at 58-59.


224 *See* Anabtawi and Stout, *supra* note 17.

225 *See* DAVIS, *supra* note 101, at 140-73 (considering increased fiduciary disclosure requirements, "pass-through" proxy voting, beneficiary nomination of pension trustees, and other measures to increase monitoring by beneficiaries). *See also* Keith T. Johnson & Frank Jan de Graaf, *Modernizing Pension Fund Legal Standards for the Twenty-First Century,* ROTMAN INTL J. PENSION MGMT. (Spring 2009).
course of ongoing corporate governance reforms. Limits to proxy access, for example, such as ownership stake requirements and rules requiring activists to “disclose or explain” their own potential conflicts of interest might alleviate some of the objections to investor-driven ESV raised earlier.\textsuperscript{226} The need to address shareholder conflicts of interest also points ultimately to the value of maintaining the fundamental director-oriented control rules, such as a strong business judgment rule, as an important safeguard against impermissible uses of shareholder power, even as investors serve as a check on managerial self-interest. In light of these rules and the availability of targeted solutions to the types of activism that pose concern, the fact that shareholders may use their power to advance the interests of stakeholders should not be viewed as inherently problematic from an efficiency standpoint.

VI. CONCLUSION

The global financial crisis has produced profound skepticism about the power of markets to right all wrongs and has renewed interest in the tools of public regulation. But, as Mark Roe observed over a decade ago, there is reason to doubt that legal change alone will lead to structural or institutional change in the actors and relationships that are entrenched in the economy.\textsuperscript{227} What is interesting about the present moment is the confluence of market and regulatory changes that has given investors greater influence in corporate governance. Equally interesting is that leading institutional investors are beginning to use their power to advance stakeholder-oriented approaches to accountability, risk management, and governance that challenge conventional understandings of corporate accountability.

As we have seen, enlightened shareholder value represents just such an alternative vision and one that offers theoretical and normative advantages over the shareholder wealth maximization norm. It also offers principled responses to many of the concerns surrounding shareholder empowerment and rising shareholder activism. Recent regulatory initiatives at the state and federal levels, such as efforts to improve disclosure of corporate risk management policies, clarify standards for corporate non-financial reporting, make institutional investor activism more transparent to fund beneficiaries, and discourage short-termism across the financial services industry, may well move corporations more quickly in this direction.

Whether these or other proposals lend support or not, investor-driven "enlightened shareholder value" shows that the practice of corporate governance has already moved beyond the shareholder-stakeholder divide. The challenge for future corporate governance reform and scholarship is now how best to optimize the contributions of stakeholders, shareholders, and corporate boards to firm success in light of this reality. How this balance will ultimately be set for public corporations remains to be seen. But if the ascendancy of shareholder primacy itself is any guide, emerging market-driven

\textsuperscript{226} See Release Nos. 33-9086; 34-61161 and related comments, supra note 29. See also Bebchuk, \textit{Shareholder Power}, supra note 28, at 908-913 (responding to this challenge).

\textsuperscript{227} \textit{Roe}, supra note 16, at 275.
norms like ESV might ultimately shape the "rules of the game" for corporations as much or more than positive legal rules.