Voting Engagement by Large Institutional Investors

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"We're riding in a car we can't get out of . . . . Governance is the seat belt and air bag."[1] – Glenn Booraem, Principal and Investment Stewardship Officer, The Vanguard Group, Inc.

While shareholder stewardship has captured much attention recently, the evidence on the role of large institutional investors remains relatively scarce. Large fund families have become an increasingly powerful force since the financial crisis of 2008, but the prevailing view holds that fund managers avoid active shareholder oversight. This study aims to contribute to the ongoing discussions about the stewardship role of large institutional investors by revealing how the biggest investors in companies listed on the London Stock Exchange behave and vote at shareholders' meetings. The results show growing shareholder stewardship efforts by large asset managers, including index (often described as passive) fund managers, over the last five years and thus challenge some common assumptions about large institutional investors. Although the shareholder opposition rate to management proposals, many of which are trivial, remains economically minor, the relative change over time is significant. The study also reveals that the primary target of investor oversight by large fund managers has been corporate governance standards and global challenges shared across many companies and countries, rather than business strategy or performance. These findings have important implications and will better inform discussions and efforts to build regulatory frameworks for effective shareholder stewardship and engagement in publicly traded companies. The results suggest that regulators need to remain realistic by not placing impractical stewardship expectations on large institutional investors alone. To go beyond governance engagement, regulatory efforts need to take a broader approach towards investor stewardship and shareholder rights. In particular, hedge funds and other shareholder activists can improve corporate strategy and operational oversight by supplying large fund managers with firm-specific

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1. Sarah Krouse et al., *Meet the New Corporate Power Brokers: Passive Investors*, WALL ST. J. (Oct. 24, 2016), https://www.wsj.com/articles/the-new-corporate-power-brokers-passive-investors-1477320101 [https://perma.cc/BKP5-KLJP].

information through activist demands.

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I. INTRODUCTION

We have been witnessing important developments on the front of shareholder stewardship. Shareholder voting, once an overlooked aspect of corporate governance, has increased in importance during the last decade. Initial corporate governance measures focused almost exclusively on the structure, composition, and practices of corporate boards.[2] The 2008 financial crisis and recent corporate scandals reinforced beliefs that

2. *See, e.g.*, COMM. ON THE FIN. ASPECTS OF CORP. GOVERNANCE, REPORT OF THE COMMITTEE ON THE FINANCIAL ASPECTS OF CORPORATE GOVERNANCE ¶ 1.8 (1992),

shareholder apathy may have contributed to increased risk-taking and director misconduct.[3] The predominantly board-centric focus of corporate governance measures has thus gradually shifted towards the recognition of the importance of shareholder engagement. When the United Kingdom published the Stewardship Code in 2010 with an intention to strengthen shareholder engagement in corporate governance, it was the only country with a code offering a set of best practice recommendations for institutional investors in publicly traded companies.[4] Many countries have followed suit; there are now about 20 stewardship codes in place around the world.[5] This number is set to increase further as the recently adopted Shareholder Rights Directive II essentially requires the implementation of minimum stewardship practices in all European Union (E.U.) countries.[6]

Recognition of the stewardship role of shareholders also led to the expansion of shareholder rights. For example, legislatures in several major jurisdictions either introduced or strengthened say-on-pay votes for executive compensation in the aftermath of the 2008 financial crisis.[7] These votes may be binding or non-binding. In the United Kingdom, shareholders of publicly traded companies approve the company's general director remuneration pay policy through a binding vote once every three years[8] and a director pay report annually in a non-binding vote.[9] The Shareholder Rights Directive II expands say-on-pay rules across the entire E.U.[10]

Hedge fund activism has further enhanced the importance of shareholder voting. Whereas previously many shareholder votes were mere formality with high approval rates, the rise of activist investors has increased the number of contested votes.[11] As a result, there are more and more closely fought votes on mergers, director elections, and other non-routine matters subject to shareholder vote.[12] Accordingly, although shareholders vote on relatively few matters,[13] shareholder voting has become one of the pillars of corporate governance.

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http://www.ecgi.org/codes/documents/cadbury.pdf [https://perma.cc/4UUJ-7MMN] (stating that the Report's corporate governance proposals aim to strengthen boards and their effectiveness; the main proposals thus focused on the role of non-executive directors and board committees). The Report is better known as the Cadbury Report, named for the Committee's Chairman.

3. *See, e.g.*, Iris H-Y Chiu, *Institutional Shareholders as Stewards: Toward a New Conception of Corporate Governance*, 6 BROOK. J. CORP. FIN. & COM. L. 387, 387 (2012).

4. FIN. REPORTING COUNCIL, PROPOSED REVISION TO THE UK STEWARDSHIP CODE 8 (2019), https://www.frc.org.uk/getattachment/dff25bf9-998e-44f6-a699-a697d932da60/;.aspx [https://perma.cc/4Q5K-C7N8].

5. Owen Walker, *Beacon of British Stewardship Needs a Brighter Flame to Beat Brexit*, FIN. TIMES (Jan. 26, 2019), https://www.ft.com/content/1a3a57be-5c15-3e03-bae0-10bd5804bf20.

