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The O.G.: Unmasking Why Governance is the Most Important Component of ESG

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THE O.G.: UNMASKING WHY GOVERNANCE IS THE *MOST* IMPORTANT COMPONENT OF ESG

LISA M. FAIRFAX*

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* Presidential Professor, University of Pennsylvania (Carey) Law School.

Introduction

Environmental, Social, and Governance ("ESG") is now dominating the corporate landscape.[1] ESG encompasses a broad array of "Environmental" issues such as climate change, "Social" issues ranging from workplace safety and child labor practices to diversity, equity, and inclusion ("DEI") initiatives, and "Governance" matters related to shareholder voting rights and board composition.[2] ESG has impacted the behavior of actors across the corporate ecosystem. Shareholders, asset managers, and financial institutions are increasingly demanding that corporations provide more ESG disclosure and make more concrete ESG commitments.[3] Boards have become increasingly focused on ESG oversight,[4] and have increasingly prioritized selecting new directors who have ESG expertise.[5] Corporations have ramped up their ESG engagement,[6] contributing to the steady rise in voluntary ESG disclosure and new ESG commitments, policies, and practices.[7]

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[1] *See* David Larcker et al., *Seven Myths of ESG*, 28 Eur. Fin. Mgmt. 869 (2022) (referring to the trend to incorporate ESG as "pervasive"); Elizabeth Pollman, *The Making and Meaning of ESG* 1 (U. Pa. Inst. for L. & Econ., Working Paper No. 659, 2022); Lisa M. Fairfax, *Dynamic Disclosure*, 101 Tex. L. Rev. 273, 274–75 (2022); Richard Mattison, *Key trends that will drive the ESG agenda in 2022*, S&P Global Insights (Jan. 31, 2022), https://www.spglobal.com/esg/insights/featured/special-editorial/key-esg-trends-in-2022 (noting rising pressure to focus on ESG issues); Lillian Tsu & Synne Chapman, *2022 Shareholder Engagement Trends and Considerations: ESG and Investor Outreach*, Cleary Gottlieb News & Insights (Jan. 11, 2022), https://www.clearygottlieb.com/news-and-insights/publication-listing/2022-shareholder-engagement-trends-and-considerations-esg-and-investor-outreach (ESG is a "mainstay" of board and investor focus); Rick A. Fleming & Alexandra M. Ledbetter, *Making Mandatory Sustainability Disclosure a Reality,* 50 Env't. L. Rep. 10647, 10648 (2020) (a "critical mass" of investors views ESG information important); Robert G. Eccles & Svetlana Klimenko, *The Investor Revolution*, Harv. Bus. Rev., 106–16 (May–June 2019) (ESG issues "almost universally" at the top of executives' minds); Virginia H. Ho & Stephen K. Park, *ESG Disclosure in Comparative Perspective*, 41 U. Pa. J. Int'l L. 249, 261 (2019).

[2] *See* Lisa M. Fairfax, *Board Committee Charters and ESG Accountability*, 12 Harv. Bus. L. Rev. 371, 374 (2022); Fairfax, *supra* note 1, at 281; Sullivan and Cromwell, 2022 Proxy Season Review: Part I: Rule 14A-8 Shareholder Proposals 2, 9, 18, 24 (2022) [hereinafter Sullivan 2022 Proxy Review], https://www.sullcrom.com/files/upload/sc-publication-2022-Proxy-Season-Part-1-Rule-14a-8.pdf (describing shareholder proposals within each ESG subject area).

[3] *See* Larcker et al., *supra* note 1; Fairfax, *supra* note 1, at 289–90.

[4] *See* Fairfax, *supra* note 2, at 375 (demonstrating sharp increase in board oversight of ESG).

[5] *See* Heidrick & Struggles, Board Monitor US 12 (2022), https://www.heidrick.com/-/media/heidrickcom/publications-and-reports/board-monitor-us-2022.pdf (noting that the share of directors with sustainability experience is on the rise, going from 6% in 2020 to 14% in 2021); Mattison, *supra* note 1 (noting pressure on boards to "shore up their ESG credentials").

[6] *See* Tsu & Chapman, *supra* note 1 ("[S]maller institutional investors and activists have made clear that ESG engagement is a priority[.]"); ISS ESG, Stewardship Excellence and Engagement 2021 3 (2021), https://www.issgovernance.com/file/publications/iss-esg-stewardship-excellence-engagement-2021.pdf ("engagement . . . is clearly on its way to going mainstream").

[7] In 2022, 96% of S&P 500 companies and 81% of Russell 1000 companies engaged in such reporting, up from 20% of S&P 500 companies eleven years ago. *See* G&A Inst., 2022 Sustainability Reporting in Focus (2022), https://www.ga-institute.com/research/ga-research-directory/

One of the confusing and confounding aspects of the meteoric rise of ESG has been its significant criticism from both sides of the ideological spectrum. Those who disagree with the notion that corporations should attend to issues beyond shareholder profit maximization have sparked a so-called anti-ESG movement, referring to ESG as "woke capitalism" and insisting that ESG is detrimental to shareholders, financial returns, and the market.[8] Those who insist that corporations have an obligation to focus on non-shareholder stakeholders, such as employees and customers, and insist that corporations should seek to ameliorate societal issues such as climate change and racial inequity, condemn ESG as a marketing ploy or "greenwashing."[9]

This article contends that these seemingly contradictory criticisms stem from the same source—the failure to sufficiently appreciate the significance of the "G" in the ESG. At best, the "G" gets overlooked because of our extreme focus on the climate issues associated with the "E" or the equity issues associated with the "S."[10] For some, the "G"'s inclusion in ESG appears perplexing because the shareholder rights and corporate governance issues encompassed within the "G" appear at odds with the broader social issues encompassed by the "E" and the "S."[11] For others, the inclusion of the "G" almost dooms any realistic effort to promote "E" and "S" issues because the "G" seems inextricably linked to shareholders and financial concerns, and given the power of shareholders, such a link limits the extent to which ESG can meaningfully

sustainability-reporting-trends/2022-sustainability-reporting-in-focus.html. In 2020, 92% of S&P 500 companies and 70% of the full Russell 1000 companies published a voluntary ESG report. *See* Lucy Pérez et al., *Does ESG Really Matter—and Why?*, McKinsey Q. 1 (Aug. 2022), https://www.mckinsey.com/business-functions/sustainability/our-insights/does-esg-really-matter-and-why; G&A Inst., 2021 Sustainability Reporting in Focus 2 (2021).

[8] *See e.g.*, Jason Wingard, *ESG: It's Not Ideology, It's Economics*, Forbes (Dec. 5, 2022), https://www.forbes.com/sites/jasonwingard/2022/12/05/esg-its-not-ideology-its-economics/?sh=31c66e505f8b (noting growth in backlash); Allison Prang, *An Anti-ESG Activist Investor Presses for Changes at Apple and Disney*, Wall St. J. (Sept. 20, 2022), https://www.wsj.com/articles/anti-esg-activist-investor-vivek-ramaswamy-presses-for-changes-at-apple-and-disney-11663684474; Laurie Clarke, *ESG Investing Facing Challenges from All Sides? Can it Survive?*, Fortune (Sept. 19, 2022), https://fortune.com/2022/12/19/esg-investing-faces-challenges-from-all-sides-can-it-survive (discussing growth in anti-ESG movement and bills related to anti-ESG actions).

[9] *See* Clarke, *supra* note 8 (noting concern that ESG topics lead to exaggeration around environmental and social issues); EY Ctr. for Bd. Matters, 2022 Proxy Season Preview 6 (2022) [hereinafter EY 2022 Proxy Season Preview], https://assets.ey.com/content/dam/ey-sites/ey-com/en_us/topics/board-matters/cbm-2022-proxy-season-preview-final-us-score-no-15036-221us.pdf.

[10] *See, e.g.*, Larcker et al., *supra* note 1, at 875 (referring to the notion that the G belongs with the E and the S as a myth); Susana Sierra, *Governance as the Force for Real Change in the ESG World*, Forbes (Sept. 27, 2022), https://www.forbes.com/sites/forbesbusinesscouncil/2022/09/27/governance-as-the-force-for-real-change-in-the-esg-world/?sh=188864d93c9e (noting that the G is the least popular and most overlooked aspect of ESG).

[11] *See* Larcker et al., *supra* note 1, at 875 ("A puzzling aspect of ESG is why governance is included as a third pillar, alongside environment and social issues.").

advance "E" and "S" issues.[12] Still others discount the "G" 's focus on shareholders and financial concerns, instead arguing that ESG has nothing to do with shareholder maximization and thus reflects a breach of fiduciary duty.[13] While these seemingly contradictory concerns appear confusing, they all animate from the same source—a failure to appreciate the "G" in ESG.

This article argues that the tendency to discount the "G," or disconnect the "G" from the "E" and "S," is not only misguided, but also fundamentally misconstrues ESG. This article further argues that the "G" is the *most* important letter in ESG, not only for those interested in ensuring meaningful corporate progress on the "E" and "S," but also for those concerned with navigating fiduciary duty issues and ensuring that corporations remain focused on financial sustainability.

This article makes four critical contributions to the ESG conversation. First, to the extent the effort to jettison the "G" is rooted in a desire to circumvent shareholders, this article makes clear that such an effort is a fool's errand because the reality of shareholder power means that no effort to meaningfully and systemically advance critical issues within the corporation is possible without shareholder advocacy and support. Indeed, critics of the "G" 's inclusion within ESG acknowledge this point when they express concerns about the dominance of shareholders implicit in the ESG.[14] However, attempting to thwart or circumvent shareholder power by disconnecting the "G" from the "E" and "S" is not a realistic solution to those concerns. Instead, the very dominance of shareholder power makes the "G" essential *precisely because* shareholder buy-in and support is essential to moving the needle on any issue within the modern corporate ecosystem.

