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The Conflict Between BlackRock's Shareholder Activism and ERISA's Fiduciary Duties

Bernard S. Sharfman

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THE CONFLICT BETWEEN BLACKROCK'S SHAREHOLDER ACTIVISM AND ERISA'S FIDUCIARY DUTIES

Bernard S. Sharfman[†]

ABSTRACT

The focus of this Article is on the agency costs that may be created by the empty voting of investment advisers to index funds and how they can be mitigated so as to protect the value of private employee pension benefit plans. This Article focuses on BlackRock because it has taken a leadership role in the leveraging of its delegated voting authority. Therefore, the issue I address in this Article is whether the fiduciary duties of a plan manager of an “employee pension benefit plan,” as authorized under the Employee Retirement Income Security Act of 1974 (“ERISA”), requires it to investigate BlackRock’s shareholder activism. This indirect approach is required as the fiduciary duties of ERISA do not generally extend to mutual funds and ETFs and their investment advisors.

This Article takes the position that a plan manager has a fiduciary duty, the duty of prudence, to investigate BlackRock’s shareholder activism. This duty applies not only to BlackRock’s mutual funds or ETFs that an ERISA plan invests in but also to those BlackRock fund selections that it makes available to its participants and beneficiaries in self-directed accounts.

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Given these fiduciary duties, this Article argues that if a plan manager were to investigate BlackRock's shareholder activism, especially its engagement strategy, it would likely find it to be in conflict with the manager's fiduciary duties. Such a finding would require a plan manager to seek out other reasonably available alternatives that are not associated with such shareholder activism.

While the focus of this Article is on BlackRock's delegated voting authority and associated shareholder activism, it is meant to apply to any and all investment advisers who attempt to leverage their delegated voting authority for purposes of engaging in such activism. Moreover, the Department of Labor should provide guidance to plan managers on when the investment products of investment advisers with delegated voting authority need to be excluded.

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INTRODUCTION

The world is full of surprises. One of those surprises is that BlackRock, Inc. (“BlackRock”), an investment adviser¹ that primarily markets and manages index funds to millions of passive investors around the globe, has become a leading shareholder activist. Based on the extremely large amount of assets it has under management, approximately \$7.3 trillion with approximately \$3.5 trillion of that being the common stock of publicly traded companies,² its importance as an activist cannot be overstated.

BlackRock and its major index-fund rivals Vanguard and State Street Global Advisors (the “Big Three”), have an enormous amount of proxy voting power. According to Bebchuk and Hirst, as of 2017 BlackRock held in its managed portfolio a 5% or more position in 488 out of the 500 common stocks that make up the S&P 500, Vanguard had such a position in all 500 companies, and State Street Global Advisors in 130.³ According to Fichtner, Heemskerk, and Garcia-Bernardo, as of March 2016 BlackRock had a 5% or more position in about 2,000 out of the approximately 3,900 U.S. publicly listed companies then existing, Vanguard had such a position in 1,750 such companies, and State Street Global Advisors in 260 companies.⁴

Yet this voting power actually understates the size of the Big Three’s voting influence; the reason being that they vote virtually all of the shares they manage while other investor types, such as retail investors, do not. For example, Brav, Cain, and Zytnick, over the time period 2015 to 2017, found that while retail investors held approximately 26% of the shares in their sample, they only cast a ballot 32% of the time.⁵ This explains Bebchuk and Hirst’s findings that while

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1. 15 U.S.C. 80b–2(a)(11) (2018) (defining “Investment adviser” as a person who “engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities . . .”).
 2. BlackRock, Inc., Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 (Form 10-Q) 46 (Aug. 7, 2020).
 3. Lucian Bebchuk & Scott Hirst, *The Specter of the Giant Three*, 99 B.U. L. REV. 721, 735, tbl.4 (2019).
 4. Jan Fichtner, Eelke M. Heemskerk & Javier Garcia-Bernardo, *Hidden Power of the Big Three? Passive Index Funds, Re-Concentration of Corporate Ownership, and New Financial Risk*, 19 BUS. & POL. 298, 311–12 (2017).
 5. Alon Brav, Matthew D. Cain & Jonathon Zytnick, *Retail Shareholder Participation in the Proxy Process: Monitoring, Engagement, and Voting*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Nov. 19, 2019), <https://corp>

on average the Big Three controlled 20.5% of shares of the companies that make up the S&P 500, they cast a combined 25.4% of the proxy votes.⁶ Bebchuk and Hirst also estimated that Vanguard had an average voting influence of 11.1%, BlackRock 8.7%, and State Street 5.6%.⁷ Consistent with Bebchuk and Hirst, Caleb Griffin finds that while the Big Three control approximately 20.1% of shares at the largest 250 publicly traded companies in the U.S., they cast a combined 25% of the proxy votes.⁸ He further estimated that Vanguard had an average voting influence of 10.6%, BlackRock 9.0%, and State Street 5.4%.⁹

What has allowed the Big Three to become such large players in proxy voting? Basically, it is a combination of the strong investor interest in such index funds combined with how these funds have been traditionally managed. It begins when an individual investor or institution (beneficial investor) decides to invest in an index mutual fund or exchange traded fund (“ETF”) that predominately invests in equity securities—for example, a fund that invests in equities that make up the S&P 500. This decision usually means that the beneficial investor is delegating its shareholder voting to the index fund, a common industry practice which relieves the beneficial investor of having to worry about shareholder voting. And the delegation of voting authority does not stop there. The mutual fund or ETF will then turn around and delegate its voting authority to the fund’s investment adviser, the adviser that is responsible for managing the fund’s portfolio of investments.

These standard practices, combined with the large movement of assets into the index funds of a relatively small number of investment advisers, has resulted in a concentration of voting power. But what is most striking about this arrangement is that the investment advisers to the funds have no economic interest in the underlying securities. This “decoupling” or “unbundling” of voting interests from economic interests in the context of shareholder voting is referred to as “empty

gov.law.harvard.edu/2019/11/19/retail-shareholder-participation/ [https://perma.cc/6K25-ST8H].

6. Bebchuk & Hirst, *supra* note 3, at 736, tbl.5.
7. *Id.*
8. Caleb N. Griffin, *Margins: Estimating the Influence of the Big Three on Shareholder Proposals*, 73 SMU L. REV. 409, 418 tbl.1 (2020).
9. *Id.* While it is beyond the scope of this Article, it should be noted that the voting power and influence of a Big Three member would be amplified if two or more of the Big Three had similar marketing and engagement strategies. In sum, an uncoordinated wolf pack would be created.

voting.”¹⁰—here, the empty voting of investment advisers to index mutual funds and ETFs.¹¹

Empty voting creates a potential misalignment between the interests of voters (investment advisers to index mutual funds and ETFs) and the residual risk bearers (beneficial investors that own shares in the index mutual funds and ETFs) and therefore creates the potential for agency costs¹²—more precisely, what Gilson and Gordon would call “the agency costs of agency capitalism.”¹³ In the case of investment advisers to index funds, these agency costs come in two flavors. The first are “passive” agency costs.¹⁴ These costs refer to the economic disincentives investment advisers to index funds have in becoming informed about the investments they manage, including when they vote their proxies.¹⁵ The second are “proactive” agency costs.¹⁶ These costs refer to the economic incentives investment advisers have to leverage their delegated voting authority for their own gain.¹⁷

Moreover, BlackRock, like the other members of the Big Three, has centralized this enormous voting authority and influence into the hands of a small group of individuals, its investment stewardship team. This allows BlackRock to aggregate shareholder voting across a myriad of funds for purposes of taking advantage of economies of scale and cost

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10. Henry T. C. Hu, *Financial Innovation and Governance Mechanisms: The Evolution of Decoupling and Transparency*, 70 BUS. LAW. 347, 355 (2015).
 11. See Bernard S. Sharfman, *Mutual Fund Advisors' "Empty Voting" Raises New Governance Issues*, COLUM. L. SCH.: BLUE SKY BLOG (July 3, 2017), <http://clsbluesky.law.columbia.edu/2017/07/03/mutual-fund-advisors-empty-voting-raises-new-governance-issues> [https://perma.cc/5KLJ-42M8].
 12. See Jill E. Fisch, *Securities Intermediaries and the Separation of Ownership from Control*, 33 SEATTLE U. L. REV. 877, 884 (2010) (“The existence of additional agency costs within the intermediary structure offers reason to question the proposition that institutional investors can improve corporate decision-making by more active participation in corporate governance.”).
 13. Ronald J. Gilson & Jeffrey N. Gordon, *The Agency Costs of Agency Capitalism: Activist Investors and the Revaluation of Governance Rights*, 113 COLUM. L. REV. 863, 889 (2013).
 14. Bernard S. Sharfman, *How the SEC Can Help Mitigate the "Proactive" Agency Costs of Agency Capitalism*, 8 AM. U. BUS. L. REV. 1, 4 (2019).
 15. See Lucian Bebchuk & Scott Hirst, *Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy*, 119 COLUM. L. REV. 2029, 2039 (2019); Lucian A. Bebchuk, Alma Cohen & Scott Hirst, *The Agency Problems of Institutional Investors*, 31 J. ECON. PERSPS. 89, 95 (2017); Gilson & Gordon, *supra* note 13, at 889–95.
 16. Sharfman, *supra* note 14, at 3.
 17. *Id.*

minimization. Its team is made up of forty-five professionals globally, with twenty-two based in the U.S. (twelve are global, and ten are local), who are, on an annual basis, responsible for the voting of tens of thousands of proxies and engaging on various matters with the management of hundreds of publicly traded companies.¹⁸ Therefore, at many public companies, BlackRock's investment stewardship team, like its chief rivals, "may now control the fate of a shareholder or management proposal, whether a nominated director receives a required majority of votes to remain on the board of directors, or if a proxy contest succeeds or fails."¹⁹

BlackRock's creation of an investment stewardship team also allows it to coordinate its shareholder activism based not only on popular corporate governance principles but also on its own company objectives. This activism is reflected in its rhetoric disclosing the objectives of its activism and the engagement strategy that it intends to use to achieve its objectives, shareholder voting, and engagement with portfolio companies. As subsequently discussed, such activism contains elements of both passive and proactive agency costs that may be harmful to both beneficial investors and public companies.

