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Beyond Unprecedented: The Post-Pandemic Economy
Episode 3: "The Rise—and Results—of Shareholder Activism"

[00:00:02] **Anne E. Robinson '94:** There's been a shift in the expectation of leaders in corporate America. They are expected to share a set of values in addition to their business plan. The risk profile to your investment returns naturally starts to include some of these other issues.

[00:00:21] **[Music and media clips of journalists saying "unprecedented"]:** The coronavirus pandemic has tanked the global economy with unprecedented speed. The steepness of the decline here is unprecedented. This is a crisis that is unprecedented. It is unprecedented, and we just don't know.

[00:00:35] **Eric Talley:** This is *Beyond Unprecedented: The Post-Pandemic Economy* from Columbia Law School and the Ira M. Millstein Center for Global Markets and Corporate Ownership. I'm Eric Talley, Sulzbacher Professor at Columbia Law School and co-director of the Millstein Center.

[00:00:50] **Kate Waldock:** And I'm Kate Waldock, a research fellow at the Millstein Center and a 2L at Columbia Law.

[00:01:00] **Talley:** The economic disruption and personal loss caused by COVID-19 during the last two years has often seemed all consuming. Yet the coronavirus pandemic has unfolded alongside two other crises confronting the nation and the world: climate change and racial justice. Today on *Beyond Unprecedented*, we look at how these two critical issues are landing squarely on the boardroom table.

[00:01:23] **Waldock:** Activist investors seeking to gain control of shares in order to influence corporate policies have seized on ESG, which is shorthand for environmental, social, and governance policies. These investors have accelerated their push during the pandemic, and they want corporations to assess climate risk and sustainability and do something to improve it. But how do shareholder activists get the buy-in of the institutional investors they need to force change? And how can those big investors measure the success of an ESG campaign, whether it's pushing for action on climate change or diversity? We're going to explore these issues later today with Anne Robinson, general counsel at Vanguard and a Columbia Law graduate. But first, Eric, we're both teachers, instructors, you're a professor. Have you found it difficult given everything that's been changing in the past couple years to hold on to the same concepts of corporate governance and corporate finance that we've always been teaching?

[00:02:20] **Talley:** I think so, Kate. It's been, actually, quite challenging to teach a class like corporate finance in that period of time because the standard lesson from that is, well, be a passive investor, diversify your investments, and hang out and try to earn a return off of that. But it's more complicated now than it used to be. The role of policy decisions inside individual companies has become much more center stage for all types of investors. And it may not always be the case that you want every single investor to be a passive investor—that sometimes getting involved in the governance of a company is an important thing for changing its trajectory. And by the same token, the types of things that investors seem to want now isn't just like the standard, well, help me generate a return with minimal risk. Investing is now, in some ways, a form of expression or a form of consumption or a form of expressive consumption. I don't know if you get the same feeling.

[00:03:21] **Waldock:** [Laughter] Absolutely. The way that I used to teach it was that there's two types of institutional investors: There's hedge funds, often activists; they're forcing returns and they're only interested in efficiencies, so maybe they'll go in and make some changes on the board to make the operations of the company more efficient—that's all they're interested in. And then on the other hand, you have large asset managers—like BlackRock, Vanguard—who are more passive and they're just interested in holding a broad index and not actually forcing changes very actively. But then I'll have an enterprising student who knows about what's going on today, and they'll be like, wait, but what about the recent Exxon issue?

[00:04:03] **Talley:** The Exxon issue is a great example. A tiny hedge fund ended up taking on the behemoth Exxon in a proxy contest for positions on the Exxon board. This hedge fund, called Engine No. 1, was largely motivated by some environmental concerns that dovetailed with some risk issues and ended up being successful. And in some ways, this was a shot across the bow of anyone who thinks about corporate governance, corporate law, corporate finance, that this broader set of issues is now elbowing itself up to have a real seat at the table of how companies are governed, the decisions that they make, and the way that they structure themselves.