Second, this article argues that the tendency to discount or overlook the "G" fundamentally misconstrues ESG. With this assertion, this article repudiates false claims that ESG is incompatible with shareholder value or otherwise represents a breach of boards' or asset managers' fiduciary duty. To be sure, there is serious confusion around the precise meaning of ESG and this confusion has enabled critics from both sides of the ideological perspective to scorn ESG.[15] ESG has sparked concerns that it is too conscious or "woke," while simultaneously igniting concerns that it is not conscious enough and is thus mere rhetoric or illusory.[16] These contradictory critiques illuminate the failure

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[12] *See id.* at 871 (noting that the corporate focus on returns harms non-shareholder stakeholders, and thus the pursuit of corporate profit works in opposition to stakeholder betterment); Dorothy Lund & Elizabeth Pollman, *The Corporate Governance Machine*, 121 COLUM. L. REV. 2563, 2628–30 (2021).

[13] *See infra* note 39 (discussing opposition to ESG activities and emphasis on concerns around breach of fiduciary duty).

[14] *See supra* note 8.

[15] *See* Pollman, *supra* note 1.

[16] *See id.* at 5; *see also* Clarke, *supra* note 8.

to appropriately understand ESG and the importance of the "G" within ESG.[17] A careful review of the origins of ESG reveals two important facts. First, ESG is not synonymous with corporate social responsibility ("CSR") and any corresponding notion that corporations should be willing to sacrifice profits in order to promote societal objectives.[18] Second, ESG is not synonymous with stakeholderism and the concept that corporations should be willing to advance other stakeholder interests without regard to shareholder concerns.[19] In fact, the report in which ESG was coined intentionally refrained from using terms such as "CSR" and "stakeholderism" to avoid the potential that ESG would be equated with such terms.[20] Distinguishing ESG from these other concepts is important because that distinction provides needed clarity around the true meaning of ESG. A deeper dive into the origins and evolution of ESG reveals that the "G" is a vital aspect of ESG precisely because of the desire to link the "E" and the "S" to shareholders and concerns around financial materiality.[21] In other words, the "G" 's focus on shareholders and financial concerns is a deliberate and central aspect of ESG.[22] This focus not only belies claims that ESG reflects a breach of any fiduciary duty to promote shareholder value, but also reveals that the desire to eliminate financial concerns associated with the "G" is premised on a flawed understanding of ESG.[23]

Third, this article strenuously argues that the "G" is a necessary pre-condition for actualizing environmental and social matters, and that the "G" has the best potential for transforming any corporate commitment on those matters from rhetoric into reality. As an initial matter, success around adoption of the issues associated with the "G" paved the way for promotion of the issues connected to the "E" and the "S."[24] Viewed from this lens, it is no accident that the rise in corporate attention on environmental and social issues came after the rise in shareholder power. That rise in power ensured that corporations would be more responsive to shareholder concerns.[25] Shareholders have used their new-found governance power to advance environmental and social issues.[26] More importantly, those who coined ESG believed that the "G" was the most important aspect of ESG because governance practices were critical

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[17] *See* Pollman, *supra* note 1, at 4–5.

[18] *See* The UN Glob. Compact, Who Cares Wins: Connecting Financial Markets to a Changing World 1–2 (2004) [hereinafter Who Cares Wins], https://www.unepfi.org/fileadmin/events/2004/stocks/who_cares_wins_global_compact_2004.pdf.

[19] *See id.*

[20] *See id*.

[21] *See* Pollman, *supra* note 1, at 12–13; Who Cares Wins, *supra* note 18, at 2.

[22] *See supra* note 21.

[23] *See* Who Cares Wins, *supra* note 18, at 3 (noting that the integration of ESG aspects was increasingly viewed as "falling within the scope" of the fiduciary duty of asset managers and other financial institutions).

[24] *See infra* Part III.C.

[25] *See id*.

[26] *See infra* Part III.B.

for advancing any issues within the corporate arena.[27] Consistent with this belief, shareholders have now been using governance tools to ensure that corporations credibly commit to their ESG promises.[28] In other words, shareholders are utilizing the "G" to transform corporations' general ESG promises into real ESG performance and progress.

Finally, linking the "G" with the "E" and the "S" facilitates a reimagining of the governance function in the corporate ecosystem. Indeed, this article contends that we are witnessing a revitalization of the original intent of governance in a manner that will better ensure that the "G" serves as a core driver of progress around the "E" and the "S." The "G" pertains to creating internal measures for monitoring behavior, and thus focuses on the creation and implementation of goals, targets, policies, practices, and procedures that ensure appropriate oversight and accountability.[29] In recent history, governance in the corporate world has been tethered to *shareholder* governance practices.[30] However, good governance was not intended to focus solely on shareholder practices, but instead was aimed at ensuring the adoption of effective governance policies and practices for all corporate commitments.[31] ESG is ushering in a potential realignment such that corporate governance is being used as it was originally intended—as an accountability tool for all corporate commitments. In the context of ESG, shareholders are now demanding that corporations adopt governance measures such as targets, goals, and policies designed to ensure that meaningful oversight and accountability metrics are in place for advancing corporate commitments related to environmental and social issues. In this way, advocates of ESG are helping to ensure that corporate governance is more closely aligned with its original intent. ESG therefore is facilitating the restoration of the original governance function—the "O.G."—and it could not have come at a more critical time in the development of corporate law and governance.

Part I of this article explores some of the reasons why the "G" has been overlooked and even actively shunned. Part II reveals the flaws in that case, highlighting the centrality of the "G" in ESG, and repudiating false claims that ESG is incompatible with shareholder value or represents a breach of fiduciary duty. Part III illuminates the way the "G" serves as a prerequisite to advancing environmental and social issues in the corporation. It then advances the argument around the revitalization of governance as an accountability measure for all corporate obligations. Part IV concludes.

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[27] *See* Pollman, *supra* note 1, at 13; Who Cares Wins, *supra* note 18, at 2 (referring to corporate governance as a "crucial prerequisite").

[28] *See, e.g.*, *infra* note 70.

[29] *See infra* Part II.B.

[30] *See, e.g.*, Lund & Pollman, *supra* note 12, at 2630 ("the shareholder primacy viewpoint has become enmeshed in our cultural and institutional understanding of good governance").

[31] *See infra* notes 197–200 and accompanying text.

I. What's "G" Got to Do with It?

On the surface, there are many reasons why the "G" may be overlooked or considered incompatible with ESG, thereby meriting removing it from ESG. This Part explores these reasons.

A. The Relative Insignificance of "G"

As an initial matter, the "G" appears to pale in significance to the "E" and the "S." Indeed, some experts warn that climate change is the greatest threat the world has ever faced, calling it an existential threat to our very existence.[32] Viewed from this perspective, it is no wonder that the "E" has a position of prominence in the ESG conversation. Similarly, there was a national increase in focus on the DEI issues associated with the "S" in the aftermath of the police shootings of unarmed Black people and the subsequent re-engagement around racial equity, coupled with the global pandemic.[33] Heightened awareness around these issues appear to relegate the "G" to a less dominant and less important role.

B. A Fatal Disconnect

Another seemingly obvious reason for discounting the "G" is that the issues associated with the "G" seem wholly incompatible with those associated with the "E" and the "S." The issues associated with the "E" relate to environmental concerns such as climate change, deforestation, recycling, water rights, and greenhouse gas emissions.[34] Issues associated with the "S" include social issues ranging from DEI initiatives, to pay equity, human rights, workers' rights, child labor, and issues impacting supply chains.[35] These "E" and "S" issues seem focused on broad societal matters, many of which are external to any specific corporation. By contrast, issues encompassed by the "G" include corporate governance concerns such as proxy access, board declassification, majority voting, supermajority voting arrangements, special meeting rights, written consent, and board composition.[36] These issues relate to shareholder

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[32] *See* Press Release, UN Hum. Rts. Off., *Climate Change the Greatest Threat the World Has Ever Faced, UN Expert Warns* (Oct. 21, 2022), https://www.ohchr.org/en/press-releases/2022/10/climate-change-greatest-threat-world-has-ever-faced-un-expert-warns#:~:text=Climate%20change%20the%20greatest%20threat,faced%2C%20UN%20expert%20warns%20%7C%20OHCHR.

[33] *See* Sullivan 2022 Proxy Review, *supra* note 2, at 1 (demonstrating an explosion in corporate attention on social issues in the aftermath of George Floyd's death and concerns related to the COVID-19 pandemic).

[34] Fairfax, *supra* note 2, at 374; *see also* Sullivan 2022 Proxy Review, *supra* note 2, at 24.

[35] Fairfax, *supra* note 2, at 374; *see also* Sullivan 2022 Proxy Review, *supra* note 2, at 9.

[36] Fairfax, *supra* note 2, at 374; *see also* Sullivan 2022 Proxy Review, *supra* note 2, at 18.

voting rights and corporate structure, and thus appear to be internal to the corporation and disconnected with any broader societal matters.

Critics from both sides of the ideological spectrum have emphasized the seeming disconnect between the "G" and the "E" and the "S," albeit for different reasons. Those hoping to encourage corporations to focus on environmental and social issues argue that issues embedded in the "G" are unconnected with whether or not a company effectively promotes environmental and social issues.[37] By contrast, a core concern of those in the anti-ESG movement is that business has no business seeking to advance environmental and social issues, both because corporations have no expertise in such matters, but also because such issues have no relationship with the corporation's core purpose.[38] Perhaps most importantly, these anti-ESG proponents strenuously contend that a corporate focus on environmental and social concerns is inconsistent with a fiduciary responsibility to promote shareholder value.[39] Indeed, some twenty Attorneys Generals signed a letter to the two largest proxy advisors characterizing their focus on ESG as a breach of fiduciary duty.[40] In this regard, both appear to believe that the "G" does not belong with the "E" and the "S," though for different and relatively contradictory reasons.

C. *Profit as Problematic*

Some contend that the "G" is problematic, and thus worthy of exclusion from ESG, because it appears focused on financial concerns in a manner that runs counter to the focus on issues associated with "E" and "S." From this perspective, the effort to encourage corporations to focus on topics within the "E" and the "S" appear aligned with the historical effort in the corporate community to encourage corporations to focus on issues beyond shareholder

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[37] *See* Larcker et al., *supra* note 1, at 875–76.