The focus of this Article is on the agency costs that may be created by the empty voting of investment advisers to index funds and how they can be mitigated so as to protect the value of private employee pension benefit plans. This Article focuses on BlackRock because it has taken a leadership role in the leveraging of its delegated voting authority. Therefore, the issue I address in this Article is whether the fiduciary duties of a plan manager of an "employee pension benefit plan," as authorized under the Employee Retirement Income Security Act of 1974 ("ERISA"),²⁰ requires it to investigate BlackRock's shareholder activism. This indirect approach is required as the fiduciary duties of ERISA do not generally extend to mutual funds and ETFs and their investment advisors.

A plan manager (trustees who retain investment and voting authority or "investment managers"²¹ that receive such authority through delegation by the trustees) of an "employee pension benefit

18. *Investment Stewardship Annual Report*, BLACKROCK 25, 68 (Sept. 2020), <https://www.blackrock.com/corporate/literature/publication/blk-annual-stewardship-report-2020.pdf> [<https://perma.cc/XE6U-4S2V>].

19. Sharfman, *supra* note 14, at 13.

20. Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, 88 Stat. 829 (codified as amended at 29 U.S.C. § 1001 *et seq.* (2012)).

21. *See* 29 U.S.C. § 1002(38).

plan²² owes a duty of loyalty²³ to participants²⁴ and beneficiaries.²⁵ A plan manager also has a duty of prudence.²⁶ This latter duty requires a plan manager to perform a careful and impartial investigation prior to making an investment decision. How these duties affect a plan manager's evaluation of an investment adviser's shareholder activism has been little examined in the academic literature. Yet the time is ripe for its study because the shareholder voting power of our public companies is now so concentrated in the hands of a small number of investment advisers.

This Article takes the position that a plan manager's fiduciary duties require it to investigate BlackRock's shareholder activism. These duties apply not only to the BlackRock mutual funds or ETFs that an ERISA plan invests in, but also to those BlackRock fund selections that it makes available to its participants and beneficiaries in self-directed accounts. This Article also argues that a plan manager, after investigating BlackRock's engagement strategy, could reasonably conclude that it is financially harmful to its plan and decide to seek out "reasonably available alternatives"²⁷ that are not associated with such an engagement strategy.

Part I of this Article discusses BlackRock's rhetoric and how it has been used to disclose the company's primary objective in its shareholder activism—the marketing of its investment products to millennials—and

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22. *See id.* § 1002(2)(A) (“[T]he terms ‘employee pension benefit plan’ and ‘pension plan’ mean any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that by its express terms or as a result of surrounding circumstances such plan, fund, or program—(i) provides retirement income to employees, or (ii) results in a deferral of income by employees for periods extending to the termination of covered employment or beyond . . .”).
 23. *See id.* § 1104(a)(1) (explaining that a fiduciary must “discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries”).
 24. *See id.* § 1002(7) (“The term ‘participant’ means any employee or former employee of an employer, or any member or former member of an employee organization, who is or may become eligible to receive a benefit of any type from an employee benefit plan which covers employees of such employer or members of such organization, or whose beneficiaries may be eligible to receive any such benefit.”).
 25. *See id.* § 1002(8) (“The term ‘beneficiary’ means a person designated by a participant, or by the terms of an employee benefit plan, who is or may become entitled to a benefit thereunder”).
 26. *See id.* § 1104(a)(1)(B); ERISA, Pub. L. No. 93-406, § 404(a)(1)(B), 88 Stat. 829, 877.
 27. Financial Factors in Selecting Plan Investments, 85 Fed. Reg. 72,846, 72,848 (Nov. 13, 2020) (to be codified at 29 C.F.R. pts. 2509 and 2550).

how it plans to engage with its portfolio companies. Part II describes BlackRock's voting and engagement record. Part III explains the fiduciary duties of ERISA. Part IV discusses how ERISA's fiduciary duties are to be applied to BlackRock's index funds. This Part proposes a new rule under ERISA: A plan manager, when selecting [index] mutual funds and ETFs for direct ownership or availability to self-directed accounts and in the general monitoring of plan's ongoing investment in these funds, has a fiduciary duty to investigate an investment adviser's [BlackRock's] shareholder activism. Part V applies this new rule to BlackRock's shareholder activism.

While the focus of this paper is on BlackRock's delegated voting authority and associated shareholder activism, it is meant to apply to any and all investment advisers who attempt to leverage their delegated voting authority for purposes of engaging in shareholder activism. Moreover, the Department of Labor ("DOL") should provide guidance to plan managers on when the investment products of investment advisers with delegated voting authority need to be excluded.

I. BLACKROCK'S RHETORIC

Through its rhetoric BlackRock has revealed: 1) its primary objective: the marketing of its investment products to millennials; 2) how that objective is going to impact its engagement strategy: a focus on advocating for stakeholders that millennials believe are most deserving; and 3) how shareholder voting will be used to persuade portfolio companies that its advocacy needs to be implemented: voting against management when management does not comply.

A. *A Focus on Stakeholders*

For some time, Larry Fink (CEO of BlackRock) has been signaling to the management of public companies and BlackRock's competitors—Vanguard, State Street Global Advisors, Fidelity, etc.—that BlackRock was going to use its huge amount of delegated voting authority to become one of the world's largest shareholder activists, advocating for *all stakeholders*, not just shareholders. These stakeholders include shareholders, directors, managers, employees, independent contractors, consultants, consumers, creditors, vendors, distributors, communities affected by the company's operations, federal, state, and local governments, and society in general, when it is positively affected by the social value created by the company or negatively affected when the company generates third-party costs such as air or water pollution.

In Fink's 2018 letter to CEOs, he set the stage for his stakeholder approach:

We also see many governments failing to prepare for the future, on issues ranging from retirement and infrastructure to auto-

mation and worker retraining. As a result, society increasingly is turning to the private sector and asking that companies respond to broader societal challenges. Indeed, the public expectations of your company have never been greater. Society is demanding that companies, both public and private, serve a *social purpose*. To prosper over time, every company must not only deliver financial performance, but also show how it makes a positive contribution to society. *Companies must benefit all of their stakeholders*, including shareholders, employees, customers, and the communities in which they operate.²⁸

In this context, “social purpose” seems to mean something much different than simply having the purpose of producing those goods and services that consumers or other companies value. Fink also wants to focus on the interests of all stakeholders, not just shareholders. The reason for the latter was not explained until Fink’s 2019 letter to CEOs.

*B. The Primary Objective: Marketing BlackRock's
Investment Products to Millennials*

In Fink’s 2019 letter to CEOs, he explained what BlackRock’s new focus on “social purpose” and “benefiting all stakeholders” was all about: the marketing of its investment products to millennials, a demographic group that is expected to inherit trillions of dollars of wealth from its baby boomer parents.²⁹

28. Larry Fink, *Larry Fink's 2018 Letter to CEOs: A Sense of Purpose*, BLACKROCK, <https://www.blackrock.com/corporate/investor-relations/2018-larry-fink-ceo-letter> [<https://perma.cc/PU37-ZE8C>] (emphases added) (last visited Apr. 6, 2021).

29. It can be argued that marketing to millennials is not BlackRock’s only objective. Secondary objectives include BlackRock using its shareholder activism to appease its own shareholders who are upset with BlackRock’s management practices. For example, in 2019, Boston Trust Walden and Mercy Investment Services submitted a shareholder proposal to BlackRock demanding that it provide a review explaining why its climate-change rhetoric does not correspond with how it actually votes at shareholder meetings. See *BlackRock, Vanguard Face Shareholder Rebuke over Climate Votes*, PENSIONS & INVS. (Dec. 13, 2019), <https://www.pionline.com/governance/blackrock-vanguard-face-shareholder-rebuke-over-climate-votes> [<https://perma.cc/7WMC-LEGR>]. The proposal was reportedly withdrawn after BlackRock agreed to give increased consideration to shareholder proposals on climate change and join Climate Action 100+, an investor group that targets its shareholder activism at fossil fuel producers and greenhouse gas emitters. *Blackrock and JP Morgan Spared ESG Voting Proposals Following Sustainability Pushes*, RESPONSIBLE INV. (Mar. 10, 2020), https://www.bostontrustwalden.com/wp-content/uploads/2020/03/Blackrock-and-JP-Morgan-spared-ESG-voting-proposals-following-sustainability-pushes_.pdf [<https://perma.cc/E3D3-NRQT>]. Or, non-shareholder activists who have a belief that BlackRock is creating harm. For example,

According to BlackRock, millennials, more so than prior generations, see the primary objective of business to be the improvement of society, not the generation of profits:³⁰

Companies that fulfill their purpose and responsibilities to stakeholders reap rewards over the long-term. Companies that ignore them stumble and fail. This dynamic is becoming increasingly apparent as the public holds companies to more exacting standards. And it will continue to accelerate as *millennials*—who today represent 35 percent of the workforce—express new expectations of the companies they work for, buy from, and invest in.