[00:04:46] **Waldock:** It seems like the standard model for activism and changes in the boardroom has sort of been turned on its head in the past few years, and I can't think of a better person to talk to about this than Anne Robinson from Vanguard.

[00:05:17] **Talley:** Anne is general counsel of the Vanguard Group and secretary of the Vanguard Funds. She has more than 20 years of legal experience in the financial services industry, where she has counseled senior executives on a wide range of legal, regulatory, and business issues. She has a J.D. from Columbia Law School. Welcome, Anne!

[00:05:36] **Robinson:** Thank you. It's great to be here.

[00:05:38] **Waldock:** I'd like to start with a pretty broad question, which is how has the pandemic—with everything that happened from the racial reckoning to the impacts of climate change that we've already seen—how has that shaped or altered the corporate mission?

[00:05:50] **Robinson:** We have seen a number of unexpected and unprecedented events that have challenged our conventional thinking about the role of different leaders in our society and in our economy. And in light of the absence, frankly, of a clear leadership platform in Washington and in other countries at a global level, there's been a shift in the expectation of leaders in corporate America. And so CEOs have been called upon to step into that void. They are now faced with having to represent their employees, their customers, their investors. They are expected to share a set of corporate values in addition to their business plan. And so I think it has really shifted the expectations of corporate leadership. And it has, interestingly, I think, also created an invitation for confusion about what the true role of companies are in our society and in our economy versus some of the other stakeholders who are perhaps not doing all of the things that they should be doing to represent their area of responsibility.

[00:07:02] **Talley:** The story of activist shareholders and activist investors is one that's been undergoing a pretty rapid change. When I started teaching corporations a couple decades ago, shareholder activists were largely the shareholder return police. Every once in a while, there was a social activist who would maybe raise a shareholder proposal, but they would hardly ever win, and they tended to have a fairly small part in the play. The type of shareholder activists that we're seeing now has changed a lot. A lot of activism is taking on a much greater public-good aspect. Can you just give me a sense of how you've seen this unfold over the last few years?

[00:07:42] **Robinson:** Sure. Let me just start by taking a step back and saying the role of asset managers, and, particularly, as I represent Vanguard, is to steward the assets of our investors. So people give us their money, we take very seriously that our responsibility is to keep it safe and make it grow. When we think about that, we think about all of the different things that could frustrate a company's ability to deliver long-term and sustainable value to their investors. And so we talk to companies to better understand their process for identifying and managing those risks. When there are activists of whatever ilk, we also talk to them to try to understand if there is a particular risk that they see that could have a great impact on corporate performance. But we are not in the business of standing over the shoulders of companies and telling them how to run their company. You can confuse an outcome like Exxon, and say that was an activist initiative, or that was a climate risk proposal. And really, it was corporate governance 101. A lot of the issues there were about a sense of accountability by the board, by the company, to its investors who wanted to ensure that there was the right composition of talent on the board to oversee that company through its risks and opportunities. There were questions about capital allocation. And their challenges could have been in any area; they just happened to be an oil and gas company with some climate-related adjacencies. But the issues in that proxy contest were governance issues. And so I think it is good that we are starting to step into conversations about governance and accountability. But I think it can also be misconstrued and give activists perhaps more attention than otherwise they would when you start to conflate the activist agenda with the institutional investor responsibility to steward their clients' investments.

[00:09:50] **Waldock:** Could you give us a little bit more background on the Exxon case?

[00:09:53] **Robinson:** We've talked about the engagement that we've had with Exxon about our expectations that they would have a wider range of backgrounds and skills on their board. We have encouraged them to engage with their investors, and we saw them improve that engagement over time, and we expect to continue to be able to have that conversation with them. In our minds, it was a governance vote, and it was not a referendum on their climate strategy. In fact, that's one of the areas where we were supportive in our voting.

[00:10:26] **Waldock:** Do you think that climate change poses a systemic risk? And if so, how are we supposed to measure it?