[38] *See, e.g.*, Letter from Sean Reyes, et al. to Glass Lewis and ISS (Jan. 17, 2023) [hereinafter Letter to Glass Lewis and ISS], https://attorneygeneral.utah.gov/wp-content/uploads/2023/01/2023-01-17-Utah-Texas-Letter-to-Glass-Lewis-ISS.pdf; Milton Friedman, *A Friedman Doctrine—The Social Responsibility of Business Is to Increase its Profits*, N.Y. TIMES (Sept. 13, 1970), https://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html.

[39] *See* Letter to Glass Lewis and ISS, *supra* note 38; *see also* Commissioner Mark T. Uyeda, Remarks at the California '40 Acts Group (Jan. 27, 2023), https://www.sec.gov/news/speech/uyeda-remarks-california-40-acts-group ("[S]ome asset managers have been walking a fine line between hewing to their fiduciary duties to their clients and furthering social and political goals that may be unrelated to the interests of their clients.").

[40] *See* Letter to Glass Lewis and ISS, *supra* note 38. In response, Glass Lewis, one of the proxy advisors that was the target of the letter, firmly rejected the characterization by noting that they evaluated ESG issues such as climate and diversity, equity, and inclusion through the lens of long-term shareholder value. *See* Letter from Glass Lewis to State Attorneys General (Jan. 31, 2023), https://aboutblaw.com/6Ay.

profit.[41] For those sympathetic to this effort, ESG has been characterized as synonymous with corporate social responsibility and viewed as a revival of CSR.[42] CSR encourages sacrificing economic concerns for doing the right thing, especially in areas related to the environment and social causes.[43] To the extent the "G" is linked with profit maximization, it seems incompatible with CSR.[44] Importantly, there is worry that linking environmental and social concerns with the economic concerns embedded in the "G" will prove counterproductive.[45] This worry is based on the view that focusing on profit concerns undermines any realistic effort to advance the interests of other stakeholders.[46] Moreover, some insist that profit cannot, and should not, be the driver of ameliorating vital environmental and social issues because the profit motive is corrupting and limiting.[47] In other words, linking the "G" with the "E" and the "S" runs the risks of undermining meaningful progress on those issues.

D. Shareholders' Power

In light of shareholders' outsized power and influence, there is an argument that the "G" needs to be decoupled from the "E" and the "S," because the "G" 's link to shareholders will crowd out any ability to focus on the interests of other stakeholders and their concerns. Most of the issues associated with the "G" are aimed at augmenting shareholders' power and influence over the corporation and its affairs.[48] By contrast, the "E" and "S" appear aligned with stakeholderism and the concept that corporations should focus on advancing the interests of the corporation's non-shareholder stakeholders, such as employees, customers, and consumers.[49] Stakeholderism suggests that

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[41] *See* Lisa M. Fairfax, *Stakeholderism, Corporate Purpose, and Credible Commitment*, 108 Va. L. Rev. 1163, 1176–77 (2022).

[42] *See* Larcker et al., *supra* note 1, at 2; Pollman, *supra* note 1, at 25. *See generally* Tim Stobierski, *15 Eye-Opening Corporate Social Responsibility Statistics*, HBS Bus. Insights Blog (June 15, 2021), https://online.hbs.edu/blog/post/corporate-social-responsibility-statistics (providing a general discussion of CSR); Mauricio Agudelo et al., *A Literature Review of the History and Evolution of Corporate Social Responsibility*, 4 Int'l J. Corp. Soc. Resp. 1 (2019).

[43] *See* Larcker et al., *supra* note 1, at 2.

[44] As Lund & Pollman note, advocates of CSR will be frustrated by the corporate governance infrastructure because it preserves shareholder primacy. *See* Lund & Pollman, *supra* note 12, at 2628. *See also id.* at 2574; Daniel Fischel, *The Corporate Governance Movement*, 35 Vand. L. Rev. 1259, 1269–72 (1982).

[45] *See* Fischel, *supra* note 44.

[46] *See* Larcker et al., *supra* note 1, at 871 (noting that the corporate focus on returns harms non-shareholder stakeholders and thus, the pursuit of corporate profit works in opposition to stakeholder betterment).

[47] *See, e.g.*, Lund & Pollman, *supra* note 12, at 2631 (noting that linking environmental and social issues to shareholder profit maximization "limits acceptable rationales and favors activity that can be reduced to measurable metrics tied to risk or financial value").

[48] *See* Lisa M. Fairfax, *From Apathy to Activism: The Emergence, Impact, and Future of Shareholder Activism as the New Corporate Governance Norm*, 99 B.U. L. Rev. 1301 (2019).

[49] *See* Larcker et al., *supra* note 1, at 871.

corporations should not solely focus on shareholders.[50] Some contend that stakeholderism means that corporations should be willing to promote the interests of other stakeholders over those of shareholders.[51] A focus on the "G" undermines this desired focus on all stakeholders.

Divorcing the "G" from the "E" and "S" is also rooted in the concern that the "G" 's focus on shareholders may undermine or severely limit appropriate policies and practices associated with environmental and social issues. From this perspective, the real concern is that shareholders cannot be trusted to effectively advocate for other stakeholders.[52] At best, we can only expect that shareholders will address the "E" and "S" issues through the prism of their benefit to shareholders.[53] At worst, particularly when shareholder and stakeholder interest collide, we can expect that shareholders will ignore or harm stakeholders and their concerns.[54] Consequently, so long as the "G" remains an aspect of ESG, any meaningful effort to promote the "E" and "S" is doomed to failure.

II. Deconstructing ESG and Repudiating False Breach Claims

On the surface, the aforementioned rationales for discounting or even excluding the "G" from ESG appear valid. However, a closer inspection of the true meaning and intended impact of ESG and corporate governance belies this appearance. This deeper dive shines a light on the centrality of the "G" to the ESG endeavor, and any potential for real progress on environmental and social issues within the corporate sphere.

A. *The Fool's Errand*

Before deconstructing ESG, it is important to tackle the concerns raised by the "G" 's connection to shareholders and shareholder power. This article insists that the reality of shareholder power means that the best strategy for grappling with this concern is through alliance rather than disassociation.

In the past two decades, we have witnessed a dramatic increase in shareholders' willingness to use their power to influence the corporation and its

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[50] *See* Fairfax, *supra* note 41, at 1171–72; Lucian Bebchuk & Roberto Tallarita, *The Illusory Promise of Stakeholder Governance*, 106 Cornell L. Rev. 91, 104 (2020); Cathy Hwang & Yaron Nili, *Shareholder-Driven Stakeholderism*, U. Chi. L. Rev. Online 4 (2020).

[51] *See* Bebchuk & Tallarita, *supra* note 50, at 120.

[52] *See* Fairfax, *supra* note 41, at 1209; Bebchuk & Tallarita, *supra* note 50, at 108–11.

[53] *See, e.g.*, *supra* note 47.

[54] *See* Lund & Pollman, *supra* note 12, at 2566 (noting concern that when corporate governance focuses on shareholder welfare, "superior governance arrangements from a social welfare perspective may be discouraged or taken off the table").

affairs.[55] First, shareholders have increased their engagement with corporations. There has been a steep rise in shareholder "request, and in some instances demand" for engagement with corporate officers and directors around issues of significance to shareholders.[56] Whereas historically there was very little interactions between the corporation and its shareholders, particularly outside of the annual meeting,[57] today, shareholder engagement is a year-round activity and is viewed as a corporate governance best practice.[58] Importantly, shareholders view engagement as the foundation of their ability to impact corporate behavior,[59] noting that its value "only grows over time."[60] As one 2022 engagement survey notes, "many large institutional investors, especially top shareholders, increasingly expect to be able to directly engage with directors."[61] Shareholders' increased engagement reflects their increased influence over the corporation and its affairs.[62]

Second, shareholders are using the shareholder proposal process to exercise their influence over corporate affairs. The shareholder proposal process allows shareholders to submit proposals related to issues they deem important to the corporation to be voted upon by their fellow shareholders.[63] The shareholder vote on any proposal is advisory and hence the corporation is not obligated to adopt any proposal even if it receives a majority shareholder vote.[64] However, the shareholder proposal process is essentially the only forum in which public company shareholders can make recommendations about vital corporate issues, and thus the process is a key forum for enabling shareholders to communicate their preferences and concerns to the corporation not only through the submission of shareholder proposals, but also through the level of shareholder support for those proposals.[65] Alas, while the shareholder proposal regime has existed since 1942, it essentially laid dormant for decades because shareholders rarely used the shareholder proposal process.[66] However, the past few decades have seen a steady increase in shareholders' use of

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[55] *See generally*, Fairfax, *supra* note 48.

[56] *See id*. at 1305.

[57] *See id*. at 1309–10.

[58] *See id*. at 1320–21, 1330.

[59] *See* VANGUARD, GLOBAL INVESTMENT STEWARDSHIP PRINCIPLES 3, (Nov. 2021), https://corporate.vanguard.com/content/dam/corp/research/pdf/Global%20investment%20stewardship%20principles_final_112021.pdf (referring to engagement as the "foundation" of their stewardship).

[60] *See* William McNabb, Vanguard Chief Exec. Officer, An Open Letter to Directors of Public Companies Worldwide 2 (Aug. 31, 2017), https://www.wlrk.com/docs/2017VanguardOpenLettertoBoards.pdf.

[61] *See* Tsu & Chapman, *supra* note 1.

[62] *See* ISS ESG, *supra* note 6 (engagement allows shareholders to actively promote positive corporate change).

[63] *See* LISA M. FAIRFAX, SHAREHOLDER DEMOCRACY 64 (2011).

[64] *See id.*

[65] *See id.* at 63.

[66] *See* Fairfax, *supra* note 48, at 1309.

the shareholder proposal process to identify issues of importance and concern with respect to the corporation and its activities.[67] In particular, in the past decade there has been an upward trend in the number of shareholder proposal submissions, with many years reflecting a record-breaking number of proposal submissions.[68] Shareholders use the proposal process to proactively seek to influence corporate decision-making around vital issues.[69] The explosion of shareholder activity in the shareholder proposal regime is yet another reflection of increased shareholder power and influence.