. . . Over the past year, we have seen some of the world's most skilled employees stage walkouts and participate in contentious town halls, expressing their perspective on the importance of corporate purpose. This phenomenon will only grow as millennials and even younger generations occupy increasingly senior positions in business. In a recent survey by Deloitte, *millennial* workers were asked what the *primary purpose* of businesses should be—63 percent more of them said “improving society” than said “generating profit.”

In the years to come, the sentiments of these generations will drive not only their decisions as employees but also as investors,

there is an organization called BlackRock's Big Problem, which is a worldwide group of NGOs and “financial advocates that are pressuring asset managers like BlackRock” to adjust their climate practices. *About, BLACKROCK'S BIG PROBLEM*, <https://www.blackrocksbigproblem.com/about> [<https://perma.cc/WJG7-CUZH>] (last visited Apr. 6, 2021). Finally, BlackRock can use its shareholder activism to mitigate political pressure. For example, five U.S. senators recently sent a letter to BlackRock criticizing how it votes on shareholder proposals involving climate change and political spending disclosures. While it is beyond the scope of this Article to explore further, buckling under this pressure would appear to violate the fiduciary duties BlackRock owes to its mutual funds and ETFs and their beneficial investors. *See* Letter from Brian Schatz, U.S. Sen., Sheldon Whitehouse, U.S. Sen., Tammy Baldwin, U.S. Sen., Elizabeth Warren, U.S. Sen. & Martin Heinrich, U.S. Sen., to Larry Fink, CEO of Blackrock (Oct. 8, 2020), [https://www.schatz.senate.gov/imo/media/doc/Letter%20to%20BlackRock%20on%202020%20proxy%20voting%20rec ord_2020.10.08.pdf](https://www.schatz.senate.gov/imo/media/doc/Letter%20to%20BlackRock%20on%202020%20proxy%20voting%20record_2020.10.08.pdf) [<https://perma.cc/HG25-NXDX>].

30. Larry Fink, *Larry Fink's 2019 Letter to CEOs: Purpose & Profit*, BLACKROCK, <https://www.blackrock.com/corporate/investor-relations/2019-larry-fink-ceo-letter> [<https://perma.cc/T2ZV-H7YJ>] (last visited Mar. 27, 2021). This letter was apparently the inspiration for Michal Barzuza, Quinn Curtis, and David H. Webber's recent article, *Shareholder Value(s): Index Fund ESG Activism and the New Millennial Corporate Governance*, 93 S. CAL. L. REV. 1243, 1246 (2020).

with the world undergoing *the largest transfer of wealth in history: \$24 trillion from baby boomers to millennials*. As wealth shifts and investing preferences change, *environmental, social, and governance issues* [ESG] will be increasingly material to corporate valuations. This is one of the reasons why BlackRock devotes considerable resources to improving the data and analytics for measuring these factors, integrates them across our entire investment platform, and engages with the companies in which we invest on behalf of our clients to better understand your approach to them.³¹

BlackRock's focus on millennials appears to make good business sense. Millennials will increasingly be the ones holding most of the wealth in the U.S., making it essential for firms to start catering to their needs and developing brand loyalty now, not later.³² In sum, by focusing on millennials now, it appears that BlackRock hopes to maintain or perhaps even expand its future market share of "assets under management" (AUM).³³

Consistent with its millennial objective, Fink announced in his 2020 letter to clients the launch of a large number of new ESG funds.³⁴ Such offerings appear to be an attempt to capitalize on the notion that millennials believe they can do good through "stock-picking." While there is no evidence to suggest that such good can result from such an activity,³⁵ the successful marketing of such funds can do a lot to enhance the profitability of BlackRock, as these funds will be able to charge higher fees.

31. Fink, *Larry Fink's 2019 Letter to CEOs*, *supra* note 30 (emphases added).

32. Barzuza, Curtis & Webber, *supra* note 30, at 1286.

33. *Id.* at 1249–50.

34. Larry Fink, *Larry Fink's 2020 Letter to Clients: Sustainability as BlackRock's New Standard for Investing*, BLACKROCK, <https://www.blackrock.com/corporate/investor-relations/2020-blackrock-client-letter> [<https://perma.cc/D35A-B5ER>] (last visited Mar. 27, 2021).

35. According to Professor Alicia Munnell:

That's preposterous to me that you have big social problems like that [(gender equality or the prevention of global warming)], and you think they can be solved by stock-picking And it's really kind of dangerous in some ways, because it makes people feel like they're doing something good to actually solve global warming, and it's really not.

Patrick Donachie, *A Blue Wave May Derail DOL's Rule on ESG in Retirement Plans*, WealthManagement.com (Oct. 28, 2020), <https://www.wealthmanagement.com/regulation-compliance/blue-wave-may-derail-dols-rule-esg-retirement-plans> [<https://perma.cc/5JQT-R33Q>].

For example, because of the portfolio screening services that an index provides,³⁶ mutual funds and ETFs that track the MSCI's KLD 400 Social Index, such as BlackRock's iShares MSCI KLD 400 Social ETF,³⁷ will typically charge significantly higher fees than funds and ETFs that track the more standardized and broadly based CRSP U.S. Total Market Index³⁸ or Fidelity U.S. Total Investable Market Index.³⁹ In sum, the offering of ESG funds that yield greater profit margins is another expected benefit of its millennial objective.

C. BlackRock's Engagement Strategy

In Fink's 2020 letters to CEOs⁴⁰ and clients,⁴¹ BlackRock explained the parameters of its engagement strategy and how it would help achieve its primary objective. First, BlackRock will be dictating its own vision of what a public company's (a company traded on a U.S. stock exchange or over-the-counter) stakeholder relationships should be by requiring its portfolio companies (virtually every public company) to disclose data on "how each company serves its full set of stakeholders."⁴² Moreover, noncompliance is not acceptable. According to Fink, "we will be increasingly disposed to *vote against* management and board directors when companies are not making sufficient progress on sustainability-related disclosures and the business practices and plans underlying them."⁴³

36. For a discussion of portfolio screening for purposes of creating an ESG index fund, see Bernard S. Sharfman, *ESG Investing Under ERISA*, 38 YALE J. ON REG. BULL. 112, 120–21 (2020).

37. *iShares MSCI KLD 400 Social ETF Fact Sheet*, BLACKROCK (Mar. 31, 2020), <https://www.ishares.com/us/literature/fact-sheet/dsi-ishares-msci-kld-400-social-etf-fund-fact-sheet-en-us.pdf> [<https://perma.cc/SNN2-VGQP>] (identifying an expense ratio of 0.25%).

38. *Vanguard Total Stock Market ETF*, VANGUARD, <https://investor.vanguard.com/etf/profile/fees/vti> [<https://perma.cc/F428-H7EY>] (last visited Mar. 27, 2021) (identifying an expense ratio of 0.03%).

39. *Fidelity's ZEROSM Total Market Index Fund*, FIDELITY INVS. (Jul. 3, 2020), <https://fundresearch.fidelity.com/mutual-funds/fundfactsheet/31635T708> [<https://perma.cc/S6H7-CNHD>] (identifying an expense ratio of 0.00%).

40. Larry Fink, *Larry Fink's 2020 Letter to CEOs: A Fundamental Reshaping of Finance*, BLACKROCK, <https://www.blackrock.com/corporate/investor-relations/2020-larry-fink-ceo-letter> [<https://perma.cc/WN4U-G47E>] (last visited Mar. 27, 2021).

41. Fink, *Larry Fink's 2020 Letter to Clients*, *supra* note 34.

42. Fink, *Larry Fink's 2020 Letter to CEOs*, *supra* note 40.

43. *Id.* (emphasis added).

These stakeholders include not only those stakeholders impacted by climate change⁴⁴ but also those who suffer from a lack of gender equality.⁴⁵ Moreover, BlackRock has recently signaled that increased attention will be given to those stakeholders impacted by COVID-19 and Black Lives Matter⁴⁶:

We have learned from our engagements that companies are finding it challenging to balance the short-term actions needed to mitigate the professional and personal effects of COVID-19 on their employees, customers, and other stakeholders. Companies are having to transition their business models to allow employees to work from home or in a safe, socially distanced environment. This transition also includes companies re-designing their supply chains and operations due to impacts caused by COVID-19.

BIS [(BlackRock Investment stewardship team)] remains focused on companies' progress with respect to diversity. The movement for racial equity and justice underscores the need for companies to do better to ensure representation at all levels of the workforce, alongside an inclusive culture in which a diverse workforce can employ skills and expertise to full effect in driving a company's strategic objectives and long-term shareholder value.⁴⁷

This engagement strategy, targeting for advocacy those stakeholders who have the most appeal to millennials, is arguably a way for BlackRock to show millennials that they have shared values. As a result, this should encourage millennials to invest in the index funds that BlackRock manages.