[00:10:31] **Robinson:** Yes, we believe that it is an investment risk, it's a material risk. How it shows up in different companies is unique to each company, but we do believe that climate risk is a significant risk and if unmanaged can frustrate long-term value creation. And so it's a topic that we engage with our portfolio companies about to better understand the board's assessment of that risk and how they're overseeing strategy to mitigate that risk.

[00:10:57] **Talley:** Anne, can I push you a little bit further on how an asset manager thinks about its customer base? There are also fund managers that are now starting to say, OK, we're going to put together an ESG-oriented fund. It might still be an index, but it's going to be a fund that doesn't have dirty energy or doesn't have some other group that we think that a particular group of investors wants to avoid. I would guess that the clients investing in that fund are a slightly different animal, may have slightly different preferences. Does it become incumbent on asset managers like Vanguard to think about tailoring their own attitudes toward corporate governance depending on which type of fund they're actually representing in which capacity?

[00:11:41] **Robinson:** One of the things we have to do is have a compelling set of products that meet the investment needs of our 30 million investors. Right now we have 18 ESG products. So when we think about the entire lineup of our portfolio, we do have ESG assessments in our investment processes, and that's one of the reasons why disclosures around ESG are so important. Most of our products are funds that track a benchmark. Whether they are considered ESG or not, we're going to hold securities for as long as they're in the underlying benchmark. So we sometimes call ourselves the sort of forever investor. What that results in is a need to be very thoughtful about how we try to influence portfolio companies to ensure that for as long as they are actually in the underlying index, they are delivering value in that index. So that's where the conversations about governance come in. We do believe that good governance drives value creation. We do, when we don't see progress, and we don't see satisfactory behavior from a governance perspective, vote accordingly. But we don't look to punish companies or require companies to behave in a particular area. It's that we're not satisfied with their governance processes. And when we are not satisfied with that, we do use the vote to indicate that change is probably in order.

[00:13:03] **Talley:** Obviously, federal regulators play a fairly significant role in this space, not just at the asset manager level but also at the public company level. And the SEC, after having sort of formally waffled about this for over a decade, is now starting to get busy trying to figure out what, if anything, it's going to do on the regulatory front when it comes to ESG matters. What's your take? What's Vanguard's take on where the SEC can both helpfully intervene and least helpfully intervene in this area?

[00:13:37] **Robinson:** So much of the value that we can add requires information. And so the quality of disclosure is really critical for the decisions that investors need to make. So understanding and having a common naming convention and nomenclature and way of evaluating the adequacy of disclosures, the categories of disclosures, is so important. How do I know as an investor that this is actually an ESG product? I think that the SEC really should think about imposing a set of common criteria for when you disclose, who discloses, and what you disclose. I think that would be incredibly helpful to have just that consistency and greater clarity.

[00:14:26] **Waldock:** We've been focusing, so far, on the E part, the environment, as well as the G part, governance. But I'd like to talk about the S part, the social element of what's been going on for the past couple of years. I think that that gets underplayed to some extent, especially when it comes to financial markets. So I wanted to ask you, what's Vanguard's position on engagement related to diversity, equity, and inclusion [DEI] initiatives and the broader role of institutional investors in this space?