Third, shareholders have increasingly adopted voting policies and practices aimed at ensuring that corporations address particular issues, and holding corporations accountable for their failures to address such issues.[70] On the one hand, these voting policies are designed to communicate shareholder expectations around corporate and board behavior.[71] On the other hand, these voting policies make clear that shareholders are willing to withhold their support from companies and directors when they engage in actions that fall short of shareholder expectations.[72] Shareholders' active use of their voting power has moved the needle significantly on their ability to impact corporate affairs.

Perhaps most significantly, shareholders have demonstrated an increased willingness to vote against management wishes.[73] Traditionally shareholders rarely voted against management and their recommendations, leaving management free to transact business without significant shareholder interference.[74] This overwhelming deference to managers no longer exists. Instead, shareholders have disregarded managerial preferences in a multitude of ways. There has been a growing amount of shareholder support for shareholder proposals despite management's recommendation to vote against such proposals.[75] Moreover, shareholders have demonstrated an increased willingness to

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[67] *See* Sullivan 2022 Proxy Review, *supra* note 2, at 1.

[68] *See id.* (record breaking proposals in 2021 and 2022); Matteo Tonello, The Conf. Bd., Shareholder Voting Trends (2018-2022) 4–5 (2022) (noting a sharp increase in the number of shareholder proposals across the last five years); *see also* Fairfax, *supra* note 48, at 1320.

[69] *See* Fairfax, *supra* note 48, at 1310.

[70] *See, e.g.*, John Galloway, *Proxy Voting Policy for U.S. Portfolio Companies*, Harv. L. F. Sch. Corp. Governance (Feb. 7, 2023), https://corpgov.law.harvard.edu/2023/02/07/proxy-voting-policy-for-u-s-portfolio-companies-2/; *see also* State St. Glob. Advisors, Proxy Voting and Engagement Guidelines (Mar. 2023), https://www.ssga.com/library-content/pdfs/asr-library/proxy-voting-and-engagement-guidelines-us-canada.pdf; John McKinley, *BlackRock Investment Stewardship Global Principles*, Harv. L. Sch. F. on Corp. Governance (Dec. 18, 2021), https://corpgov.law.harvard.edu/2021/12/18/blackrock-investment-stewardship-global-principles-2/.

[71] *See* McKinley, *supra* note 70 ("[We] will express any concerns through our voting where a company's actions or disclosures are inadequate.").

[72] *See id.*

[73] *See* Tonello, *supra* note 68, at 3 (detailing shareholder votes in support of shareholder proposals).

[74] *See* Fairfax, *supra* note 48, at 1309.

[75] *See* Sullivan 2022 Proxy Review, *supra* note 2, at 2, 9, 18 (revealing that a large portion of shareholder proposals received a substantial percentage of the shareholder vote, many of which received a majority of the shareholder vote); *see also* Fairfax, *supra* note 48, at 1318–19.

vote against particular directors.[76] While directors continue to receive a strong percentage of shareholder support, average shareholder support for directors has been declining.[77] The percentage of directors who fail to receive majority support has always been low, however, there has been a growing number of directors receiving less than majority shareholder support.[78] Shareholders' willingness to defy management, and not only disregard their recommendations, but also reject director candidates, is a strong signal of shareholders' new willingness to actively exercise their power and authority over corporate affairs.[79] Each of these actions underscores shareholders' increasing power and willingness to use their influence to shape, and even thwart, managerial decision-making.

Importantly, boards and corporations have been responsive to shareholders. In the past, shareholder attempts to influence corporate affairs was seen as inappropriate and undesirable.[80] Today, both shareholders and boards have embraced a belief in the appropriateness of some level of shareholder activism, along with a belief in the appropriateness of enabling shareholders to have greater voice and influence over corporate matters.[81] Hence, it is now commonplace for boards to express the view that increased shareholder influence represents an important accountability check and is in the best interest of the corporation.[82]

Boards also have made corporate changes in response to shareholder influence. This response is remarkable precisely because historically, boards strenuously resisted or otherwise refused to adopt shareholder recommendations.[83] However, the landscape has shifted dramatically in favor of responsiveness to shareholders. Thus, whereas boards were previously reluctant and unwilling to routinely engage with shareholders, today's corporation and board actively seeks out engagement opportunities with shareholders.[84] In contrast to the days in which boards refused to adopt shareholder proposals, even when they received majority shareholder approval,[85] it has now become common for boards to enact policies and practices embedded in shareholder proposals, even after such boards recommend against shareholder support for the

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[76] *See* Tonello, *supra* note 68, at 7; *see also* PwC Governance Insights, Boardroom Recap: The 2022 Proxy Season 4–5 (2022), https://www.pwc.com/us/en/services/governance-insights-center/assets/pwc-boardroom-recap-2022-proxy-season.pdf.

[77] *See* Tonello, *supra* note 68, at 7 (noting that average support for directors has been declining in recent years); *see also* PwC Governance Insights, *supra* note 76, at 5.

[78] *See* Fairfax, *supra* note 55, at 1318.

[79] *See id.* at 1319.

[80] *See id.* at 1310–12.

[81] *See id.* at 1322–32.

[82] *See id.* at 1329–32 (providing examples of board disclosures affirming the appropriateness of shareholder voice and influence).

[83] *See, e.g.*, Lucian A. Bebchuk, *The Case for Increasing Shareholder Power*, 118 Harv. L. Rev. 833, 854 (2005).

[84] *See* Fairfax, *supra* note 48, at 1321.

[85] *See supra* note 83.

proposal.[86] Boards also have been willing to change their composition—adding and in some cases removing directors—in order to comply with shareholder demands.[87] These activities leave no doubt that boards have become more responsive to shareholder concerns, and thus the rise in shareholder power has resulted in an increase in shareholder influence over the corporation.

As an example, the 2022 proxy statement for The Walt Disney Company ("Disney") includes an entire section on Disney's shareholder engagement process coupled with strong disclosure around Disney's commitment to shareholder engagement.[88] According to the proxy statement, Disney contacted 85% of its largest shareholders in 2021 for purposes of engagement, and that engagement took place throughout the calendar year.[89] This level of intentional and year-round engagement is both an exemplar of the new norm in shareholder engagement, and in sharp contrast to historical norms of little shareholder engagement. Disney's proxy statement includes a two-page chart with two columns, one labeled "what we heard," and the other labeled "what we did."[90] Disney describes the chart as a summary of the "feedback the Company received from investors and actions the Company took in response."[91] The chart is a visible and prominent depiction of the manner in which shareholder power has resulted in director responsiveness to shareholders.

Against this backdrop of heightened shareholder power and corporate responsiveness, it seems a fool's errand to seek to convince the corporation to take actions that do not align with shareholder preferences. The fact that boards and corporations have complied with shareholder demands despite initial, and sometimes strenuous resistance, underscores the folly of such an endeavor.[92] Shareholder influence and interference is now a fact of modern corporate life. In this regard, it strains credulity to think that stakeholders outside of the corporate sphere could do an end-run around shareholder power. Indeed, critics' concern about the way the "G" 's focus on shareholders may crowd out the interest of other stakeholders is an acknowledgement of shareholder power and the difficulties of circumventing the influence of that power.

Moreover, the better strategic choice would be to make allies of shareholders. Indeed, ESG reflects an acknowledgement of the difficulties of persuading boards and corporations to address environmental and social issues without shareholder buy-in. The adoption of ESG stemmed from the

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[86] *See* Fairfax, *supra* note 48, at 1327–29.

[87] *See id.*; *see also* PwC Governance Insights, *supra* note 76, at 5.

[88] The Walt Disney Co., Notice of Annual Meeting of Shareholders and Proxy Statement 6–8 (2022).

[89] *Id.* at 6.

[90] *Id.* at 7–8.

[91] *Id.* at 7.

[92] *See* Lisa M. Fairfax, *Just Say Yes? The Fiduciary Duty Implications of Directorial Acquiescence*, 106 Iowa L. Rev. 1315, 1328–29 (2021) (discussing initial resistance to shareholder preferences).

significant frustration experienced by organizations outside of the corporation seeking to focus corporate attention on issues without any appropriate allies.[93] These organizations eventually came to believe that they needed shareholders in their camp in order to achieve success.[94] And their belief has been validated. When shareholders and asset managers endorsed ESG, it "took off."[95] Viewed from this lens, the effort to circumvent shareholder power by eliminating the "G" is ill-advised strategic choice.

B. Misunderstanding and Miscommunication on ESG

Putting aside the feasibility concerns with disconnecting the "G" from the "E" and the "S," the effort to decouple the "G" fundamentally misconstrues the purpose and mission of ESG in at least three important ways. First, ESG was always meant to focus on financial concerns. Second, ESG was always meant to be connected to shareholders and shareholder value. Finally, the originators of ESG viewed the "G" as integral to the successful advancement of environmental and social concerns. For these reasons, those who seek to divorce the "G" from ESG in order to protect ESG from shareholders and their financial considerations misconstrue ESG's purpose and intent. Perhaps more importantly, those who contend that ESG has nothing to do with financial concerns are similarly misguided.

1. The Explicit Focus on "G"

ESG was first coined in a 2004 report entitled *Who Cares Wins: Connecting Financial Markets to a Changing World*.[96] From its very first pages, the report makes abundantly clear that the "G" was an integral component of ESG. The report emphasized the notion that a company's implementation of best practices in corporate governance is crucial to the successful implementation of other recommendations relating to environmental and social issues.[97] According to Paul Clements-Hunt, one of the leaders of the effort to promote ESG during this time-period, the initial view was that it should be called "GES" since there was a strong belief that governance was the most important

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[93] *See* Who Cares Wins, *supra* note 18, at 1.

[94] *See id.*

[95] Lund & Pollman, *supra* note 12, at 2567 ("[T]he ESG movement took off when it was framed in terms of shareholder value.").

