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Michal Barzuza, Quinn Curtis & David H. Webber, *Shareholder Value(s): Index Fund ESG Activism and the New Millennial Corporate Governance*, 93 **S. Cal. L. Rev.** __ (forthcoming, 2020), available at SSRN.

Index funds have become a subject of intense scrutiny, first and foremost, because they are enormous. BlackRock, Vanguard, and State Street – the "big three," with several trillion dollars in assets under management collectively – control around one-quarter of the stock of the S&P 500 companies. Accordingly, there is keen interest in understanding how they exercise the rights associated with that mountain of stock. As a threshold matter, why exert themselves at all, when their passive management model thrives on low fees, and therefore low costs? And why, despite these incentives, have they become increasingly vocal on sustainability-related matters, sometimes described as "environmental, social, and governance" (ESG) issues? As Michal Barzuza, Quinn Curtis, and David Webber argue in the paper cited above, the answer may relate to an overlooked dimension of the competition among these major institutions – the urgent effort to attract Millennial assets.

Whereas actively managed funds aim to beat the market, and accordingly compete on performance, index funds simply aim to match the market, and accordingly compete on price. Index funds cannot sell underperforming stocks because, by definition, they track a particular index, and they would seem to lack any straightforward incentive to engage in activism because this drives up costs and correlatively diminishes the competitiveness of their fees. As the authors acknowledge, this view of the matter is consistent with evidence showing that "index funds vote their proxies, but rarely initiate shareholder action, and have small – but growing – corporate governance operations."

Nevertheless, Barzuza, Curtis, and Webber document "extensive index fund activism around board diversity and other social issues." Notably, these index funds "have not been afraid to aggressively challenge boards when companies are not responsive to calls for gender diversity, including voting against current directors" – an approach initially adopted by State Street and followed soon thereafter by others. Meanwhile, climate change has also become a major focus, with BlackRock leading the charge and others following suit.

How might this be squared with the fee structure and associated incentives described above? Given the mixed results of the empirical literature, the authors argue that "conventional shareholder value creation is unlikely to explain index funds' commitment to promoting diversity." Meanwhile, given the Department of Labor's skepticism regarding the compatibility of ESG investment with investment duties under ERISA – applicable to 401(k) plans, from which "the big three hold vast sums" – they argue that "regulatory uncertainty around index funds' social activism … is evidence against the view that these governance interventions are explained as a means of staving off regulatory intervention."

A more plausible explanation, they argue, lies in a different direction – an increasingly heated competition to secure assets from investors who increasingly care about these issues. "In the coming decades," they observe, "between $12 and $30 trillion will be transferred to Millennials," generally understood to mean those born in the 1980s and 1990s. This will represent "the largest intergenerational wealth shift in history," and a growing body of research indicates that Millennial investors are more likely to invest based on ESG considerations than are others. These developments have not been lost on the big index funds, which "are taking Millennial wealth seriously." Accordingly, "competition for their assets – and future assets – has already begun in earnest."

The authors' novel insights certainly provide a helpful means of understanding the index funds and their role in corporate governance generally. At the same time, however, the evidence that they marshal to support their argument may also illuminate the degree to which various forms of sustainability-related initiatives might plausibly be advanced by this important category of institutional investors. Notably, the tension they cite between the desire to "avoid challenging management because they fear loss of access to companies' 401(k) platforms," on the one hand, and the desire to appeal to Millennial investors, on the other, may help explain why the index funds have pursued some ESG issues more energetically than others. For example, they suggest that "fear of confronting management may explain index funds' more cautious approach to climate change so far." Whereas "Millennials care about both diversity and climate, the gender composition of a corporate board is a far less sensitive issue for most firms than their carbon footprint." Accordingly, index funds may "intervene aggressively when the cost is low and tread lightly when it is not." In each context, they argue, it is "a straightforward cost-benefit calculation."

Clearly much work remains to be done regarding the significance and impacts of the business models and ESG-related activism of index funds. Likewise, Millennial wealth and values will remain dynamic subjects of study for decades to come. In the meantime, Barzuza, Curtis, and Webber's analysis sheds new light on their complex interactions, and reveals dynamics that may have profound impacts on these investment structures and their potential to promote corporate sustainability.

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