II. PUTTING WORDS INTO ACTION: BLACKROCK'S VOTING AND ENGAGEMENT RECORD

Besides its rhetoric, BlackRock's shareholder activism is made up of shareholder voting and engagement (direct or indirect communication) with the management of portfolio companies. Voting and engagement are intertwined activities, with voting being the stick that BlackRock can use to pressure companies to adopt their stakeholder

44. *Id.*

45. Fink, *Larry Fink's 2020 Letter to Clients*, *supra* note 34.

46. *BlackRock Investment Stewardship Global Quarterly Stewardship Report July 2020*, BLACKROCK 1, 4, <https://www.blackrock.com/corporate/literature/publication/blk-qrtly-stewardship-report-q2-2020.pdf> [<https://perma.cc/ES6N-778C>].

47. *Id.* at 3.

policies. Based on its second-quarter 2020 *Global Quarterly Stewardship Report* (the “Report”),⁴⁸ it is now clear that BlackRock’s investment stewardship team has ramped up its shareholder activism. On a global basis, again utilizing only around forty-five professionals, the team accomplished the following in the second quarter of 2020:

- **Voting:** Globally, “voted at more than 9,200 shareholder meetings [(9,540 meetings)] on more than 100,000 proposals [(103,169)]. . . . [v]oted *against* at least one management proposal at 43% of shareholder meetings globally and against management’s recommendation on 9% of all proposals.”⁴⁹

Specific to North America, BlackRock voted at 3,085 shareholder meetings, voted on 27,126 proposals, voted against at least one management proposal at 30% of the meetings, and voted against management’s recommendation on 7% of all proposals.⁵⁰ Moreover, as what appears to be the primary way of enforcing their engagement objectives, they voted against board-nominated directors approximately 9% of the time (1,751 votes against out of 19,459 total votes).⁵¹

- **Engagement:** Globally, “a 22% increase in total company engagements [(974)] compared to Q2 2019. [The team] engaged in direct dialogue with 812 companies, interacting multiple times with 13% of them.”⁵² These engagements were divided into three themes: governance, environmental, and social.⁵³

Under the governance theme, the top engagement topics were board composition and effectiveness (discussed 504 times), corporate strategy (“long-term strategic direction, how strategy, purpose and culture are aligned, and corporate milestones against which to assess management” discussed 383 times), and executive compensation (discussed 379 times).⁵⁴

Under the environmental theme, the top engagement topics were climate risk management (discussed 272 times) and operational sustainability (“waste and water management,

48. *Id.* at 1.

49. *Id.* at 4 (emphasis added).

50. *Id.* at 6.

51. *Id.*

52. *Id.* at 4.

53. *Id.* at 5.

54. *Id.*

packaging, product life-cycle management, product offerings, and energy efficiency” discussed 245 times).⁵⁵

Under the social theme, the top engagement topics were human capital management (discussed 236 times; a threefold rise).⁵⁶

- **Voting and Engagement:** “[I]dentified 244 companies” that it believed were “making insufficient progress integrating *climate risk* into their business models or disclosures.”⁵⁷ “Of these companies, [it] took voting action against 53, or 22% and . . . put the remaining 191 companies ‘on watch.’”⁵⁸ “Those companies that do not make significant progress” on “integrating *climate risk* into their business models or disclosures” “risk voting action against management in 2021.”⁵⁹ In addition, when it came to shareholder proposals on the environment, out of 30 votes, they voted with shareholders 20% of the time.⁶⁰

III. ERISA'S FIDUCIARY DUTIES

What does the law have to say about BlackRock's shareholder activism? For purposes of this Article, the law is ERISA and its fiduciary duties. Justice Stephen Breyer, in his opinion in *Varsity Corp. v. Howe*, begins this Article's explanation of ERISA's fiduciary duties:

ERISA protects employee pensions and other benefits by providing insurance (for vested pension rights, see ERISA § 4001 *et seq.*), specifying certain plan characteristics in detail (such as when and how pensions vest, see §§ 201–211), and by setting forth certain general fiduciary duties applicable to the management of both pension and nonpension benefit plans. . . .

In doing so, we recognize that these fiduciary duties draw much of their content from the common law of trusts, the law that governed most benefit plans before ERISA's enactment.

We also recognize, however, that trust law does not tell the entire story. After all, ERISA's standards and procedural protections

55. *Id.*

56. *Id.* at 4–5.

57. *Id.* (emphasis added).

58. *Id.*

59. *Id.* (emphasis added).

60. *Id.* at 7.

partly reflect a congressional determination that the common law of trusts did not offer completely satisfactory protection. And, even with respect to the trust-like fiduciary standards ERISA imposes, Congress “expect[ed] that the courts will interpret this prudent man rule (and the other fiduciary standards) bearing in mind the special nature and purpose of employee benefit plans,” as they “develop a ‘federal common law of rights and obligations under ERISA-regulated plans.’”⁶¹

Given that fiduciary framework, this Article seeks a fact pattern where the fiduciary duties of ERISA require a plan manager to investigate BlackRock’s shareholder activism. Please note that this Article is not talking about the fiduciary duties of BlackRock under ERISA. In general, as an investment adviser to mutual funds and ETFs, it has none unless it directly manages all or part of a plan.⁶² Therefore, this Article is focused on how the fiduciary duties of a plan manager interacts with BlackRock’s shareholder activism.

A. Duty of Loyalty

ERISA Section 3(21)(A) provides that a “person is a fiduciary with respect to a plan to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or

61. 516 U.S. 489, 496–97 (1996) (citations omitted).

62. ERISA § 3(21)(B), 29 U.S.C. § 1002(21)(B), provides:

If any money or other property of an employee benefit plan is invested in securities issued by an investment company registered under the Investment Company Act of 1940 [15 U.S.C. 80a–1 et seq.], such investment shall not by itself cause such investment company or such investment company’s investment adviser or principal underwriter to be deemed to be a fiduciary or a party in interest as those terms are defined in this title, except insofar as such investment company or its investment adviser or principal underwriter acts in connection with an employee benefit plan covering employees of the investment company, the investment adviser, or its principal underwriter. Nothing contained in this subparagraph shall limit the duties imposed on such investment company, investment adviser, or principal underwriter by any other law.

See also Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. 55,219, 55,234 (proposed Sept. 4, 2020) (to be codified at 29 C.F.R. pt. 2509, 2550) (“ERISA does not govern the management of the portfolio internal to a fund registered with the SEC, including such fund’s exercise of its shareholder rights appurtenant to the portfolio of stocks it holds. . .”).

disposition of its assets.”⁶³ Fiduciaries include trustees⁶⁴ who retain management control over plan assets and investment managers⁶⁵ who, because of their financial expertise, are commonly delegated such authority by the trustees (“plan managers”). These fiduciaries must go about their work under the guidance of very strict fiduciary duties of loyalty and care.⁶⁶

Under ERISA’s duty of loyalty, a plan manager shall discharge his duties with respect to a plan “solely in the interest of the participants and beneficiaries and for the *exclusive* purpose of benefitting them.”⁶⁷ This “sole interest rule” is a codification of what is found in the common law of trusts.⁶⁸ It creates a very specific and narrow path for a plan manager when considering an investment strategy or providing mutual-fund or ETF selections for self-directed individual accounts.

According to the Restatement (Third) of Trusts, “the trustee [plan manager] has a duty to the beneficiaries [and participants] not to be influenced by the interest of any third person or by motives other than the accomplishment of the purposes of the trust [ERISA plan].”⁶⁹ Moreover, a “trustee [plan manager] who is influenced by his own or a third party’s interests is disloyal, because the trustee [plan manager] is no longer acting *solely* in the interest of the beneficiaries.”⁷⁰

In addition, based on the U.S. Supreme Court’s interpretation of the statutory language, the fiduciary must act on behalf of the plan for the “exclusive purpose” of:

“providing benefits to participants and their beneficiaries” while “defraying reasonable expenses of administering the plan.” Read in the context of ERISA as a whole, the term “benefits” in the provision just quoted must be understood to refer to the sort of *financial* benefits (such as retirement income) that trustees who manage investments typically seek to secure for the trust’s beneficiaries. *Cf.* § 1002(2)(A) (defining “employee pension

63. 29 U.S.C. § 1002(21)(A).

64. *See id.* § 1105(c)(3).

65. *See id.* § 1102(c)(3).

66. Cent. States, Se. & Sw. Areas Pension Fund v. Cent. Transp., Inc., 472 U.S. 559, 570–71 (1985).

67. 29 U.S.C. § 1104(a)(1)(A)(i) (emphasis added).

68. Max M. Schanzenbach & Robert H. Sitkoff, *Reconciling Fiduciary Duty and Social Conscience: The Law and Economics of ESG Investing by a Trustee*, 72 STAN. L. REV. 381, 403 (2020).

69. *Id.* at 400 (citing RESTATEMENT (THIRD) OF TRUSTS § 78(1) cmt. f. (AM. L. INST. 2007)).

70. *Id.* at 401 (emphasis added).

benefit plan” and “pension plan” to mean plans that provide employees with “retirement income” or other “deferral of income”).⁷¹

The Court provided further that “[t]he term [‘benefits’] does not cover nonpecuniary benefits” such as promoting the goal of employee ownership of company stock.⁷² Therefore, ERISA’s fiduciary duties incorporate a mandatory “common investor purpose,”⁷³ the pursuit of *financial* benefits for the plan beneficiaries, that does not allow for the pursuit of nonfinancial or nonmonetary benefits even if participants and beneficiaries approve. In sum, plan managers are to be constantly guided by the fiduciary principles of acting “*solely* in the interest of the participants and beneficiaries” and for the *exclusive purpose* of providing financial benefits to them.