[96] *See* Who Cares Wins, *supra* note 18, at 1; Betsy Atkins, *Demystifying ESG: Its History and Current Status*, Forbes (June 8, 2020), https://www.forbes.com/sites/betsyatkins/2020/06/08/demystifying-esgits-history--current-status/?sh=5f73e21a2cdd.

[97] *See* Who Cares Wins, *supra* note 18, at 2.

area of focus.[98] However, it was decided that "GES" was "not so catchy, not so sexy," so the decision was made to begin with the "E."[99] This focused attention on the "G" reveals that the "G was not an anachronistic appendage or dissimilar concept, but rather a vital and connected set of issues and means of execution for relevant E and S issues."[100]

The report also made clear that the "G" represents a necessary precursor to advancing the "E" and the "S." The report contended that sound corporate governance and attention to risk management were "crucial pre-requisites to successfully implementing policies and measures to address environmental and social challenges."[101]

2. The Economics of ESG

ESG is explicitly focused on financial matters and the financial community. The very title of the report "connecting financial markets" underscores its core purpose. The report describes its purpose as outlining recommendations to "better integrate environmental, social and governance issues" into investment policy.[102] It goes on to stress a desire to "develop guidelines and recommendations on how to better integrate environmental, social and corporate governance issues in asset management, securities brokerage services and associated research functions."[103] The report also stresses as a core goal the desire to provide guidance on how best to improve integration and consideration of ESG issues in investment decisions.[104] The report is replete with references to its core theme of integrating environmental and social issues into the financial and investment arena. Even a casual read of the report illustrates this clear financial goal.

This goal was buttressed by endorsement of the report from leaders in the financial community. The report grew out of a joint initiative of financial institutions concerned with the absence of harmonization and intentionality in considering the financial impacts of environmental and social issues.[105] The endorsing group of eighteen financial institutions with combined assets under management of over $6 trillion, included some of the world's largest financial entities such as Morgan Stanley, Goldman Sachs, and UBS.[106] The report included a series of recommendations targeting different financial actors, aimed

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[98] *See* Qayyum Rajan, *Where Did the Term ESG Come from Anyway?*, ESG Analytics (Mar. 29, 2022), https://www.esganalytics.io/insights/where-did-the-term-esg-come-from-anyway.
[99] *See id.*
[100] *See* Pollman, *supra* note 1, at 13.
[101] *See* Who Cares Wins, *supra* note 18, at 2.
[102] *See id.* at i.
[103] *See id.*
[104] *See id.*
[105] *See id.*
[106] *See id.*

at encouraging those actors to develop strategies for a more holistic integration of ESG issues into the financial market. The financial community's partnership in the very origins of ESG underscores ESG's intentionally financial roots and purpose.

The report was specifically premised on the notion that ESG impacted shareholder value.[107] The report pointed out that "investment markets have a clear self-interest" in better integration of environmental and social issues because such integration "will ultimately contribute to more stable and predictable markets."[108] The report noted that connecting "E" and "S" issues to financial matters would improve shareholder value by enabling corporations to manage risk and assess new opportunities.[109] According to its executive summary, the financial institutions endorsing the report were "convinced" that when companies perform better on ESG issues, they increase shareholder value.[110] The report also expressed a belief that the failure to attend to environmental and social issues posed a risk to shareholder value and market stability.[111] ESG grew out of this belief in the financial materiality of environmental and social factors.

3. The Financial Origins Persist

The belief that ESG is linked to shareholder value has remained a central tenet of shareholders who embrace ESG today. The largest institutional shareholders repeatedly emphasize that their focus on ESG is linked to long-term value.[112] Larry Fink, the CEO of BlackRock, stated: "profits and purpose are inextricably linked . . . when a company truly understands and expresses its purpose, it functions with the focus and strategic discipline that drive long-term profitability."[113] Vanguard and State Street have expressed similar views. Vanguard's former CEO referred to ESG as "an economic imperative, not an ideological one."[114] State Street has stood firm in its belief that ESG considerations influence long-term financial performance.[115] Indeed, State Street insists that its focus on ESG considerations is integral to its "fiduciary duty to maximize the long-term risk-adjusted returns of our clients' investments."[116] These

[107] *See id.* at 3.
[108] *See id.*
[109] *See id.* at 1.
[110] *See id.* at i.
[111] *See id.*
[112] *See* Lund & Pollman, *supra* note 12, at 2590–91.
[113] Larry Fink, *Purpose & Profit*, Harv. L. Sch. F. on Corp. Governance (Jan. 23, 2019), https://corpgov.law.harvard.edu/2019/01/23/purpose-profit/.
[114] *See supra* note 60.
[115] *See* State St. Glob. Advisors, ESG Investment Statement 1 (2022), https://www.ssga.com/library-content/pdfs/esg-investment-statement.pdf.
[116] State St. Glob. Advisors, Guidance on Diversity Disclosure and Practices 5 (2022), https://www.ssga.com/library-content/pdfs/asr-library/proxy-voting-guidance-diversity-disclosures.pdf.

sentiments extend beyond the nation's largest shareholders and asset managers. A 2017 survey of 475 global institutional investors revealed that 68% of respondents indicated that the integration of ESG factors has significantly improved financial returns, and 77% of respondents indicated their belief that ESG factors "play a role" in a company's financial performance.[117] Similarly, a 2020 U.S. Government Accountability Office ("GAO") study found that most shareholders believe that ESG factors could have a "substantial effect on a company's long-term financial performance."[118] The study also found that most shareholders focus on ESG issues to monitor and evaluate the risks and opportunities that could impact a company's financial wellbeing.[119] Members of the business community beyond shareholders also speak of ESG in terms of shareholder value. The Business Roundtable, an association of CEOs of large U.S. public companies, framed corporate commitment to stakeholders in terms of its benefit to long-term shareholder value.[120] Thus, ESG is being used by shareholders and corporations to "monitor and manage the risks facing the company due to environmental and social impact."[121] This obvious and intentional link between shareholder value and ESG means that divorcing the "G" from the "E" and the "S" would undermine the entire premise of ESG.

Of course, there are those who would like ESG to be synonymous with CSR or stakeholderism, and thus seek to discount or ignore the link between the "G," and the "E" and "S." These critics do not like the obvious connection between shareholder value and such issues, and worry that it will undermine progress around environmental and social goals.[122] This criticism reflects a failure to truly acknowledge the quintessentially financial purpose and intent of ESG.

To be sure, this acknowledgement does not negate the possibility that linking environmental and social issues to shareholder value may limit the focus of corporate attention with respect to those matters. It is entirely possible that such a link will lead to the exclusion of corporate focus on environmental and social issues that a corporation does not deem material.[123] It is also

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[117] *See Asset Owners Say Integration of ESG Has Significantly Improved Returns, State Street Global Advisors Study Shows*, Bus. Wire (Apr. 19, 2017, 12:30 PM) [hereinafter *State Street Global Advisors Study*], https://www.businesswire.com/news/home/20170419006214/en/Asset-Owners-Say-Integration-of-ESG-has-Significantly-Improved-Returns-State-Street-Global-Advisors-Study-Shows; *see also* Atkins, *supra* note 96.

[118] *See* GAO, Public Companies Disclosure of Environmental, Social and Governance Factors and Options to Enhance Them 9 (2020), https://www.gao.gov/assets/710/707967.pdf.

[119] *See id.* at 5.

[120] *See* Statement on the Purpose of a Corporation, Bus. Roundtable (Aug. 19, 2019), https://system.businessroundtable.org/app/uploads/sites/5/2023/02/WSJ_BRT_POC_Ad.pdf.

[121] *See* Pollman, *supra* note 1, at 23.

[122] *See* Larcker, *supra* note 1, at 875.

[123] *See* Fairfax, *supra* note 41, at 1191 (ESG focuses on financial materiality and acknowledges that corporations may focus on different ESG factors depending on their assessment of materiality).

possible that such a focus will result in troubling limits on the corporation's willingness to address certain environmental and social issues, especially under circumstances when a corporation believes that the costs of addressing those issues are outweighed by any benefits to shareholder value.[124] In other words, linking environmental and social issues to shareholder value necessarily creates limits on the extent to which those issues will be fully addressed, at least under the prism of ESG. However, it is unrealistic to think that any one concept can fully address all relevant issues—especially issues as expansive as those under the ESG umbrella. More importantly, the embrace of ESG does not prevent corporations from embracing CSR. In fact, many companies continue to issue CSR reports or otherwise make disclosures around CSR even as they also embrace ESG.[125] These actions reveal that there is a distinction between the two concepts, while also suggesting that focusing on ESG is not a zero-sum game with respect to a corporation's focus on other important societal issues.

Moreover, to date, shareholders have shown themselves to be important allies in advancing environmental and social issues.[126] Indeed, corporations have dramatically increased their attention on environmental and social issues to include increases in ESG disclosures, commitments, policies, and programs.[127] Commentators agree that shareholder influence and pressure contributed significantly to these trends.[128] A recent survey of S&P 1500 companies' adoption of ESG-related policies found that shareholders have played a significant role in influencing companies to adopt such policies.[129] The survey demonstrates that shareholders have moved the needle in significant ways with respect to corporate attention on environmental and social concerns.

4. The Fiduciary Fallout

While some worry that ESG's focus on shareholder value will undermine its focus on environmental and social matters, anti-ESG critics raise a contradictory concern. Those critics either refuse to acknowledge, or do not believe, the assertions of shareholders when they contend that their support of ESG is contingent on its connection to shareholders and long-term value. This is made clear by the repeated insistence from anti-ESG critics that ESG runs afoul of

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[124] *See id.* at 1206 (discussing potential restrictions on ESG goals based on shareholder financial interest).

[125] *See* Fairfax, *supra* note 1, at 292 (discussing content of voluntary ESG disclosure).

[126] *See* Hwang & Nili, *supra* note 50, at 9–10 (most ESG-related changes are driven by shareholders).

[127] *See* Fairfax, *supra* note 1, at 5–6.

[128] *See id.* at 20–22.