[00:14:53] **Robinson:** We believe that diversity, equity, and inclusion risks are equally as disruptive as climate-related risks, and I think we've really tried to push for greater understanding and disclosure about how diversity, equity, and inclusion risks can frustrate that long-term value creation. What I will say is that if you think about the life cycle of climate risk, it started out that the science was less settled and agreed upon, the requirements and the frameworks for how you think about who discloses, what to disclose, and when to disclose were less settled. There are a number of organizations that have come together and said we need better information, and this is the way to start to provide it. I think DEI is a little bit more nascent in that stage. I think we all understand from the studies that say that diversity has an impact in terms of the performance of boards. I think we've seen the studies that say that if you have a culture that is not inclusive, you're not getting the best of your employees. I think we've seen that hostile work environments can create very real risks in the form of brand evaluation, litigation for discrimination, really embarrassing situations for a company that frustrate consumer loyalty. So I think there's a lot of insight and evidence that this is also a pretty significant risk in the overall portfolio of companies. But I don't think that it is as mature as climate risk in terms of saying, is there a particular industry that is more likely impacted by not having good DEI programs? Is there a particular area demographically—if you're reliant on clients in particular areas—is there some other way of really zeroing in on how we should be thinking about the risk that not having good DEI practices, how that risk shows up in a particular portfolio company's performance. And so what in large part we have done is two things: We have said the best way to figure that out is to have a board that brings diverse thinking to the boardroom, and so we've called for greater diversity at the board level. We have, when asking and talking to portfolio companies about their talent strategy and their workforce strategy, said there needs to be greater disclosure about diversity from a representation standpoint across your workforce but also policies and culture from an equity and inclusion standpoint in your workforce because your workforce is a critical component to your ability to generate revenues and deliver value to your investors.

[00:17:43] **Talley:** In recent years, we have also seen some regulatory and statutory movement in this area. Nasdaq recently had approved its regulations that would essentially have a disclosure obligation on diversity at the board level. California has also passed regulations that would apply to public companies about diversity representation, both of women and underrepresented groups at the board level. There are activists that are shareholder activists that are also pressing companies to do racial equity audit. Can you give us a sense of, first, what are they, and what's your take on that development?

[00:18:21] **Robinson:** It's a really interesting one. I think we first started to see them in the last couple of years, and my sense is that they will not go away, they will refine their approach. And so what they are proposals essentially requesting that a third party, an independent party conduct an audit related to racial equity, racial justice, civil rights, sort of social platform issues. So far, the ones that we've seen are fairly broadly written, and they include just about any aspect of the company's policies and processes, business practices that could have an impact on communities of color and other underrepresented communities. The arguments around how those equity audits relate to material or even a specific risk is more attenuated than some of the other proposals that are in areas that are a little bit more mature. Some of the proponents of these equity audits, part of what they are asserting is that they question the independence and credibility of the board and management, and so that the independence of the audit is really what they're looking for. And I think there are a couple of things about that that are challenging. First and foremost, our governance construct says that a board should be independent, a board should be competent, and a competent and independent board should provide oversight over management in the delivery of the business plan, the assessment of risks, the assessment of strategy, and that if you have an independent and a competent and highly engaged board, there's just a higher hurdle for less settled bodies of risk to say I need another independent body to come in and assess it. The other thing is, like I started out saying, the clarity around the risks that are the target of many of the audits and their impact on performance, it's just less mature, and so it becomes a little harder to support. I think that as investors start to refine the framework to evaluate how DEI risk shows up in portfolio companies, the sophistication of some of the shareholder proposals that we're seeing will shift and mature a little bit as well.

[00:20:39] **Talley:** I guess there's also a dimension to this that involves those third-party auditors or aspiring third-party auditors. How do you evaluate this industry as it grows up?

[00:20:53] **Robinson:** I think that there is and could be a very constructive role for third parties to play, but I think they're ahead of themselves if they start with the audit. You start with the framework, you start with the baseline, what is the risk and how does it relate to financial performance? And how do I think about what a good program looks like against which to audit a company?

[00:21:15] **Talley:** And I guess there are a couple of examples of companies that have pushed in this direction. Are there models out there that are models that come from a company that might have some traction elsewhere?

[00:21:27] **Robinson:** For the ones that are already out there, I look at them as being in two buckets. The third-party audits that we're seeing successful, some of them are at firms that have had issues. So there's been litigation, or there have been complaints. There's already been an acknowledged identification of a material risk. And so when you know that there's a problem and the risk has already materialized, you're not necessarily auditing against a visionary statement, you're auditing against managing the existing risk that you've identified. If you've been sued, it's a part of the remedy. Then the others that are from companies that are being very proactive and going out and contracting for a third-party audit on their own, the one thing that is really important to note about them is that they are carefully crafted to audit against a benchmark. So it isn't meant to indict the independence of the board or anyone else, it is to say we'd just like a third-party assessment of how we're doing against this program that we've put in place. You know, the most important thing, which we've called for for years, is just disclosure. So tell us about your policies, your programs, tell us about it. And then that leads to the ability to assess, is it robust? Is it thoughtful? Do you even have them? They are the baseline criteria by which you want to start the process of shaping a framework to evaluate both the materiality and its potential impact on financial performance. But you really do have to have enhanced disclosures so that you can just take a look at what's happening before you decide whether it's good or bad.