6. Directive 2017/828, of the European Parliament and of the Council of 17 May 2017 Amending Directive 2007/36/EC as Regards the Encouragement of Long-Term Shareholder Engagement, art. 1, 2017 O. J. (L 132) 1, 16–19 [hereinafter Shareholder Rights Directive II].

7. For an overview of say-on-pay rules in eight major countries, see Randall S. Thomas & Christoph Van der Elst, *Say on Pay Around the World*, 92 WASH. U. L. REV. 653, 658–710 (2015).

8. COMPANIES ACT 2006, c. 46 s. 439(1), (5).

9. COMPANIES ACT 2006, c. 46 s. 439A(1).

10. Shareholder Rights Directive II, *supra* note 6, art. 1, at 19–21.

11. *See* Marcel Kahan & Edward Rock, *The Hanging Chads of Corporate Voting*, 96 GEO. L.J. 1227, 1229 (2008).

12. *Id.* at 1229–30.

13. For the typical list of matters subject to shareholder vote, see *infra* notes 70–71 and accompanying text.

In parallel to the increasing role of shareholder voting, a small group of large institutional investors has been amassing voting rights in publicly traded companies worldwide. The world's largest asset manager by assets, BlackRock Inc., attracted $1 billion of new client money on average every day during 2017, passing the threshold of $6 trillion in assets under management by the end of the year.[14] Another giant investment manager, The Vanguard Group, Inc., which collected even more money, reached $5 trillion in assets under management in 2017, up from $77 billion 25 years ago.[15] Cash inflows into passive funds, although still impressive, somewhat slowed down in 2018 mainly driven by investor uncertainty about the prospects of stock markets amid escalating "trade wars" and political uncertainty in Europe.[16] But the competitive needs to cut management costs have spurred a wave of mergers in the asset management industry, thus further strengthening the voting power of a small number of large managers.[17]

Big asset managers are now among the largest shareholders of publicly traded companies in many developed countries and are thus in a strong position to influence corporate decision-making.[18] With increasing investments of large fund families in shares of publicly traded companies comes increased scrutiny of their behavior as shareholders. Notwithstanding the importance of large institutional investors, however, we have surprisingly little systematic knowledge how they approach shareholder voting. It is not clear whether large institutional investors practice what they preach about the importance of voting as a corporate governance mechanism and whether the increased attention to voting from policymakers has translated into enhanced shareholder engagement efforts by institutional investors. The existing literature is based on data from U.S. mutual funds; discussions in other countries, meanwhile, rely mostly on insights from occasional news publications. Lack of systematic evidence, however, has not prevented a range of accusations, including that fund managers give priority to short-term targets over the long-term growth of the portfolio companies;[19] prefer to sell shares rather than engage in voting activism;[20] are so deferential to company managers[21] that they constitute "absentee" or "reluctant" owners.[22] Although often based on anecdotal evidence, almost every discussion

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14. *See* Sarah Krouse, *BlackRock Takes in a Record Cash Haul*, WALL ST. J., Jan. 13-14, 2018, at B10.

15. *See* Sarah Krouse, *Vanguard "Just Getting Started"*, WALL ST. J., Jan. 5, 2018, at B2.

16. *See* Dawn Lim, *BlackRock Assets Drop Sharply*, WALL ST. J., Jan. 17, 2019, at B1, B10; Chris Flood, *ETF Growth Sputters in 'Rocky' 2018*, FIN. TIMES, Jan. 14, 2019, at 2 (UK ed.); Chris Flood, *Vanguard is Still Fastest-Growing Fund Manager*, FIN. TIMES, Jan. 7, 2019, at 1–2 (UK ed.); Asjylyn Loder, *BlackRock Squeezed as Investors Pivot*, WALL ST. J., July 17, 2018, at A1, A2.

17. *See* JACKIE COOK & JASMIN SETHI, MORNINGSTAR, ASSET MANAGERS AS STEWARDS OF SUSTAINABLE BUSINESS: IMPLICATIONS OF THE RISE IN PASSIVE INVESTING 1–2 (2019), https://www.morningstar.com/lp/asset-managers-role [https://perma.cc/3QWZ-PLL4].

18. *See infra* Part II.

19. *See, e.g.*, JOHN KAY, THE KAY REVIEW OF UK EQUITY MARKETS AND LONG-TERM DECISION MAKING: FINAL REPORT (2012), https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/253454/bis-12-917-kay-review-of-equity-markets-final-report.pdf [https://perma.cc/FR6W-L9PE].

20. *See id.* at 42; James Cotter et al., *ISS Recommendations and Mutual Fund Voting on Proxy Proposals*, 55 VILL. L. REV. 1, 15, 22 (2010); Bernard S. Black & John C. Coffee, Jr., *Hail Britannia?: Institutional Investor Behavior Under Limited Regulation*, 92 MICH. L. REV. 1997, 2053 (1994).

21. *See* Cotter et al., *supra* note 20, at 15; Black & Coffee, Jr., *supra* note 20, at 2039.