[129] *See* Hwang & Nili, *supra* note 50, at 9–10.

fiduciary duty.[130] In sharp contrast to this insistence, a proper understanding of ESG clearly reveals that ESG is aligned with fiduciary duty. Even apart from the fact that fiduciary duty enables a focus on other stakeholders,[131] it is clear that ESG was meant to align with shareholders and long-term financial value. In responding to the claim that a focus on ESG represented a breach of duty, one proxy advisor reiterated that their policies on environmental and social issues focus on long-term shareholder value and the extent to which such issues impact shareholder value.[132] The advisor went on to state that such issues have been widely recognized as "material risk-return" factors, and thus that simply ignoring them "is not an option today."[133] Such statements underscore the alignment between ESG and a board or asset manager's fiduciary duty precisely because they underscore the underlying premise of ESG's focus on financial value and materiality. As Professor Pollman emphasizes, the irony of those who criticize ESG as antithetical to financial matters is that "ESG was pitched from its beginning as aligning with financial materiality and the pursuit of long-term value maximization in capital markets."[134] This pitch, and the continued focus on shareholder value, makes the so-called fiduciary duty concerns unwarranted.

Importantly, it is worth noting that concerns about fiduciary duty breaches are without merit even if those raising the concerns disagree with the notion that environmental and social considerations impact shareholder value and financial performance. At the outset, it must be made clear that the law enables boards to consider other stakeholders when carrying out their fiduciary duties.[135] Then too, disagreement about the extent to which an issue impacts firm value does not impact a fiduciary duty analysis. This is because fidelity to fiduciary duty does not require that fiduciaries obtain agreement or

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[130] *See* Letter to Glass Lewis and ISS, *supra* note 38.

[131] *See infra* note 135.

[132] *See* Letter from Glass Lewis to State Attorneys General, *supra* note 40, at 3.

[133] *See id.*

[134] *See* Pollman, *supra* note 1, at 27.

[135] *See, e.g.,* Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984); Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985)*; see also* Dorothy S. Lund, *Corporate Finance for Social Good*, 121 Colum. L. Rev. 1617, 1618–20 (2021); Jill E. Fisch & Steven Davidoff Solomon, *Should Corporations Have a Purpose*?, 99 Tex. L. Rev. 1309, 1309–11 (2021) ("[T]he proposition that existing law prohibits corporate decisionmakers from considering and incorporating the interests of stakeholders and society is overstated."); Bebchuk & Tallarita, *supra* note 51, at 18; Leo E. Strine, Jr., *Restoration: The Role Stakeholder Governance Must Play in Recreating a Fair and Sustainable American Economy: A Reply to Professor Rock*, 76 Bus. Law 397, 411–15 (2021) (discussing origins of social purpose debate); Robert Thompson, *Anti-Primacy: Sharing Power in American Corporations*, 71 Bus. Law. 382, 390 (2016) (noting survey revealing that most directors felt accountable to multiple stakeholders); Larry Ribstein, *Accountability and Responsibility in Corporate Governance*, 81 Notre Dame L. Rev. 1431, 1436 (2006) ("[M]anagers who carefully attend to the firm's profits must also seek at least to some extent to further society's interests.").

consensus.[136] Nor does it require that fiduciaries provide unequivocal proof of their assertions around shareholder value and financial materiality.[137] Instead, fiduciary duty law gives fiduciaries broad discretion in the exercise of their fiduciary duties, and thus, only demands that fiduciaries *reasonably believe* that their actions will enhance the best interests of the corporation and improve shareholder value.[138] The origins of ESG, the repeated assertions around a belief in the connection between shareholder value and ESG, and the scientific and empirical evidence that supports that belief, clearly align with appropriate exercise of fiduciary duty in this realm.

Viewed from this perspective, those who are concerned about the corporation's bottom-line should take comfort in the fact that the "G" is so closely aligned with ESG. This is because the "G" is what anchors ESG to issues around financial materiality and sustainability.

III. Towards a Reconceptualization of the "G"

This Part not only makes clear that the "G" is the most important aspect of ESG for actualizing critical environmental and social goals, but also reveals the manner in which ESG is responsible for better ensuring that governance is more closely aligned with its original intent.

A. A Necessary Pre-Cursor Revisited

As the report predicted, governance or "G" issues were a necessary precondition for shareholder activism around environmental and social issues. Indeed, shareholders efforts to secure governance rights ushered in several important governance practices that predate the intense focus on environmental and social issues. Importantly, those efforts were an essential precursor to the current rise in corporate attention on environmental and social concerns. Shareholders' ability to secure important governance rights set the stage for shareholders' ability to influence environmental and social issues by increasing their ability to exercise power over director elections and corporate affairs. This means that rather than being at odds with the "E" and the "S," the "G" has everything to do with them. The next section is a sampling of some of the core governance rights that paved the way for shareholders' ability to influence corporate matters associated with environmental and social concerns.

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[136] *See* Shlensky v. Wrigley, 237 N.E. 776, 781 (Ill. App. Ct. 1968) (courts have made clear that directors do not have to follow the practices or policies of other directors and corporations in order to comply with their fiduciary duty); *see also In re* Walt Disney Co. Derivative Litig., 906 A.2d 27, 56 (Del. Ch. 2003).

[137] *See In re* Walt Disney Co., 906 A.2d at 56.

[138] *See Aronson*, 473 A.2d at 811–12; *Unocal Corp.*, 493 A2d at 954; *see also* Fairfax, *supra* note 92, at 1334–36.

1. Board Declassification

Board declassification refers to the elimination of classified boards whereby directors on such boards are elected to staggered terms.[139] Classified boards ensure that shareholders cannot replace the entire board in one election cycle.[140] Shareholders have long viewed classified boards as an entrenchment device that insulates boards and undermines shareholders' ability to influence elections and corporate affairs.[141] While classified boards used to be the norm, shareholder activism has now resulted in some 86.3% of S&P 500 companies declassifying their board.[142]

2. Majority Voting

Majority voting refers to a director voting system whereby directors must receive a majority of the shareholder vote in order to be deemed elected.[143] Just over ten years ago, plurality voting was the norm.[144] Under plurality voting, directors are elected so long as they receive a plurality of shareholder votes, without regard to votes withheld or cast against them.[145] Under such a system, a director could be elected to the board even if a majority of shareholders voted against her. Shareholders vigorously fought to displace plurality voting with majority voting based on their belief that plurality voting undermined director accountability and responsiveness to shareholder concerns.[146] As a result of shareholder action, today over 90% of S&P 500 companies have adopted some form of majority voting.[147]

3. Supermajority Voting

Today, some 71% of S&P 500 companies have eliminated supermajority voting practices.[148] Such practices refer to voting rules that require more than a simple majority of shareholder votes, particularly in circumstances such as the adoption of bylaw amendments or the approval of fundamental transactions.[149] The elimination of supermajority voting enhances shareholder influence by making it easier to obtain the shareholder votes necessary to approve

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[139] *See* Fairfax, *supra* note 38, at 1316.
[140] *See id.*
[141] *See id.*
[142] *See* TONELLO, *supra* note 73.
[143] *See* Fairfax, *supra* note 48, at 1315–16.
[144] *See* TONELLO, *supra* note 73.
[145] *See* Fairfax, *supra* note 48, at 1315.
[146] *See id.* at 1316.
[147] *See* TONELLO, *supra* note 73.
[148] *See* SULLIVAN 2022 PROXY REVIEW, *supra* note 2, at 18.
[149] *See* Fairfax, *supra* note 48, at 1317.

important corporate transactions. While supermajority voting schemes used to dominate the public company landscape, shareholder action around this issue has led to simply majority structures becoming the norm.

4. Proxy Access

Proxy access refers to the ability of shareholders to nominate director candidates of their choice on the corporation's proxy statement. Shareholders have long sought to obtain proxy access based on the premise that the ability to have a cost-effective way to nominate candidates of their choice was crucial for ensuring that the shareholder vote meaningfully impacted director elections.[150] Prior to 2015, only a handful of companies had adopted proxy access.[151] By the end of 2019, 76% of S&P 500 companies had adopted proxy access, up from less than 1% in 2014.[152] The proxy access right has been referred to as the "holy grail" of shareholder rights, and thus sweeping adoption of proxy access represents a vital symbol of shareholders' increased power and influence over corporate affairs.[153]

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These governance practices paved the way for shareholders who are concerned about ESG to effectively advance such issues, tilting the balance in favor of shareholders.[154] Studies reveal that the adoption of these governance practices has made companies more responsive to shareholder interests.[155] Hence, the widespread adoption of these governance practices help explain *why* corporations and boards have done an about-face with respect to their shareholder interactions, particularly regarding environmental and social concerns.

B. "G" as the Engine Driving the "E" and "S"

Shareholders have used the governance rights they secured in connection with the "G" issues to advance the "E" and "S" issues. One survey found that the 2021 proxy season marked an escalation of shareholder engagement on ESG issues, as well as an expansion in the strategic use of governance tools to

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[150] *See id.*
[151] *See* Sidley Austin LLP, Proxy Access: A Five-Year Review 1 (2020), https://www.sidley.com/-/media/update-pdfs/2020/01/proxy-access/proxy-access_-a-fiveyear-review-jan-2020.pdf?la=en.
[152] *See id.* at 2.
[153] *See* Fairfax, *supra* note 63.
[154] *See* Lund & Pollman, *supra* note 12, at 2582.
[155] *See* Kobi Kastiel & Yaron Nili, *The Giant Shadow of Corporate Gadflies*, 94 S. Cal. L. Rev. 569, 586 (2021); Stephen Choi et al., *Does Majority Voting Improve Board Accountability?*, 83 U. Chi. L. Rev. 1119, 1129–34 (2016) (demonstrating that companies respond to shareholder interests after adoption of majority voting).

advance those issues.[156] Indeed, many shareholders have been explicit in their use of governance tactics to ensure progress around ESG. One particularly visible example comes from the New York City Pension Fund, a public pension fund known for its activism. The Fund launched several first-in-the-nation initiatives—referred to as Board Accountability Projects—that explicitly link the exercise of governance rights with the advancement of environmental and social issues.[157] As this action suggests, governance tools are a means to an end. And, for many shareholders, that end is linked to environmental and social goals. "There's a broader appreciation of the idea that good governance translates into better management of areas such as carbon footprint, as well as how management engages with the workforce."[158] The ensuing discussion highlights shareholder use of specific governance tools to prompt progress around environmental and social issues.