This fiduciary duty of loyalty is very strict and narrowly confided to making sure that participants and beneficiaries receive the retirement benefits that they are entitled to, period. The reason for this is Congressional intent. Congress was obsessed with the financial corruption in private pension plans during the 50s and 60s and wanted to make sure a repeat did not occur.⁷⁴ This corruption included the widespread looting of union-controlled employee retirement plans.⁷⁵

B. Duty of Prudence

Under ERISA, the duty of prudence requires that a plan manager act “with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims.”⁷⁶ Thus, a prudent person standard applies.

71. Fifth Third Bancorp v. Dudenhoeffer, 573 U.S. 409, 420–21 (2014) (quoting 29 U.S.C. § 1104(a)(1)(A)(i)–(ii)). Such an understanding of “exclusive purpose” makes it extremely difficult to accept David Webber’s argument that it is permissible to use the funds of ERISA plans for purposes of creating jobs for plan participants. See David H. Webber, *The Use and Abuse of Labor’s Capital*, 89 N.Y.U. L. REV. 2106, 2126–27 (2014).

72. *Dudenhoeffer*, 573 U.S. at 421.

73. Sean J. Griffith, *Opt-In Stewardship: Toward an Optimal Delegation of Mutual Fund Voting Authority*, 98 TEX. L. REV. 983, 990 (2020).

74. See Daniel R. Fischel & John H. Langbein, *ERISA’s Fundamental Contradiction: The Exclusive Benefit Rule*, 55 U. CHI. L. REV. 1105, 1110 (1988).

75. *Id.*

76. 29 U.S.C. § 1104(a)(1)(B); ERISA, Pub. L. No. 93-406, § 404(a)(1)(B), 88 Stat. 829, 877.

This standard certainly applies when a plan manager selects its investments.⁷⁷ Moreover, critical to determining whether a plan manager has met its duty of prudence is a finding that the fiduciary has acted independently⁷⁸ and impartially⁷⁹ when making its investment decisions. As a result, “[t]he duty of prudence prevents a fiduciary from choosing an investment alternative that is financially less beneficial than *reasonably available alternatives*.”⁸⁰

C. ERISA's Duties and Shareholder Voting/Engagement

As I have previously written on this subject:

[S]ince 1988, when first presented in a formal Opinion Letter now commonly referred to as the “Avon Letter,” it has been DOL policy that the fiduciary act of managing plan assets also includes managing the voting rights associated with a plan’s equity holdings.⁸¹

In the Avon Letter, the Pension and Welfare Benefits Administration, the DOL department that preceded the Employee Benefits Security Administration in the administration of ERISA,⁸² stated that “[i]n general, the *fiduciary* act of managing

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77. *Donovan v. Cunningham*, 716 F.2d 1455, 1467 (5th Cir. 1983) (“In addition, the prudent man rule as codified in ERISA is a flexible standard: the adequacy of a fiduciary’s investigation is to be evaluated in light of the ‘character and aims’ of the particular type of plan he serves.”) (citing 29 U.S.C. § 1104(a)(1)(B)).
78. *Fink v. Nat’l Sav. & Tr. Co.*, 772 F.2d 951, 957 (D.C. Cir. 1985) (“A fiduciary’s independent investigation of the merits of a particular investment is at the heart of the prudent person standard.”).
79. CRAIG C. MARTIN, MICHAEL A. DOORNWEERD, AMANDA S. AMERT & DOUGLAS A. SONDEGROTH, *JENNER & BLOCK PRACTICE SERIES: ERISA LITIGATION HANDBOOK* (2012) (quoting *Bussian v. RJR Nabisco, Inc.*, 223 F.3d 286, 302 (5th Cir. 2000) and citing *Flanigan v. Gen. Elec. Co.*, 242 F.3d 78, 86 (2d Cir. 2001)) (explaining that the duty of prudence requires a plan manager to conduct a “thorough, impartial investigation”).
80. *Financial Factors in Selecting Plan Investments*, 85 Fed. Reg. 72,846, 72,848 (Nov. 13, 2020) (to be codified at 29 C.F.R. pt. 2509, 2550) (emphasis added).
81. U.S. Dep’t of Labor, Pension & Welfare Benefit Admin., *Opinion Letter on Avon Products, Inc. Employees’ Retirement Plan at *2* (Feb. 23, 1988) [hereinafter *Avon Letter*].
82. *History of EBSA and ERISA*, U.S. DEP’T OF LABOR: EMP. BENEFITS SEC. ADMIN., <https://www.dol.gov/agencies/ebsa/about-ebsa/about-us/history-of-ebsa-and-erisa> [https://perma.cc/687X-KZ2G] (last visited Apr. 1, 2021) (“Until February 2003, EBSA was known as the Pension and Welfare Benefits Administration (PWBA).”).

plan assets which are shares of corporate stock would include the voting of proxies *appurtenant* to those shares of stock.”⁸³ This policy has been explicitly affirmed by the DOL in 1990,⁸⁴ 1994,⁸⁵ 2008,⁸⁶ 2016,⁸⁷ and 2018.⁸⁸

Such a policy presumes that significant, not *de minimis*, financial value will accrue to beneficiaries and participants if a plan manager, in accordance with [its] fiduciary duties, properly manages the shareholder voting rights associated with their plan's equity holdings.⁸⁹

1. Shareholder Voting

How shareholder voting is to be approached by a plan manager consistent with its fiduciary duties was summarized in footnote 4 of the Avon Letter:

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83. Avon Letter, *supra* note 81, at *2 (emphases added).
84. U.S. Dep't of Labor, Pension & Welfare Benefit Admin., Opinion Letter on Responsibilities of Plan Fiduciaries under ERISA with Respect to Voting Proxies at *3 (Jan. 23, 1990) (“If either the plan or the investment management contract (in the absence of a specific plan provision) expressly precludes the investment manager from voting proxies, the responsibility for such proxy voting would be part of the trustees’ exclusive responsibility to manage and control the assets of the plan.”).
85. Interpretive Bulletins Relating to the Employee Retirement Income Security Act of 1974, 59 Fed. Reg. 38,863 (July 29, 1994) (to be codified at 29 CFR pt. 2509) (“[A] statement of proxy voting policy would be an important part of any comprehensive statement of investment policy.”).
86. Interpretive Bulletin Relating to Exercise of Shareholder Rights, 73 Fed. Reg. 61,731, 61,732 (Oct. 17, 2008) (to be codified at 29 C.F.R. pt. 2509) (“The fiduciary act of managing plan assets that are shares of corporate stock includes the management of voting rights appurtenant to those shares of stock.”).
87. Interpretive Bulletin Relating to the Exercise of Shareholder Rights and Written Statements of Investment Policy, Including Proxy Voting Policies or Guidelines, 81 Fed. Reg. 95,879, 95,880 (Dec. 29, 2016) (to be codified at 29 C.F.R. pt. 2509) (“The Department’s longstanding position is that the fiduciary act of managing plan assets which are shares of corporate stock includes decisions on the voting of proxies . . .”).
88. *Field Assistance Bulletin No. 2018-01*, U.S. DEP’T OF LABOR, EMP. BENEFITS SEC. ADMIN. (Apr. 23, 2018), <https://www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/field-assistance-bulletins/2018-01> [<https://perma.cc/L9LB-2TPR>].
89. Bernard S. Sharfman, *Now Is the Time to Designate Proxy Advisors as Fiduciaries under ERISA*, 25 STAN. J.L. BUS. & FIN. 1, 8 (2020).

Section 404(a)(1) requires, among other things, that a fiduciary of a plan act prudently, solely in the interest of the plan's participants and beneficiaries, and for the exclusive purpose of providing benefits to participants and beneficiaries. *To act prudently in the voting of proxies (as well as in all other fiduciary matters), a plan fiduciary must consider those factors which would affect the value of the plan's investment.* Similarly, the Department [of Labor] has construed the requirements that a fiduciary act solely in the interest of, and for the exclusive purpose of providing benefits to, participants and beneficiaries as *prohibiting a fiduciary from subordinating the interests of participants and beneficiaries in their retirement income to unrelated objectives.*⁹⁰

Accordingly, when a plan manager votes on behalf of an ERISA pension plan, it must do so within the strict and narrow boundaries of what the fiduciary duties of ERISA require. The DOL's recently proposed rule, *Fiduciary Duties Regarding Proxy Voting and Shareholder Rights*, is very clear on the purpose of shareholder voting: "ERISA mandates that fiduciaries manage voting rights prudently and for the 'exclusive purpose' of securing economic benefits for plan participants and beneficiaries—which may or may not require a proxy vote to be cast."⁹¹

In the specific context of shareholder voting under the duty of prudence:

[F]iduciaries must perform *reasonable investigations*, understanding that certain proposals may require a more detailed or particularized voting analysis. Information that will better enable fiduciaries to determine whether or how to vote proxies on particular matters includes the cost of voting, including opportunity costs; the type of proposal (*e.g.*, those relating to social or public policy agendas versus those dealing with issues that have a direct economic impact on the investment); voting recommendations of management; and an analysis of the particular shareholder proponents. In the Department's view, fiduciaries must be prepared to articulate the anticipated economic benefit of proxy-vote decisions in the event they decide to vote.⁹²

90. Avon Letter, *supra* note 81, at 11 n.4 (emphasis added).

91. Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. 55,219, 55,223 (proposed Sept. 4, 2020) (to be codified at 29 C.F.R. pt. 2509, 2550).