22. *See, e.g.*, Alan Sykes, *Proposals for Internationally Competitive Corporate Governance in Britain and America*, 2 CORP. GOV.: INT'L REV. 187, 188 (1994); *Survey of Corporate Governance: Reluctant Owners*, ECONOMIST, Jan. 29, 1994, at 16–17. The term "absentee owners" was coined by Merrick Dodd to describe

of the role of large institutional investors builds on these assumptions.[23]

Recent governance initiatives led by large institutional investors suggest, however, the reality may be different or, at least, has been changing. Consider, for example, the decision of State Street Global Advisors (State Street or SSGA), the world's third largest asset manager with more than $2.8 trillion in assets under management, to vote against the re-election of directors at 400 companies in 2017 on grounds that these companies failed to take significant steps in improving gender diversity on corporate boards.[24] Similarly, Laurence (Larry) Fink, the Chairman and CEO of BlackRock, has repeatedly called for companies to better explain their long-term strategies and societal impact.[25] In his recent annual letter to chief executives of companies in which BlackRock invests, Mr. Fink promised to strengthen shareholder engagement.[26] Shortly after this, BlackRock updated its proxy voting guidelines explicitly to promote board diversity by requiring its portfolio companies to have at least two female directors.[27] BlackRock, Vanguard, and State Street also vote or plan to vote against board candidates that serve at multiple boards on a premise that they lack time to perform adequately.[28] BlackRock, for example, cast 168 votes against directors because of "overboarding" concerns in the first three quarters of 2017.[29] The latest examples come from the London-based Legal & General Investment Management Limited (LGIM or Legal & General) which reiterated its policy of voting against the chairman of any board of directors where the share of female directors has not reached at least one-quarter.[30] Legal & General made further updates in its voting guidelines in 2019 by promising to vote against directors that hold an executive position in one company and have more than one outside director role at any other board.[31]

This study aims to fill the information vacuum about the voting behavior of large fund managers by offering evidence on their shareholder engagement efforts in U.K. listed companies. That fund managers fail to exercise stewardship is a hypothesis, not an axiom.

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dispersed individual minority shareholders without much power to influence powerful company CEOs. *See* E. Merrick Dodd, Jr., *For Whom Are Corporate Managers Trustees?*, 45 HARV. L. REV. 1145, 1153 (1932).

23. The common accusations that institutional investors and asset managers focus too much on short-term returns and do not engage with companies in which they hold shares appear also in the European Union's recent Shareholders Rights Directive II. *See* Shareholder Rights Directive II, *supra* note 6, recitals 2, 15, at 1, 3.

24. *See* Geoffrey Rogow, *Group Seeks to Close Wall Street's Gender Gap*, WALL ST. J., July 29-30, 2017, at B10; Justin Baer & Joann S. Lublin, *State Street Falls Short in Bid for Women Directors*, WALL ST. J., July 27, 2017, at B10. None of the 400 companies had a single female director. The fund manager voted against all directors responsible for nominating new board members at each of these companies.

25. *See* Sarah Krouse, *BlackRock's Fink Pledges to Intensify Shareholder Activism*, WALL ST. J., Jan. 17, 2018, at B12.

26. *See* Larry Fink, *Annual Letter to CEOs: A Sense of Purpose*, BLACKROCK, https://www.blackrock.com/corporate/investor-relations/2018-larry-fink-ceo-letter [https://perma.cc/95JR-5SK3] (last visited Feb. 24, 2020) ("The time has come for a new model of shareholder engagement – one that strengthens and deepens communication between shareholders and the companies that they own.").

27. *See* Sarah Krouse, *BlackRock Presses Board Makeup*, WALL ST. J., Feb. 3-4, 2018, at B10.

28. *See* Cara Lombardo & Dawn Lim, *Vanguard Sets Sights on Board Members*, WALL ST. J., Apr. 12, 2019, at B1, B10; Sarah Krouse & Joann S. Lublin, *Directors Are Told: Don't Go "Overboard"*, WALL ST. J., Sept. 27, 2017, at B1.

29. *See* Krouse & Lublin, *supra* note 28, at B11.

30. *See* LEGAL & GEN. INV. MGMT., ACTIVE OWNERSHIP: POSITIVE ENGAGEMENT TO ENHANCE LONG-TERM VALUE 26 (2018), http://www.lgim.com/files/_document-library/capabilities/cg-annual-report-2017-full.pdf [https://perma.cc/NR9E-86JB].

31. *See* Owen Walker, *LGIM Toughens Stance on 'Overboarding' Directors*, FIN. TIMES (Apr. 15, 2019), https://www.ft.com/content/cc5411d7-4619-30f3-b275-463096cad117.

The increasing significance of shareholder voting in corporate governance and global efforts to build regulatory frameworks for effective stewardship require a better understanding of how large institutional investors in general, and passive fund managers in particular, perform their investment stewardship role. This information is vital to understanding what kind of shareholder engagement we can realistically expect from institutional investors and, accordingly, how far regulators can go in relying on shareholder oversight as a disciplinary mechanism. Without answering these questions, it is unclear whether further efforts to strengthen shareholder involvement in corporate governance are desirable from a policy perspective.