1. Proxy Access

Shareholders are using the power they received through proxy access to increase director accountability for ESG.[159] For example, the New York City Pension Fund has referred to the proxy access right as the "starting point" for advancing these important issues.[160] The Fund measured the success of its proxy access campaign based on its ability to ensure corporate responsiveness to important social issues, maintaining that the "increased . . . responsiveness provided by proxy access" has directly led to improved board diversity in terms of race and gender.[161] The Fund also noted that proxy access helps ensure that shareholders have a strong voice in the corporation so that they can focus corporate attention on issues such as "the company's approach to climate change risks, and treatment of employees."[162]

2. Voting Rights

Shareholders are using their increased voting power to advance environmental and social issues. ISS, the world's largest proxy advisor, recommended

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[156] *See* Julien Abriola et al., Institutional S'holder Serv., Climate & Voting: 2021 Review and Global Trends 4 (2021) (noting an expanded use of governance-related tactics to promote ESG, such as several ESG related vote-no campaigns, a rise in say on climate proposals, and a climate-related proxy contest).

[157] *See Overview, Board Accountability Project*, N.Y.C. Comptroller, https://comptroller.nyc.gov/services/financial-matters/boardroom-accountability-project/overview/ (last visited Sept. 23, 2023).

[158] *State Street Global Advisors Study*, *supra* note 117, at 6.

[159] *See* EY 2022 Proxy Season Preview, *supra* note 9, at 2.

[160] *See Overview, Board Accountability Project*, *supra* note 157.

[161] *See* Sidley Austin LLP, *supra* note 151.

[162] *See Overview, Board Accountability Project*, *supra* note 157.

that shareholders withhold the vote against directors for material failures to mitigate environmental, social and governance risks, such as significant environmental incidents or large-scale or repeated worker injuries or fatalities.[163] ISS also recommended voting against directors in circumstances in which a company is not doing enough to understand and mitigate risks related to climate change.[164] Similarly, BlackRock noted that it would consider voting against directors when there is insufficient oversight of material ESG risks.[165] In cases of ESG risk oversight failure, Vanguard will also generally vote against the chair of the committee responsible for overseeing material social and environmental risks.[166] These actions are not isolated to the largest shareholders and proxy advisors. Rather, a majority of shareholders anticipated that oversight of climate risk would play a more prominent role in their usage of voting rights in 2022 director elections.[167] According to one survey, 73% of shareholders indicated that ESG oversight would be an increasingly important factor in how they exercise their director vote in the 2022 proxy season.[168] Another survey found that shareholders planned to use more proactive voting strategies to hold boards accountable for ESG.[169]

Shareholders also have used their voting rights to focus attention on specific "E" and "S" issues. For example, BlackRock indicated that it may withhold support for directors if a company is not effectively addressing or disclosing material human rights-related risks or impacts.[170] BlackRock also noted that they may vote against directors responsible for human capital management decisions in the event of insufficient oversight disclosure.[171] Similarly, State Street indicated that it may vote against directors of companies with insufficient human capital management disclosure.[172]

The connection between shareholders' use of their increased governance power and "E" and "S" issues can particularly be seen with respect to board diversity. BlackRock has indicated that they may vote against members of the

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[163] *See* Institutional S'holder Serv., United States Sustainability Proxy Voting Guidelines 2023 Policy Recommendations 16–17 (2023) https://www.issgovernance.com/file/policy/active/specialty/Sustainability-US-Voting-Guidelines.pdf.

[164] *See* Tonello, *supra* note 68, at 8.

[165] *See id*. at 21.

[166] *See* Gibson, Dunn & Crutcher LLP, Blackrock, Vanguard and State Street Update Corporate Governance and ESG Policies and Priorities for 2022 4 (2022), https://www.gibsondunn.com/wp-content/uploads/2022/01/blackrock-vanguard-and-state-street-update-corporate-governance-and-esg-policies-and-priorities-for-2022.pdf.

[167] *See* EY 2022 Proxy Season Review, *supra* note 9, at 2.

[168] *See id.*

[169] *See* EY 2022 Proxy Season Review, *supra* note 9, at 3.

[170] *See* BlackRock, Our Approach to Engagement on Corporate Human Rights Risks 2 (2023), https://www.blackrock.com/corporate/literature/publication/blk-commentary-engagement-on-human-rights.pdf.

[171] *See* Shawn Bisman & Felipe Cambeiro, *Big Three Institutional Investors*, Harv. L. Sch. F. on Corp. Governance (Apr. 13, 2022), https://corpgov.law.harvard.edu/2022/04/13/__trashed/.

[172] *See id.*

nominating committee for any perceived lack of commitment to board diversity.[173] Vanguard also noted that they may withhold the vote from the chair of the nominating committee when there is insufficient progress on board diversity or board diversity disclosures.[174] State Street similarly indicated that they may vote against the nominating committee chair when there is no disclosure on the board's racial and ethnic composition or the board does not have at least one director from an underrepresented racial or ethnic community.[175] State Street also noted that they may withhold votes against companies that do not have at least one female director.[176] Additionality, beginning in 2023, State Street may vote against the nominating committee chair of Russell 3000 companies if they do not have at least 30% female directors.[177]

While the application of these policies is discretionary and on a case-by-case basis, it is clear that shareholders are, in fact, acting on their ability to use their vote in connection with ESG. In 2019, BlackRock withheld votes or voted against 4,800 directors at 2,700 companies who they believed were not addressing critical ESG issues.[178] Insufficient board diversity was a top reason BlackRock withheld its vote against directors in 2021.[179] BlackRock's Stewardship Report stated that it has voted against 255 directors for climate-related reasons, up from votes against only 55 directors in 2020.[180] This behavior is not isolated to BlackRock.[181] Thus, studies reveal a link between directors receiving less than majority support and weak records on environmental and social issues.[182] In addition, lack of board diversity was a factor in at least 12% of cases where directors received less than majority shareholder support.[183]

3. Activist Campaigns

There has also been a surge in activist campaigns associated with environmental and social issues.[184] Such campaigns grew from 2% of all campaigns in 2018 to 12% in 2020.[185] Importantly, changes in supermajority voting rules

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[173] *See id.*
[174] *See id.*
[175] *See* State Street Global Advisors, *supra* note 116, at 2.
[176] *See* Gibson, Dunn & Crutcher LLP, *supra* note 166, at 8.
[177] *See id.*
[178] *See* Fink, *supra* note 113.
[179] *See* Gibson, Dunn & Crutcher LLP, *supra* note 166, at 2.
[180] *See* Cydney Posner, *Blackrock Flexes Its Muscles During the 2020–21 Proxy Period*, Harv. L. Sch. F. on Corp. Governance (Aug. 16, 2021), https://corpgov.law.harvard.edu/2021/08/16/blackrock-flexes-its-muscles-during-the-2020-21-proxy-period/.
[181] *See* Tonello, *supra* note 73.
[182] *See id.*; Mattison, *supra* note 1 (noting rise in votes against directors for lack of credible climate action plans).
[183] *See* PwC Governance Insights, *supra* note 76, at 5.
[184] *See* Mattison, *supra* note 1.
[185] *See id.*

increase the ability of shareholders to take over a company, thereby increasing their ability to use M&A tactics to influence corporate behavior around environmental and social issues. Board declassification similarly enhances shareholder power around M&A activity by enhancing the ability to gain control of the board. Hence, governance change also facilitates the ability to use shareholder activism as a mechanism for impacting environmental and social concerns. Of course, activist campaigns are often viewed as antithetical to environmental and social issues because they are seen as driven by a desire to extract profits from the corporation at the expense of employee stability and other stakeholder concerns.[186] On the one hand, this reality underscores the fact that not all exercises of shareholder power benefit other stakeholders. On the other hand, the fact that even activist campaigns are being used by shareholders to advance ESG further underscores the way ESG has influenced the shareholder and corporate landscape.

To be sure, not all shareholders are using their newfound governance power to advance environmental and social goals. For example, in 2022 there was an increase in the number of proposals submitted by anti-ESG groups.[187] Such groups submit proposals aimed at undermining ESG by questioning workplace diversity metrics, training, and policies or urging corporations to assess the cost and benefits of ESG activities related to climate change, civil rights or racial equity audits, or other environmental and social issues.[188] The rise in these proposals confirms that some shareholders have used their governance power to thwart ESG.

However, most shareholders have been using their power to support ESG. This is evident from the record-breaking number of submissions for environmental and social proposals, alongside the increased amount of shareholder support for those proposals, with many receiving majority shareholder support for the first time in history.[189] Anti-ESG proposals, in contrast, receive significantly lower shareholder support than proposals seeking to advance ESG.[190] This divergence can really be seen when shareholders must make a choice between supporting ESG issues and undermining those issues. For example, shareholders at Johnson and Johnson supported racial equity proposals with 63% of votes cast, but a proposal associated with questioning the appropriateness of a civil rights audit from an anti-ESG group received only 2.7% of the votes cast.[191] Thus, when confronted with a pro- and anti-ESG proposal on the same topic, shareholders overwhelmingly supported the proposal aimed

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[186] *See generally* Lynn A. Stout, *The Toxic Side Effects of Shareholder Primacy*, 161 U. Pa. L. Rev. 2003 (2013).

[187] *See* Sullivan 2022 Proxy Review, *supra* note 2, at 5–6.

[188] *See id.* at 6.

[189] *See id.* at 1.

[190] *See id.* at 5.

[191] *See id.* at 12.

at advancing ESG. These results highlight the strong shareholder support for ESG issues. Moreover, this example is yet another instance in which shareholder governance rights are being used to advance environmental and social concerns.