[00:23:12] **Waldock:** One of the broader themes that's emerged for me from this episode is that because of certain voids in the policy sphere, issues like climate change and diversity and inclusion, have really, the responsibility for those have really been thrust on asset managers in a way that was maybe too much. I mean, the balance between policy and asset management maybe shifted too much in the direction of the financial markets having to be accountable for these issues. So what would you say to investors who have so far been voting with their dollars? How can we force policymakers to take back some of that responsibility and be more accountable?

[00:23:56] **Robinson:** Yeah, absolutely. I think it's a wonderful point. So first, we do believe that asset managers have a role to play, so we're not stepping back from our role. We do think that there is an important role that asset managers play in helping companies in the process of delivering long-term value for their investors understand their risk profile, and the risk profile to your investment returns naturally starts to include some of these other issues that policymakers should play a bigger role in. But we don't even have the platform to solve the problem. If every single asset manager did just about everything they could within the confines of the rules and regulations that apply to us and limit the things that we can do, it wouldn't be enough, and so everyone has a role to play. I think depoliticizing some of the debate is helpful. Activating investors to exercise their influence with more than just their dollars—I think they become a greater voice and a greater source to drive accountability among policymakers—is a terrific thing that could happen. But it's also not just the policymakers, it's the consumers themselves, and so everybody has to do their part, and investors who vote with their dollars and don't behave as a consumer in a way that's consistent with their stated values, they've also got to take a look at that.

[00:25:23] **Talley:** How is it going to evolve over the next decade?

[00:25:26] **Robinson:** What I would love to see is a real common fluency and understanding around the issues. More consistent disclosure and strategic engagement. I'd like to see it with less friction, the idea that we are all marching towards managing the risk that climate change imposes on both investment portfolios and society. There is a lot there that's actually not as at odds as people make it seem. And so I'd like for, again, the participation of all stakeholders to be mature enough so that if I'm doing what I'm supposed to do, policymakers are doing what they're supposed to do, consumers are doing what they're all supposed to do, it becomes a less tense and friction-based relationship, and we're all operating within our areas of responsibility towards a common goal. And that I'd like to see by 10 years from now, we all ought to have a common language, a common set of priorities, and a consistent understanding of the respective roles that we all play.

[00:26:39] **Waldock:** Anne, thank you so much for joining us on the show.

[00:26:42] **Robinson:** Thank you for having me.

[00:26:44] **Waldock:** Our guest today was Anne Robinson. Join us next time for another episode of *Beyond Unprecedented* and make sure to follow us on Apple, Spotify, or wherever you get your podcasts.

[00:26:56] **Talley:** *Beyond Unprecedented* is brought to you by Columbia Law School and the Ira M. Millstein Center for Global Markets and Corporate Ownership. This podcast is produced by the Office of Communications, Marketing, and Public Affairs at Columbia Law School. Our executive producer is Michael Patullo. Julie Godsoe, Nancy Goldfarb, and Cary Midland are producers. Editing and engineering by Jake Rosati. Writing by Martha Moore. Production coordination by Zoe Attridge. Special thanks to Erica Mitnick Klein and Molly Calkins at the Millstein Center. If you like what you hear, please leave us a review on your podcast platform. The more reviews we have, the more people will listen. If you're interested in learning more about law, the economy, and society, visit us at law.columbia.edu or follow us on Facebook, Twitter, and Instagram. Thanks so much for listening.