This study uses the voting records of large fund managers to fill this informational gap and to explore the stewardship role performed by asset managers in the United Kingdom. The study covers every company included in the FTSE 100 index on June 30, 2017. The sample includes votes cast by the largest asset managers at shareholder meetings held during the five-year period from 2013 to 2017. This results in more than 10,500 items voted and above 147,000 votes cast at the shareholders' meetings of the largest U.K. companies by the largest asset managers.[32]

The results of this study suggest a need to rethink some common beliefs about the shareholder engagement of large institutional investors. Voting engagement by big asset managers, including index fund managers, contrary to the prevailing opinion, has been growing in recent years.[33] Although the frequency of votes against management proposals remains low in absolute terms, the relative opposition rate has changed significantly over time.[34] One of the key findings of this study is that large asset managers in the United Kingdom have, in the exercise of their stewardship role, tended to promote universally acknowledged corporate governance standards and actions addressing global challenges which can be applied on an industry-wide basis, rather than focusing on company-specific performance and operational information. For example, the largest institutional investors in listed U.K. companies were engaging actively with some types of proposals, such as voting on compensation-related matters, but were less active in relation to other proposals, such as director elections.[35] This shows that large fund managers, given their limited monitoring resources, have been focusing on promoting standard measures of good governance.

This result resonates strongly with the empirical findings of a study by Lucian Bebchuk and Scott Hirst on the stewardship efforts of the Big Three index funds—BlackRock, Vanguard, and State Street—in U.S. companies in terms of focusing on governance principles and underinvesting in business performance oversight and director elections.[36] But this study offers additional nuances by showing that these stewardship patterns extend beyond index fund managers and that predominantly actively-managed fund families are not better stewards in general.[37] Furthermore, this study shows that stewardship efforts, regardless of investment strategies, differ substantially across fund managers, which means the agency-cost analytic framework of stewardship by large asset

32. For the detailed description of the research design, see *infra* Part IV.A.

33. *See infra* Part IV.B.1.

34. *Id.*

35. *See infra* Part IV.B.2.

36. *See* Lucian Bebchuk & Scott Hirst, *Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy*, 119 COLUM. L. REV. 2029, 2088–91, 2095–2101 (2019).

37. *See infra* Part IV.B.4.

managers offered by Bebchuk and Hirst does not fully explain the voting practices of fund managers.[38] Additional factors other than incentives to maximize net management fees or business ties with portfolio companies must be driving the decisions of fund managers to invest in stewardship. For example, fund manager's individual perspective (ideologies of the manager's top officers) or broader cultural viewpoints dominating in the market where the fund manager operates may influence the role and intensity of stewardship taken by a fund manager.

This study's findings challenge the prevailing assumptions about passive engagement by large fund managers and have important implications both for the ongoing academic discussions on shareholder voting and for the most recent policy proposals to strengthen shareholder engagement. The results suggest that regulators need to remain realistic by not placing impractical engagement expectations on large institutional investors alone. Asset managers face a dilemma of keeping management costs at minimum and strengthening shareholder engagement. Hence, to go beyond governance engagement, regulatory efforts need to take a more holistic approach towards investor stewardship and shareholder rights. In particular, hedge funds and other shareholder activists can improve corporate strategy and performance engagement by supplying large fund managers with firm-specific information through activist demands.

The Article proceeds, in Part II, with documenting the increasing role of the big asset managers among the largest shareholders of companies listed on the London Stock Exchange. Part III offers brief theoretical discussion of the implications of ownership by large fund families, some of which are dominated by passively managed funds, for corporate governance. Part IV presents the practice of voting by the big asset managers and changes over the past five years. Part V discusses the findings and lists some key implications of the empirical study of voting practices by the big fund managers. Conclusions and suggestions for future research directions are in Part VI.

II. THE RISE OF LARGE FUND FAMILIES AND THEIR STRENGTHENED ROLE AS SHAREHOLDERS

Through the control of funds' assets under management, the largest asset managers have amassed significant influence over listed companies. In companies with widespread ownership structures, the largest fund managers are the primary controllers and play an increasingly important role in corporate governance matters. This Part explores the voting power of large fund families in greater detail by studying the ownership structures of U.K. listed companies through the identification of the largest ten shareholders in every FTSE 350 company. Information on the largest shareholders and the size of their shareholdings comes from Thomson ONE Banker's Share Ownership database.

That institutional investors are major owners of publicly traded companies is not in itself a recent phenomenon. This has long been documented and is the consequence of a global move away from direct ownership by individuals and households towards ownership through financial intermediaries, like banks, insurance companies, various investment funds, and pension funds.[39] Today, as 40 years ago, institutional investors are the largest

38. *See id.*

39. GILE R. DOWNES, JR. ET AL., INSTITUTIONAL INVESTORS AND CORPORATE BEHAVIOR 1 (1999); JOHN SCOTT, CAPITALIST PROPERTY AND FINANCIAL POWER: A COMPARATIVE STUDY OF BRITAIN, THE UNITED STATES AND JAPAN 88 (1986); Gerald F. Davis, *A New Finance Capitalism? Mutual Funds and Ownership Re-*

shareholders of U.K. listed companies.[40] What has changed is the identity of the dominant actors.