92. *Id.* at 55, 224 (emphasis added) (footnote omitted).

2. Shareholder Engagement

DOL guidance on shareholder engagement is also clear and unambiguous. Not surprisingly, engagement is allowed as long as it resides within the confines of a plan manager's fiduciary duties. According to the DOL's recently proposed rule on shareholder voting, "ERISA does not permit fiduciaries, in voting proxies or *exercising other shareholder rights*, to subordinate the economic interests of participants and beneficiaries to unrelated objectives."⁹³ Moreover, the DOL "has rejected a construction of ERISA . . . that would permit plan fiduciaries to expend trust assets to promote myriad public policy preferences, *including through shareholder engagement activities*, voting proxies, or other investment policies."⁹⁴

Moreover, the duty of prudence will require a reasonable investigation into the costs and benefits of any engagement activity. This investigation must be done in order to conclude that there is "a reasonable expectation that such activities are likely to enhance the [economic] value of the plan's investments after taking into account the costs."⁹⁵

The key point is that a plan manager is allowed to engage with the management of a portfolio company but only if the engagement conforms to its fiduciary duties. This means that engagement must only be utilized if there is "a reasonable expectation that such activities are likely to enhance the [economic] value of the plan's investments after taking into account the costs."⁹⁶

IV. ERISA'S FIDUCIARY DUTIES AND INDEX FUNDS: ISSUE AND RULE

In the Avon Letter, the DOL was discussing shareholder voting in the context of "the voting of proxies on plan-owned stock."⁹⁷ Back in 1988, when the letter was written, the DOL was undoubtedly referring to the right to vote the proxies associated with the common stock of public companies held in portfolio. As the letter says: "In general, the fiduciary act of managing plan assets which are shares of *corporate stock* would include the voting of proxies appurtenant to those shares of stock."⁹⁸

93. *Id.* at 55,220–21 (emphasis added).

94. *Id.* at 55,221 (emphasis added).

95. *Field Assistance Bulletin No. 2018-01*, *supra* note 88.

96. *Id.*

97. Avon Letter, *supra* note 81, at 1.

98. *Id.* (emphasis added).

The direct ownership of corporate stock in ERISA plans is still significant. The DOL recently reported that ERISA plans hold in portfolio approximately \$2.1 trillion of such stock.⁹⁹ But over time, the nature of stock ownership has changed dramatically, as more and more plan assets are invested in mutual funds and ETFs.¹⁰⁰ While the total dollar amount of equity index funds held in ERISA plans, either directly or through self-directed accounts, is not known, the Investment Company Institute has reported that 401K (ERISA) plans held over \$2 billion in mutual fund equities as of June 30, 2020.¹⁰¹

A. *The Issue*

As previously discussed, when a plan manager utilizes index mutual funds and/or ETFs for its portfolio or offers them as selections in self-directed individual accounts, the plan has delegated away its voting authority to the investment advisers of those funds. This delegated voting authority does not come under the fiduciary duties of ERISA.¹⁰² Therefore, given our focus on BlackRock, the issue becomes whether under the fact pattern of an ERISA plan investing in BlackRock's index funds either directly or through self-directed accounts, does the plan manager have a fiduciary duty to investigate BlackRock's shareholder activism?¹⁰³

B. *The Rule*

Based on the rationales found in Section C of this Part, it is argued that a plan manager must do the following: A plan manager, when selecting [index] mutual funds and ETFs for direct ownership or availability to self-directed accounts and in the general monitoring of

99. Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. 55,219, 55,228 (Sept. 4, 2020) (to be codified at 29 C.F.R. pt. 2509, 2550).

100. *Id.* at 55,222.

101. INV. CO. INST., REPORT: THE US RETIREMENT MARKET, SECOND QUARTER 2020 (Sept. 24, 2020), available at https://www.ici.org/info/ret_20_q2_data.xls.

102. See text accompanying notes 68–70.

103. It is interesting to note that the DOL did not address this issue in its recent proposed rule on proxy voting, *Fiduciary Duties Regarding Proxy Voting and Shareholder Rights*. See *supra* note 91. This author believes that this was an important omission in the proposed rule. To correct this omission, this author in his comment letter to the DOL on this proposed rule asked the DOL to address this issue. See Letter from Bernard S. Sharfman to the Dep't of Labor on Its Proposed Rule, *Fiduciary Duties Regarding Proxy Voting and Shareholder Rights*, <https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AB91/00057.pdf> [<https://perma.cc/Q7HN-N3KN>].

plan's ongoing investment in these funds, has a fiduciary duty to investigate an investment adviser's [BlackRock's] shareholder activism.

This rule is to apply to all index mutual funds and ETFs that an ERISA plan manager is considering to add, or has added, to its ERISA plan. However, for purposes of this Article, it will only be discussed in the context of the index funds that use BlackRock as its investment adviser.

C. Rationales for the Rule

Duty of Prudence Rationale: For a plan manager to adequately complete its financial analysis of a BlackRock index fund prior to making its investment decision, the investment adviser's shareholder activism must be investigated for its potential to financially harm or benefit the plan. This activism is now an attribute of the investment that needs to be evaluated for purposes of making the investment decision.¹⁰⁴

Abdication Rationale: While the voting authority of an investment adviser to a mutual fund or ETF does not come under the fiduciary duties of ERISA, it is doubtful that the intent of the Avon Letter and all subsequent guidance in this regard was meant to absolve a plan manager of any fiduciary duty associated with the shareholder voting of shares that it now owns indirectly through its share ownership in mutual funds and ETFs. The result would be an abdication of duties in the context of shareholder voting. If a plan only invests in index funds and does not have direct holdings of voting stock, this would be a total abdication of duties.

104. As a DOL advisory opinion stated:

Section 3(21)(B) provides that a plan's investment in a registered investment company "shall not by itself cause such investment company or such investment company's investment adviser or principal underwriter to be deemed to be a fiduciary or a party in interest as those terms are defined in [Title I of ERISA], except insofar as such investment company or its investment adviser or principal underwriter acts in connection with an employee benefit plan covering employees of the investment company, the investment adviser, or its principal underwriter."

U.S. Dep't of Labor, Emp. Benefits Sec. Admin., Advisory Opinion 2009-04a, at 1 (Dec. 4, 2009), <https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/advisory-opinions/2009-04a> [<https://perma.cc/J7A9-3E64>]. But "ERISA's exclusion for mutual funds is not absolute. It does not apply to a plan fiduciary's decision to invest plan assets in a mutual fund." *Id.* at 2.

V. APPLYING THE RULE TO BLACKROCK'S
SHAREHOLDER ACTIVISM

The following investigates how BlackRock utilizes its shareholder activism. It focuses on BlackRock's marketing objective, as identified in its rhetoric, and the stakeholder approach that underlies its engagement strategy.

A. *BlackRock's Shareholder Activism in a Theoretical Framework*

ERISA's fiduciary duties require a plan manager to place a value on BlackRock's shareholder activism so it can see how it impacts the overall financial value of an index fund investment. Such value is derived from its impact on the governance of the firms that are in the index. To understand how this value can be gauged, let's consider the fiduciary duties of ERISA in the context of Goshen and Squire's "principal-cost theory."¹⁰⁵ Under this theory, "each firm's optimal governance structure minimizes total control costs, which are the sum of principal costs and agent costs."¹⁰⁶ According to Goshen and Squire, "Principal costs occur when investors exercise control (shareholders), and agent costs occur when managers exercise control."¹⁰⁷ These two category of costs are further sub-divided into "principal competence costs, principal conflict costs, agent competence costs, and agent conflict costs."¹⁰⁸ Competence costs are "the costs of honest mistakes and of efforts to avoid such mistakes, and conflict costs as the costs of self-seeking conduct and of efficient efforts to prevent such conduct."¹⁰⁹ Most importantly, "[a] governance structure that maximizes firm value allocates control in the manner that minimizes the sum of costs across the four categories."¹¹⁰

ERISA's fiduciary duties are neutral (without bias) to how the minimization of total control costs is achieved. A plan manager, as part of its investment analysis of investing in BlackRock's index funds or allowing them to be used in self-directed accounts, would need to reasonably gauge the positive or negative value of shareholder activism at all the companies that make up the fund index. Such shareholder activism implicates the potential for increased principal competence or

105. Zohar Goshen & Richard Squire, *Principal Costs: A New Theory for Corporate Law and Governance*, 117 COLUM. L. REV. 767, 770 (2017).

106. *Id.* (emphasis omitted).

107. *Id.*

108. *Id.* at 784.

109. *Id.*

110. *Id.*

conflict costs while at the same time signaling the potential for reduced agent competence or conflict costs on a portfolio-wide basis. If this activism reduces total control costs on a portfolio basis, then it has value. If it increases total control costs on a portfolio basis, then it does financial harm. If the latter is significant, then the plan manager should seek out “reasonably available alternatives”¹¹¹ that are not involved in such activism. If it does not, then it would be supporting, through the voting authority that it has delegated away to BlackRock, shareholder activism that is doing harm to the value of its investment.