C. The Reconceptualization

The focus on "G" in the context of ESG also has had a pivotal impact on the reconceptualization of governance. In modern times, governance has been closely associated with advancing shareholder power. As Professors Dorothy Lund and Elizabeth Pollman note in their article *Corporate Governance Machine*, good corporate governance has become inextricably linked to shareholder primacy.[192] This link permeates all aspects of the corporate law and securities arena. Delaware law equates good governance with maximizing shareholder value.[193] When Congress adopts corporate governance regulations, those regulations inevitably focus on augmenting shareholder power.[194] The SEC's corporate governance rules similarly focus on enhancing shareholder power or protecting shareholders.[195] In other words, good corporate governance has become synonymous with maximizing shareholder welfare.[196]

However, governance and corporate governance were not intended to be tethered solely to shareholders and augmenting their power; instead, governance and corporate governance have a much broader focus of ensuring accountability for all corporate activities. Governance refers to establishing a system of internal checks and balances to control and direct the exercise of power.[197] In other words, governance is associated with accountability. Good governance involves the creation and implementation of goals, targets, policies, practices, and procedures that ensure appropriate oversight and accountability. Corporate governance relates to establishing internal constraints on corporate power through the use of such metrics.[198] As one commentator notes, good corporate governance requires companies to look inward and "become watchdogs of their own performance."[199] Because the board represents a primary source of accountability within the corporate sphere, good corporate

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[192] *See* Lund & Pollman, *supra* note 12, at 2576–78 ("good governance" linked to aligning corporate policies and practices with quarterly earnings and investor expectations).

[193] *See* Leo E. Strine Jr., *The Dangers of Denial: The Need for a Clear-Eyed Understanding of the Power and Accountability Structure Established by the Delaware General Corporation Law*, 50 Wake Forest L. Rev. 761, 768 (2015).

[194] *See* Lund & Pollman, *supra* note 12, at 2582.

[195] *See id.* at 2585.

[196] *See id.* at 2574–76.

[197] *See* Larcker et al., *supra* note 1, at 875; Lund & Pollman, *supra* note 12, at 2572–73; Mariana Pargendler, *The Corporate Governance Obsession*, 42 J. Corp. L. 359, 375 (2016).

[198] *See* Lund & Pollman*, supra* note 12, at 2572.

[199] *See* Sierra, *supra* note 10.

governance transforms the board into an internal auditor with responsibility for implementing practices and procedures that constrain corporate power and hold officers and directors accountable for their corporate commitments.[200] As this suggests, good corporate governance is not intended to be simply about shareholders and their power, but instead is aimed at ensuring appropriate governance practices for any corporate issue.

Shareholders have been instrumental in refocusing governance to align with this original intent. Thus, shareholders have focused on governance not simply as a mechanism for advancing their own power and voice, but also as a vehicle for holding corporations responsible for their commitments beyond shareholders. In particular, shareholders have refocused governance to push for greater board oversight of environmental and social issues, more specific environmental and social disclosure, and the adoption of specific environmental and social targets and goals.[201] In 2022, environmental proposals around specific targets and goals represented the largest number of submitted shareholder proposals.[202] These proposals also received the largest average shareholder votes and were the most likely to receive majority shareholder support.[203] Such proposals also were withdrawn at high rates, which is an indication that companies have agreed to adopt environmental target or goals.[204] In 2021 there were 19 withhold-the-vote campaigns targeting companies that failed to implement specific climate-related plans consistent with their climate commitments.[205]

Outside of the shareholder proposal context, the largest shareholders have prioritized the importance of governance targets and goals for corporations. Vanguard's stewardship principles now emphasize its support for metrics and targets related to climate and DEI.[206] State Street has articulated its governance expectations in a multitude of ways, indicating its expectation that companies establish time-bound goals, the policies and programs in place to meet those goals, and the way they are "measured, managed and progressing."[207] State Street has also urged corporations to clearly articulate plans for oversight of important social issues.[208] In the context of racial equity, for example, State

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[200] *See* Ralph Nader et al., Taming the Giant Corporation: How the Largest Corporations Control Our Lives 119 (1976); Lund & Pollman, *supra* note 12, at 2572.

[201] *See* Mattison, *supra* note 1 (noting that companies will face increase pressure from shareholders and stakeholders to develop "concrete, near term plans" for their ESG commitments).

[202] *See* Sullivan 2022 Proxy Review, *supra* note 2, at 24 (similarly, in 2021, the vast majority of environmental shareholder proposals focused on encouraging companies to adopt climate targets); Julien Abriola et al., *supra* note 156, at 6 (shareholders have focused on targets aligned with net-zero pledges and goals); *id.*

[203] *See* Sullivan 2022 Proxy Review, *supra* note 2, at 24.

[204] *See id.* at 26.

[205] *See* Julien Abriola et al., *supra* note 156, at 6.

[206] *See* Vanguard, *supra* note 59, at 7.

[207] *See* State Street Global Advisors, *supra* note 116, at 1.

[208] *See* Sullivan 2022 Proxy Review, *supra* note 2, at 10; *id.* at 4 (focused on process for oversight of diversity issues).

Street has voiced an expectation for companies to clearly articulate and disclose the board's process for overseeing risks related to racial equity and civil rights and its plan for addressing these risks.[209] As a result of this focus, corporations are being advised to "identify specific, quantifiable ESG-related measures that are aligned with the company's corporate purpose and culture, and be prepared to demonstrate how these measures inform the company's plans for growth and financial performance."[210] This focus on governance in relation to environmental and social issues reflects a reconstitution of governance.

This focus is also a recognition that good governance practices are essential for transforming rhetoric into reality, and thus, it is the letter "G" that has the best potential for ensuring that corporations will actually make real on their commitments related to the "E" and the "S."[211] Shareholders focus on governance because they "want to see companies back up bold pronouncements and long-term commitments with short-term, interim goals, clear reporting on progress and direct board oversight."[212] Shareholders have made clear that corporate pronouncements around environmental and social matters lack value without governance goals and targets.[213] Shareholders have expressed the view that companies must set concrete goals and timelines in order to be taken seriously.[214] Governance is especially important in the context of environmental and social goals because of the long-term nature of many of those goals. Setting specific targets allows for year-to-year comparisons to assess forward progress. As Vanguard notes, "target setting allows for progress checks across many years."[215] A proxy survey summarized the focus on governance in this way: "This year, investors expressed a growing skepticism of broad pronouncements that lack specific detail and a deeper focus on how company actions and practices across a multitude of dimensions align with company's public commitments and values."[216] In other words, shareholders have begun to realize what the originators of ESG did—governance measures are critical for ensuring effective implementation of environmental and social commitments.

In the context of ESG, we are therefore witnessing a revitalization of the original intent of governance. Shareholders are playing a pivotal role in this revitalization because they have been on the frontlines of encouraging

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[209] *See* State Street Global Advisors, *supra* note 116, at 4.

[210] *See* Tsu & Chapman, *supra* note 1.

[211] *See* Mattison, *supra* note 1 (noting that expectations to develop specific plans with respect to ESG commitments stems from the desire to hold entities "accountable to their commitments").

[212] *See* EY 2022 Proxy Season Preview, *supra* note 9, at 1.

[213] *See id.* at 6.

[214] *See* Press Release, N.Y.C. Comptroller, *NYC Comptroller Lander and City Pension Funds Call on Major U.S. and Canadian Banks to Set Absolute GHG Emissions Targets for High Emitting Sectors* (Jan. 24, 2023), https://comptroller.nyc.gov/newsroom/absolute-ghg-emissions-reduction-proposal/.

[215] *See* Vanguard, *supra* note 59, at 8.

[216] *See* EY 2022 Proxy Season Preview, *supra* note 9, at 6.

corporations to implement governance practices around these "E" and "S" issues. In this way, shareholders have been the primary advocates for ensuring that the "G" relates to ensuring meaningful accountability around the "E" and the "S." Instead of further entrenching governance into the realm of shareholder primacy, ESG has served to reconceptualize governance as a vital means of ensuring effective compliance with corporate commitments, including, of course, commitments related to environmental and social issues.

IV. Conclusion

In a recent article in the Harvard Business Review, Former Delaware Supreme Court Justice Leo Strine and his colleagues penned an article entitled: *It's Time to Focus on the "G" in ESG*.[217] The article was aimed at calling out shareholders to ensure that their own corporate governance practices are aligned with the environmental and social goals they profess to support.[218] However, the article's title highlights the core theme of this article. This article strenuously insists that rather than distance the "G" from ESG, it is imperative that we focus on the "G." Like those who coined ESG, this article contends that effective governance policies and practices have the best chance of facilitating long-term corporate focus on disclosing, monitoring, and addressing environmental and social concerns. This article also insists that the "G" has the best chance of ensuring that corporate attention on the "E" and "S" does not stray from fiduciary obligations. In this respect, an appropriate focus on the "G" is the solution for concerns animating both sides of the ideological debate.

This article does not seek to paint shareholders as perfect, or even as perfect ambassadors for other stakeholders. Shareholder behavior can be just as problematic as any other individual or entity. Moreover, shareholders do not have monolithic interests, which means that there are shareholders who seek to ignore ESG, and other stakeholders, as well as shareholders, intent on actively thwarting any effort to promote ESG. Finally, there are natural limits to shareholder power, as well as inevitable limits on shareholders' willingness to exercise their power, in favor of other groups.

However, it would be a mistake to discount the outsized role shareholders have played in advancing the ESG agenda. We double down on that mistake by failing to acknowledge the pivotal role of the "G" in moving the "E" and the "S" forward. Shareholder empowerment via an array of governance changes has been the primary driver of the increasing corporate focus on environmental and social policies and practices. More importantly, shareholders

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[217] *See* Leo Strine et al., *It's Time to Focus on the "G" in ESG*, Harv. Bus. Rev. (Nov. 18, 2022), https://hbr.org/2022/11/its-time-to-focus-on-the-g-in-esg.

[218] *See id.*

have been instrumental in ensuring that their newly enacted corporate governance policies and practices do not simply revolve around amplifying shareholder power, but instead serve to transform corporations' relatively vague environmental and social commitments into concrete plans and measurable goals. That is, shareholders have encouraged corporations to use governance as an accountability tool for the full range of commitments embedded in ESG, leading to a more appropriate realignment of our understanding of good corporate governance.