The leading institutional investors around the globe today are big asset managers, also known as fund managers, fund advisors, or general partners. An asset manager runs an investment fund by giving investment advice.[41] Most large asset managers have advisory relationships with multiple funds which offer various products that can be differentiated based on investment strategy, types of portfolio securities, markets, or the currency of investments. Funds that share a common management company are often referred to as a "fund family" or "fund complex."[42] An asset manager is responsible for voting the shares owned by funds affiliated with it.

Asset managers employ two primary strategies for managing investment funds—active and passive management. Active management, which traditionally used to be the only way of investing, involves making investment decisions by picking financial instruments and deciding when to buy or sell. The success of an actively managed fund hinges on the ability of the fund's manager to beat the market by identifying promising investment opportunities, thus delivering superior returns over a market benchmark, like FTSE or S&P indexes. This measure of return is referred to as "alpha."

Passive management, by contrast, attempts to deliver a market return by building a portfolio that mirrors the entire market. For example, a passively managed fund may buy shares in every company included in a given stock index in proportion to the weight of each company in the index and produce returns that match the rate of return of the overall market, minus costs of the management. For this reason, passive funds are often referred to as "index" or, in British terminology, "tracker" funds. Unlike in an actively managed fund, the role of a passive fund's management company in investment decisions comes down to closely tracking a specific index. This minimal role results in reduced management costs and, therefore, in cheaper financial products for investors.[43]

Big asset managers have become a powerful force since the financial crisis of 2008. They filled the void left by banks, which were scaling back.[44] Consequently, the holdings

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Concentration in the United States, 5 EUR. MGMT. REV. 11, 15 (2008).

40. There is no standard way of measuring common ownership—where an investor owns shares in two or more companies—by institutional investors. Some studies simply count the number of times an investor appears among the shareholders of different companies; others use a minimum shareholding threshold to exclude instances of insignificant share ownership from calculations; the third group of studies calculates the simple or asset-weighted average shareholding of an investor in two or more companies. For more detailed methodological discussion of quantifying common ownership and a proposal of a new measure, see Erik P. Gilje et al., *Who's Paying Attention: Measuring Common Ownership and Its Impact on Managerial Incentives* 9–20 (Nat'l Bureau of Econ. Research, Working Paper No. 25644, forthcoming 2020).

41. John Morley, *The Separation of Funds and Managers: A Theory of Investment Fund Structure and Regulation*, 123 YALE L.J. 1228, 1238–39 (2014).

42. *Id.* at 1239.

43. So called "smart beta" funds, which use algorithms to design winning investment strategies, blur the lines between the traditional division of funds into active and passive. On the one hand, smart beta funds rely on factors typically used by active managers, such as value versus growth stocks, dividend yield, and momentum, for identifying winning stocks. On the other hand, smart beta funds, like passively managed funds, follow an originally designed investment strategy and do not involve an active manager who picks the portfolio, thereby reducing management costs. Martin Lettau & Ananth Madhavan, *Exchange-Traded Funds 101 for Economists*, 32 J. ECON. PERSP. 135, 144–45 (2018).

44. For example, in June 2009, BlackRock announced the acquisition of Barclays Global Investors, the asset management subsidiary of Barclays PLC, a British bank. Financial troubles forced Barclays to sell one of

of banks and insurance companies have gradually declined in relative importance to holdings by fund families managed by independent asset managers. The increasing popularity of big passive fund managers, primarily BlackRock and Vanguard, has certainly contributed to this change.[45] Along with the rapid growth in assets under management came the increased clout of investment managers in financial markets and corporate governance matters.

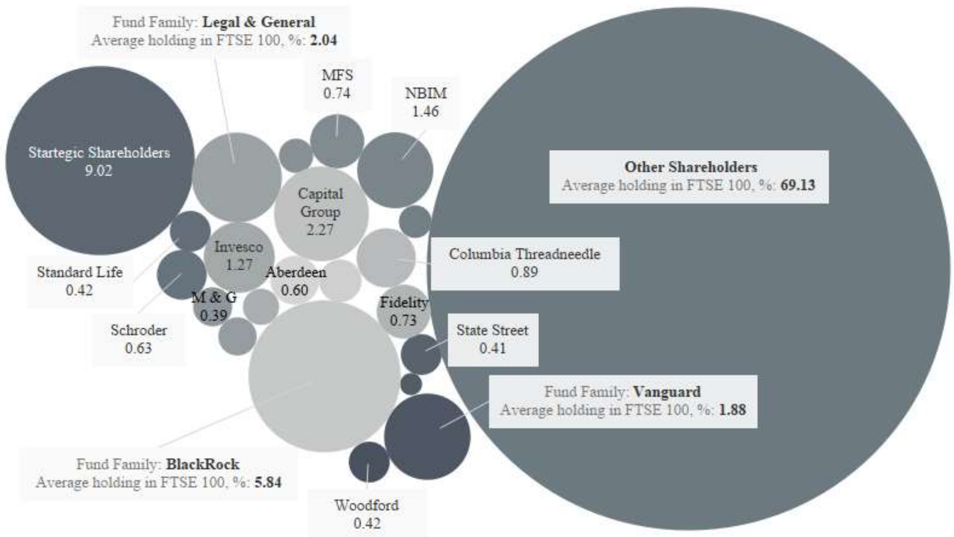
In the United Kingdom, BlackRock funds owned 5.84% of the FTSE 100 companies in 2017 (Figure 1). Other big fund families, like Legal & General, Norges Bank Investment Management (NBIM), and Vanguard, typically held shareholdings below 3%. The largest five asset managers controlled together about 13.5% of the FTSE 100 companies in 2017.