B. Marketing Objective

We first look at the primary objective of BlackRock's shareholder activism, the marketing of its investment products to millennials. From the perspective of BlackRock, the successful achievement of such a marketing objective would be a great financial win for the company and its own shareholders. It is no secret that the index-fund business, of which BlackRock is a leader, has become cutthroat and does not appear to be generating fees for anyone, including BlackRock. One way to increase fees is to convince investors, such as millennials, that the world would be a better place if they would just invest in ESG index funds. As previously discussed, the offering of ESG funds may be significantly more profitable for the investment adviser than lower-cost funds that use standardized indexes.¹¹²

This marketing objective is definitely not consistent with a plan manager's fiduciary duties. BlackRock's voting and engagement behavior is being skewed in the direction of a particular subset of beneficial and potential beneficial investors, those who fit BlackRock's marketing profile of a *millennial*, so as to enhance BlackRock's own profitability. Moreover, this investor group is presumed not to be exclusively interested in the financial benefits their investments can provide. Therefore, the marketing to millennials is not being done “solely in the interest of the participants and beneficiaries” and for the “exclusive purpose” of providing financial benefits to beneficial investors such as participants and beneficiaries of an ERISA plan.

From a theoretical perspective, BlackRock's marketing objective definitely indicates an increase in principal conflict costs without any reduction in agent costs. Nevertheless, this marketing objective is not enough, on its own, for a plan manager to decline to consider the inclusion of BlackRock's index funds into its plan's portfolio. There is still no evidence how it would impact the financial benefits of a BlackRock index fund compared to “reasonably available alterna-

111. Financial Factors in Selecting Plan Investments, 85 Fed. Reg. 72,846, 72,848 (Nov. 13, 2020) (to be codified at 29 C.F.R. pt. 2509, 2550).

112. See *supra* Part I.B.

tives.”¹¹³ Without such evidence, you cannot say that this marketing objective has created financial harm for its investors.

C. Engagement Strategy and Stakeholder Approach

As previously discussed, BlackRock has an engagement strategy that focuses on benefiting various stakeholders who most appeal to millennials. These stakeholders, at least for the time being, are those who have been impacted by climate change, gender equality, global supply chains and operations impacted by Covid-19, and racial equity.¹¹⁴ BlackRock has the ability and willingness to enforce this engagement strategy by threatening to vote against management on various management and shareholder proposals. Based on its recent shareholder voting record, it appears to do so mainly by voting against management's nominees for board membership.¹¹⁵

Clearly, this strategy is not being done “solely in the interest of the participants and beneficiaries” and for the “exclusive purpose” of providing financial benefits.¹¹⁶ As a result, this strategy has the potential for serious principal conflict costs. It is a red flag, suggesting that the plan manager would be better off seeking “reasonably available alternatives”¹¹⁷ that do not include this engagement strategy.

1. A Harmful Engagement Strategy

A strong argument can also be made that BlackRock's engagement strategy of trying to influence the stakeholder relationships of its portfolio companies for purposes of marketing to millennials will result in financial harm to the beneficial investors of BlackRock's index funds, including the participants and beneficiaries of ERISA plans. This is the result of stakeholder relationships being extremely complex, creating the need for constant management, and BlackRock's investment stewardship team being extremely uninformed about these relationships.

a. The Complexity of Stakeholder Relationships

As I have previously written:

The management of [stakeholder] relationships is complex and is usually placed in the hands of those who have the knowledge and

113. Financial Factors in Selecting Plan Investments, 85 Fed. Reg. at 72,848.

114. *See supra* Part I.

115. *See supra* Part II.

116. Financial Factors in Selecting Plan Investments, 85 Fed. Reg. at 72,846, 72,847.

117. *Id.* at 72,848.

expertise to manage them: the company's management team, up and down the line.¹¹⁸

. . . .

. . . Moreover, [stakeholder] relationships can change on a daily basis: consumers who have ever-changing tastes or are becoming increasingly sensitive to the negative externalities that the company may create; competitors that introduce new products; changing technologies; threats to global and domestic supply chains for key components and raw materials; credit and equity markets that require ever-changing terms; and competitive labor markets for skilled talent. A failure to deal with these stakeholder relationship issues in an integrated manner can lead a company to report mediocre financial results and eventual failure.¹¹⁹

The following quote by Emily Winston gets to the heart of how complex stakeholder relationships are and why it is very unusual for shareholders to be involved in their management:

Public shareholders are not perfectly informed. Corporate managers have access to information about their firms to which public shareholders do not have access. Prominent in this category of private information is information about the corporation's relationships with its non-shareholder stakeholders. Corporations' relationships with their stakeholders are governed by agreements that are, to varying degrees, *incomplete*. At-will employees and customers, in particular, have very incomplete agreements with corporations, meaning most, if not all, terms of agreement are not explicitly specified. Even the more specific contracts, such as those with suppliers and creditors, will still have unspecified terms and *will need to be negotiated repeatedly over the course of the corporation's life*. Stakeholder agreements are therefore the subject of ongoing negotiations between firm managers and the relevant stakeholders. Managing these relationships is the role of a corporate manager, and it exposes managers to vital information about those stakeholder relationships to which shareholders are not privy. *This information is not reducible to metrics that can be effectively transferred to shareholders*, and public shareholders, by their nature, are not positioned, nor do they have the expertise, to be intimately

118. Bernard S. Sharfman, *Why BlackRock's Stakeholder Approach Won't Work*, REALCLEARMARKETS (May 18, 2020), https://www.realclearmarkets.com/articles/2020/05/18/why_blackrocks_stakeholder_approach_wont_work_491618.html [<https://perma.cc/5RVH-J4A7>].

119. *Id.*

involved in the management of other stakeholder relationships. Thus, information asymmetries will prevent shareholders from being effective monitors of other stakeholder interests.¹²⁰

This understanding has led Professor Winston to conclude:

Even when shareholders are financially incentivized to use their power to promote the interests of other stakeholders, they will lack the information about stakeholder relationships necessary to do so effectively. This asymmetry of information means that shareholders cannot incorporate stakeholder information into their assessment of firm value, so managing to shareholder expectations will not maximize the value created by stakeholder relationships.¹²¹

In sum, “while corporate attention to non-shareholder stakeholders can improve firm value, shareholder oversight of these stakeholder relationships will not succeed in having this effect.”¹²²

b. An Extremely Uninformed Shareholder

BlackRock gives all the indications of being an uninformed investor, even more so than the average shareholder. As previously mentioned, BlackRock's investment stewardship team is only made up of forty-five professionals covering the globe, not just the U.S. markets.¹²³ Of the twenty-two based in the U.S., twelve are focused globally while only ten are exclusively focused on North America.¹²⁴ But being focused on North America means more than evaluating U.S. public companies, it also means Canada as well. For example, take this recent quote by a BlackRock analyst: “I cover industrials and materials in the US and Canada. I cover approximately 800 companies in those sectors and am responsible for the engagement and proxy voting with those firms.”¹²⁵ When compared to an equity analyst who covers only five to fifteen companies at a time,¹²⁶ this is an astonishing number of companies to cover on an annual basis. It is not hard to conclude that it is not

120. Emily Winston, *Managerial Fixation and the Limitations of Shareholder Oversight*, 71 HASTINGS L.J. 699, 705 (2020) (emphases added).

121. *Id.* at 699.

122. *Id.*

123. *Investment Stewardship Annual Report*, *supra* note 18.

124. *See id.*

125. Ben Ashwell, *How BlackRock Connects the Dots on ESG*, Corp. Sec'y (Oct. 12, 2020), <https://www.corporatesecretary.com/articles/esg/32296/how-blackrock-connects-dots-esg> [<https://perma.cc/Q5ZE-DJN5>].

126. Griffith, *supra* note 73, at 1001.

possible for an analyst covering so many companies to become informed about any one of them.

Moreover, BlackRock and the other members of the Big Three are in the worst possible position for becoming informed and getting involved in the management of a public company's stakeholder relationships. According to law professor Charles Korsmo:

A large and growing share of institutional investment is in the form of "passive" index funds. . . . They seek to offer a market return and compete by offering the lowest possible fees to individual investors. As a result, they expend little or no effort seeking to value the firms they invest in. While these index funds are certainly "sophisticated" investors in the sense that they understand the central lesson of modern portfolio theory [(that it is more efficient to have a properly diversified investment portfolio than to try to pick stock winners using only publicly available information)] . . . they are not "sophisticated" in the sense of knowing anything about the firms they invest in. The whole philosophy of index investing is that it is unnecessary to know anything about the firms you invest in.¹²⁷

According to Bebchuk and Hirst, when investment stewardship teams from the Big Three engage with their portfolio companies, they show zero interest in financial underperformance: "We reviewed all of the examples of behind-the-scenes engagements described in the Big Three Stewardship Reports. *We found zero cases where engagement was described as being motivated by financial underperformance.*"¹²⁸ In the specific case of BlackRock's investment stewardship team, given the extremely limited resources it has to work with, why should we expect anything more?

Think about this in terms of BlackRock's recent focus on global supply chains and how the coronavirus exposed their weaknesses.¹²⁹ Where does BlackRock's expertise come from when it weighs in on how supply chains need to be restructured? This type of inquiry may sound good to millennials who would like to see supply chains and their associated job offerings become more domestic, and therefore make more jobs available to them, but with BlackRock being uninformed and not focused on the financial performance of its portfolio companies, one must conclude that BlackRock's investment stewardship team will not be able to add anything of real value to this kind of decision-making.