Figure 1. Voting Power of Big Asset Managers in the FTSE 100 Companies, 2017[46]

its most lucrative assets, including the iShares unit which was at the time the leader in the business of passive exchange traded funds. Attracta Mooney & Peter Smith, *Deal of the Decade: How BlackRock Buying BGI Changed the Industry*, FIN. TIMES (May 6, 2019), https://www.ft.com/content/48e703d8-6d87-11e9-80c7-60ee53e6681d.

45. A recent empirical study offers evidence linking the rise of index investing with the increased level of common ownership of publicly traded companies, but the study refrains from making any causal claims. *See* Gilje et al., *supra* note 40, at 29.

46. Ownership data collected from Thomson ONE Banker's Share Ownership database.



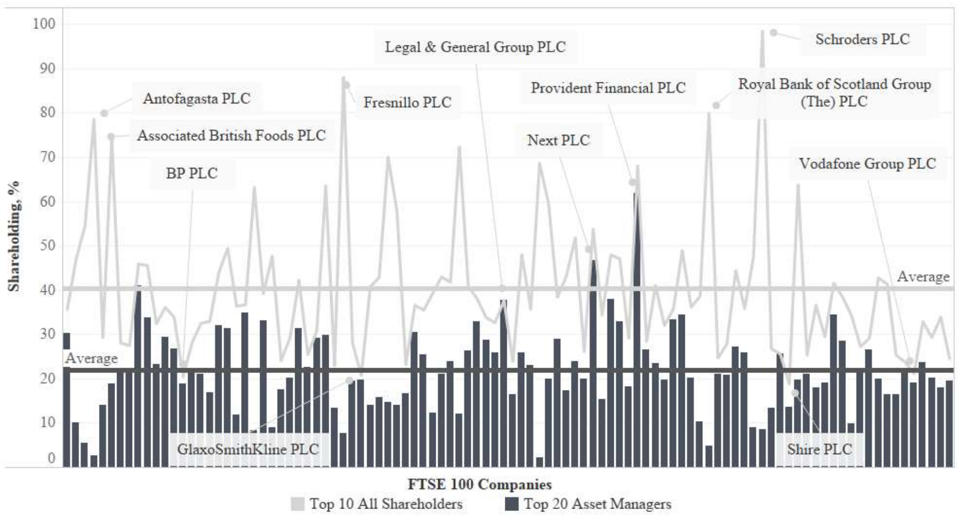
Note: The reported results include only those shareholdings where an asset manager was among the top 10 shareholders of an FTSE 100 company. The share of the largest asset managers in the FTSE companies will be higher if the average calculations include asset managers' all shareholdings, including situations where the shareholding is smaller and thus is not reported among the list of top 10 shareholders.

Figure 2 compares the combined holdings of the largest 10 shareholders overall and of the largest 20 asset managers in all FTSE 100 companies. On average, the biggest 10 shareholders owned 40.32% of the FTSE 100 companies. Remarkably, more than half of this share (21.85%) was controlled by the 20 largest asset managers. The combined holdings of the top 20 asset managers were above 30% in 16 companies with the largest shareholding exceeding 60%.

In contrast, strategic shareholders—such as company founders, managers, or government agencies—played more modest roles. Forty companies had at least one strategic entity among their top 10 shareholders with an average FTSE 100 shareholding of just above 9%. In many of the remaining companies, all top 10 shareholders were asset managers.[47] Moreover, often the largest strategic shareholders had minority stakes: only in 24 companies the combined holdings of strategic entities exceeded 5% and only in 15 companies were these holdings 25% or higher.

47. Legal & General Group PLC is the only company where all top ten shareholders are from the list of the 20 largest asset managers with a combined share of 37.74%.

Figure 2. The Ownership Structure of the FTSE 100 Companies, 2017[48]



Big asset managers wielded substantial voting power in the FTSE 350 companies as well, but their shareholdings were more evenly distributed without a pronounced leader (compare Figures 1 and 3). In particular, BlackRock funds, the largest investors in the FTSE 350 companies, owned only 3.46% of the FTSE 350 companies in 2017.[49] Nevertheless, the largest 20 investors had comparable voting power in both indexes as they held 21.97% of shares in the FTSE 350 companies, just above of the corresponding holding of the largest asset managers in the FTSE 100 companies. The influence of strategic shareholders was only slightly stronger in the FTSE 350 companies as almost half of the FTSE 250 companies (117 companies) had strategic entities among their top 10 shareholders.[50] Clearly, a group of big investment fund managers, although falling short of effectually controlling U.K. publicly-traded companies, nonetheless, has significant voting power in corporate decision-making.

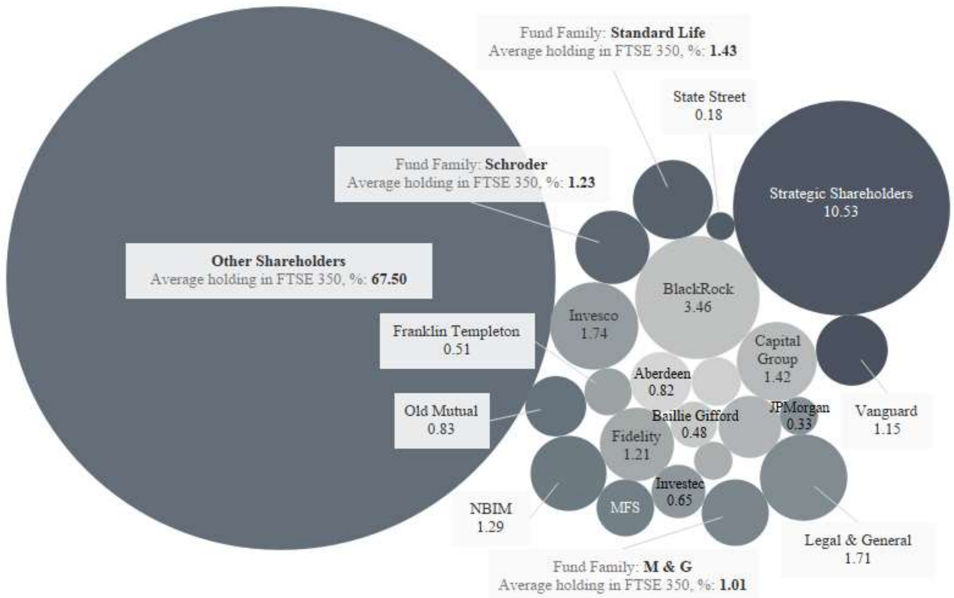
Figure 3. Voting Power of Big Asset Managers in the FTSE 350 Companies, 2017[51]

48. Ownership data collected from Thomson ONE Banker's Share Ownership database.

49. See *infra* Figure 3.

50. The average shareholding of strategic entities with top 10 shareholdings was 11.13%. In 51 companies (20.4% of FTSE 250), strategic shareholdings were 25% or more and in 88 companies (35.2%), strategic shareholdings were higher than 5%.

51. Ownership data collected from Thomson ONE Banker's Share Ownership database.



Note: The reported results include only those shareholdings where an asset manager was among the top 10 shareholders of an FTSE 350 company. The share of the largest asset managers in FTSE companies will be higher if the average calculations include all of the asset managers' shareholdings, including situations where the shareholding is smaller and thus is not reported among the list of top 10 shareholders.

The voting power of the big asset managers becomes more striking when considering the largest shareholdings only.[52] For example, BlackRock and Vanguard were among the top 10 shareholders in 90% of the FTSE 100 companies in 2017 with average shareholdings of 6.49% and 2.09%, respectively. Moreover, BlackRock was the largest shareholder in almost half of these companies, sometimes with shareholdings above 10%. For comparison, strategic entities and sovereign wealth funds were the largest shareholders in only 28 FTSE 100 companies.

The situation was similar in the FTSE 350 companies. Legal & General, the largest U.K.-based asset manager, dominated the list of the largest shareholders of the FTSE 350 companies: the asset manager appeared among the top 10 shareholders in almost three-quarters of the companies included in the index as of June 2017. BlackRock was again the most common largest shareholder (62 companies) but more companies had strategic entities as their largest shareholders—almost one-quarter or 85 FTSE 350 companies. Table 1 below presents the complete results on the top 20 shareholders in the largest 350 UK publicly traded companies: Panel A focuses on the FTSE 100 companies and Panel B offers evidence for the FTSE 350 companies.

52. See *infra* Table 1.

Table 1. The Largest Shareholders in UK Listed Companies, 2017[53]

The table shows the largest shareholders in U.K. listed companies in 2017 by the number of times a shareholder appears among the top 10 shareholders. All largest shareholders are asset managers. An asset manager may control shareholdings through more than one investment fund affiliated with the manager. The table reports the combined results of all funds affiliated with an asset manager. The table also reports the number of companies where an asset manager is the single largest shareholder and typical shareholding sizes (average, median, maximum, and minimum). Panel A presents data on the largest shareholders of the FTSE 100 companies; the combined results for the FTSE 350 companies are in Panel B.