127. Charles R. Korsmo, *Delaware's Retreat from Judicial Scrutiny of Mergers*, 10 U.C. IRVINE L. REV. 55, 99 (2019) (emphasis added) (footnote omitted).

128. Bebchuk & Hirst, *Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy*, *supra* note 15, at 2096 (emphasis added).

129. *BlackRock Investment Stewardship Global Quarterly Stewardship Report*, *supra* note 46, at 3.

Finally, it must be noted that BlackRock's investment stewardship team may actually reduce firm value if its shareholder activism is successful. If BlackRock tries to pressure a company to make changes to its stakeholder relationships that management knows are value-reducing, management may counter-propose and agree to a less suboptimal, non-wealth-maximizing alternative in order to avoid the uncertain outcome of BlackRock going public with its concerns. This is an argument similar to the one made by John Matsusaka and Oguzhan Ozbas in a recent paper on shareholder proposals submitted by activists:

Managers have an incentive to deter proposals from activist shareholders by adjusting corporate policy; one might conjecture that external pressure leads them to choose policies more appealing to other shareholders in order to reduce the electoral prospects of activist proposals. However, we show that when deterrence occurs, it is always by moving policy toward the position favored by the activist, even if this reduces shareholder wealth. Our analysis stresses the central role of *voting uncertainty* in determining the value consequences of shareholder rights and proxy access.¹³⁰

The recent work of Nickolay Gantchev and Mariassunta Giannetti supports the idea that corporate boards would simply be acting rationally to reduce uncertainty if they were to privately agree to a less wealth-reducing alternative. Gantchev and Giannetti found that value-destroying shareholder proposals, typically submitted by high-volume submitters of proposals, may actually go to a vote, receive majority support, and be implemented by management.¹³¹ Therefore, the risk that management may have to fully implement BlackRock's uninformed recommendations, if BlackRock were to go public and receive support from other uninformed and opportunistic shareholders, may lead them to privately agree to less harmful arrangements.

2. Summary of BlackRock's Engagement Strategy

BlackRock's engagement strategy is arguably not appropriate for enhancing the financial benefits of its beneficial investors, including those who are ERISA plan participants and beneficiaries. This strategy exhibits significant principal conflict and competency costs. If BlackRock's investment stewardship team were truly interested in

130. John G. Matsusaka & Oguzhan Ozbas, *A Theory of Shareholder Approval and Proposal Rights*, 33 J. L. ECON. & ORG. 377, 377 (2017) (emphasis added).

131. Nickolay Gantchev & Mariassunta Giannetti, *The Costs and Benefits of Shareholder Democracy 2* (Oct. 2020) (unpublished manuscript) (http://ssrn.com/abstract_id=3269378).

enhancing the financial benefits provided to ERISA plan participants and beneficiaries, it is extremely doubtful that it would do so by becoming a third-party monitor and manager of its portfolio companies' stakeholder relationships. Therefore, a plan manager, after investigating BlackRock's engagement strategy, could reasonably conclude that it is financially harmful to its plan and decide to seek out "reasonably available alternatives"¹³² that are not associated with such an engagement strategy.

*D. Under ERISA, What Kind of Shareholder Activism and
Engagement Strategy Adds Value?*

Under ERISA, the sole and exclusive focus of a plan manager is to protect and enhance the financial benefits of a plan's participants and beneficiaries.¹³³ This objective limits the types of shareholder activism and engagement strategies that would be looked upon with favor by a plan manager. And it appears that hedge fund activism meets this criteria.

Hedge fund activism begins with an unregulated investment fund investing significant resources to identify an underperforming public company that may financially benefit from a significant change in business strategy.¹³⁴ In this identification process, the hedge fund becomes very informed about the target company. Once that company is identified and found acceptable for activism, the hedge fund devotes a significant amount of funds in the accumulation of the target company's stock, usually around five to ten percent of the shares outstanding.¹³⁵ (Of course, given that a member of the Big Three already owns around five to ten percent of the voting stock of many U.S. public companies,¹³⁶ the accumulation of a company's outstanding stock would not likely be an issue.) According to Rose and Sharfman, "[t]he catalyst for the accumulation is a determination by the hedge fund that the target company is currently not maximizing returns, but that if management would implement the hedge fund's recommended

132. Financial Factors in Selecting Plan Investments, 85 Fed. Reg. 72,846, 72,848 (Nov. 13, 2020) (to be codified at 29 C.F.R. pt. 2509, 2550).

133. *Id.*

134. Bernard S. Sharfman, *A Theory of Shareholder Activism and its Place in Corporate Law*, 82 TENN. L. REV. 791, 806 (2015) [hereinafter Sharfman, *Shareholder Activism*].

135. *Id.* at 809.

136. Bebchuk & Hirst, *Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy*, *supra* note 15, at 2033.

changes, company performance would improve, the stock would increase in value, and the hedge fund would reap excess returns.”¹³⁷

The hedge fund activist then invests more resources into its engagement strategy.¹³⁸ The strategy begins with a private meeting with the target's board of directors and executive management.¹³⁹ Then, if necessary, it goes public with its recommended changes to increase the price of the target's stock.¹⁴⁰ It can incorporate several hostile components such as “a threatened or actual proxy contest, takeover, lawsuit, or public campaign that is openly confrontational.”¹⁴¹

In sum, the hedge fund activist has an expectation that if the target company “would change its strategies to what the hedge fund believes is correct, then company performance will improve, the stock will increase in value, and the hedge fund will earn excess returns on its investment.”¹⁴² Its engagement strategy reveals itself in the advocacy that the hedge fund uses to persuade the target company to implement the strategic changes (private versus public, hostile or not) that it believes will significantly increase the target's stock price. Extensive empirical evidence has confirmed that this type of activism has, on average, been wealth enhancing for investors.¹⁴³ Based on this empirical evidence, it can be argued that what has occurred is that not only is there a reduction in principal competency costs, as reflected in the informed nature of the hedge fund activist as shareholder, but also a reduction in agent competency costs given that the information is willingly received and absorbed by management.

137. Paul Rose & Bernard S. Sharfman, *Shareholder Activism as a Corrective Mechanism in Corporate Governance*, 2014 BYU L. REV. 1015, 1034 (2014).

138. Sharfman, *Shareholder Activism*, *supra* note 134, at 809.

139. *Id.*

140. *Id.*

141. Alon Brav, Wei Jang, Frank Partnoy & Randall Thomas, *Hedge Fund Activism, Corporate Governance, and Firm Performance*, 63 J. FINANCE 1729, 1732 (2008).

142. Sharfman, *Shareholder Activism*, *supra* note 134, at 806.

143. Lucian A. Bebchuk, Alon Brav & Wei Jiang, *The Long-Term Effects of Hedge Fund Activism*, 115 COLUM. L. REV. 1085, 1085 (2015); Brav et al., *supra* note 141, at 1731; Nicole M. Boyson & Robert M. Mooradian, *Corporate Governance and Hedge Fund Activism*, 14 REV. DERIVATIVES RSCH. 169, 175–78, 201 (2011); Christopher P. Clifford, *Value Creation or Destruction? Hedge Funds as Shareholder Activists*, 14 J. CORP. FIN. 323, 324 (2008); Robin M. Greenwood & Michael Schor, *Investor Activism and Takeovers*, 92 J. FIN. ECON. 362, 374 (2009); April Klein & Emanuel Zur, *Entrepreneurial Shareholder Activism: Hedge Funds and Other Private Investors*, 64 J. FIN. 187, 213, 217–18 (2009).

It is possible that BlackRock or another Big Three member may consider taking up an engagement strategy that mimics what a hedge fund activist would use. Interestingly, this would make Bebchuk and Hirst quite happy, as they basically have advocated for the Big Three to invest the resources necessary for them to act like super huge hedge fund activists.¹⁴⁴ However, this would require a total change of a Big Three's business model, i.e., moving from making minimal investments in being informed to one where huge amounts of resources are being expended toward becoming informed about the portfolio companies they manage and then investing even further in becoming effective in advocating for strategic change at those companies. This change does not seem likely, but it would be consistent with ERISA's fiduciary duties.

CONCLUSION

An ERISA plan manager cannot simply delegate away its fiduciary duties when delegating its shareholder voting authority to BlackRock. The plan manager's duty of prudence requires it to investigate BlackRock's shareholder activism to see what financial impact it will have on its participants and beneficiaries.

This Article argues that after an appropriate investigation, a plan manager may find that BlackRock's engagement strategy is not consistent with its fiduciary duties. Therefore, a plan manager may decide to seek out reasonably available index fund alternatives that are not associated with such a strategy. For the BlackRock funds to become more desirable for inclusion in a plan's investment portfolio or be used in self-directed accounts, it would appear that BlackRock could create a firewall between funds that are to be included in ERISA plans and those that are not. The former would somehow not be associated with the current engagement strategy implemented by its investment stewardship team. Or, BlackRock could simply shut down its engagement strategy until it could implement a strategy of shareholder activism, such as the hedge fund approach proposed by Bebchuk and Hirst, that would not be expected to have a negative financial impact.

While the focus of this Article is on BlackRock's delegated voting authority and associated shareholder activism, it is meant to apply to any and all investment advisers who attempt to leverage their delegated voting authority for purposes of engaging in such activism. Moreover, the DOL should provide guidance to plan managers on when the investment products of investment advisers with delegated voting authority need to be excluded.

144. Bebchuk & Hirst, *Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy*, *supra* note 15.