53. The data were collected from Thomson ONE Banker's Share Ownership database.

Panel A. The Largest Shareholders in the FTSE 100 companies

#	Asset Manager	Country	Firms with top 10 shareholder	Firms with top shareholder	Average holding, %	Median holding, %	Maximum holding, %	Minimum holding, %
1	BlackRock Inc.	USA	90	43	6.49	6.04	12.62	0.57
–	The Vanguard Group, Inc.	USA	90	0	2.09	2.28	3.16	0.53
3	Legal & General Investment Management Ltd.	UK	87	0	2.35	2.42	4.03	0.53
4	Norges Bank Investment Management (NBIM)	Norway	61	2	2.39	2.02	8.99	0.51
5	Capital Group	USA	40	8	3.99	5.03	15.82	1.16
6	Aberdeen Asset Management*	UK	30	0	2.01	1.41	4.99	0.82
7	Invesco Ltd.	USA	26	1	4.69	4.82	18.99	1.06
–	State Street Global Advisors	USA	26	0	1.45	1.41	3.20	1.01
9	Columbia Threadneedle Investments (UK)	UK	23	2	3.85	3.98	9.94	1.18
10	Schroder Investment Management Ltd. (SIM)	UK	18	1	3.48	3.13	11.17	0.61
–	M&G Investment Management Ltd.	UK	18	0	2.14	1.72	5.24	0.69
12	Fidelity Investments**	USA	15	4	4.87	4.07	13.25	0.88
13	Artemis Investment Management LLP	UK	14	1	3.29	3.04	6.71	1.07
14	MFS Investment Management	USA	13	1	5.27	5.09	10.72	1.27
15	Standard Life Investments Ltd.*	UK	10	1	4.23	3.75	10.96	1.67
–	Franklin Templeton Investments	USA	10	0	3.03	3.15	6.17	0.89
–	Newton Investment Management Ltd.	UK	10	0	2.71	2.03	5.16	1.27
18	Woodford Investment Management Ltd.	UK	9	0	4.70	3.12	18.6	1.22
–	Lindsell Train Limited	UK	9	0	4.12	5.00	6.52	1.35
–	Marathon Asset Management LLP	UK	9	0	3.32	3.25	5.84	1.65
–	T. Rowe Price Group, Inc.	USA	9	0	1.24	1.35	2.39	0.59

Panel B. The Largest Shareholders in the FTSE 350 companies

#	Asset Manager	Country	Firms with top 10 shareholder	Firms with top shareholder	Average holding, %	Median holding, %	Maximum holding, %	Minimum holding, %
1	Legal & General Investment Management Ltd.	UK	251	1	2.38	2.34	5.60	0.17
2	BlackRock Inc.	USA	199	62	6.09	5.54	19.81	0.22
3	The Vanguard Group, Inc.	USA	195	0	2.07	2.23	3.83	0.29
4	Norges Bank Investment Management (NBIM)	Norway	163	2	2.77	2.56	9.51	0.46
5	Aberdeen Asset Management*	UK	99	2	2.89	2.25	10.62	0.36
6	M&G Investment Management Ltd.	UK	93	3	3.80	3.11	15.57	0.46
7	Standard Life Investments Ltd.*	UK	83	16	6.05	5.04	13.85	0.86
8	Schroder Investment Management Ltd. (SIM)	UK	82	9	5.25	4.81	18.01	0.61
9	Capital Group	USA	78	15	6.36	5.08	19.83	0.53
–	Fidelity Investments**	USA	78	14	5.43	4.85	28.95	0.39
11	Invesco	USA	69	17	8.85	4.96	30.52	1.06
12	Columbia Threadneedle Investments (UK)	UK	63	7	4.91	4.90	17.99	0.00
13	Old Mutual Global Investors	UK	52	5	5.61	4.83	19.32	0.39
14	Investec Asset Management	UK	45	5	5.08	4.95	13.97	0.46
–	Artemis Investment Management LLP	UK	45	3	4.24	4.48	9.96	0.74
16	Franklin Templeton Investments	USA	42	1	4.25	4.24	16.79	0.89
17	Baillie Gifford & Co.	UK	40	0	4.21	4.11	8.32	0.92
–	State Street Global Advisors	USA	40	0	1.58	1.34	3.87	0.36
19	MFS Investment Management	USA	39	9	6.67	5.25	15.26	1.27
20	JPMorgan Asset Management U.K. Limited	UK	38	1	3.07	2.93	8.25	0.44
–	Dimensional Fund Advisors, L.P.	USA	38	0	3.00	2.97	6.33	0.50

Notes: * Aberdeen Asset Management and Standard Life Investments agreed to merge in March 2017. The merger was completed in August 2017 with the merged company named Aberdeen Standard Investments.

** The reported results for Fidelity Investments do not include holdings controlled by Fidelity International, an independent asset manager. Fidelity International, formerly Fidelity Worldwide Investment Ltd., was established in 1969 as the subsidiary of Fidelity Investments to serve non-U.S. markets. It was spun off in 1980 and is currently controlled by its employees, although the founding family of Fidelity Investments continues owning a substantial minority shareholding in Fidelity International. Fidelity International appeared among the top 10 shareholders of the FTSE 100 and the FTSE 350 companies seven and 17 times, respectively, and thus falls outside the Table's top-20 list of asset managers.

The influence of large shareholders is stronger in practice given the actual corporate voting turnout. In companies with many shareholders—all publicly traded companies certainly meet this test—not all shareholders vote their shares. Data on shareholder voting turnout, a measure showing the percentage of total outstanding shares voted during the general meetings of shareholders, show that the average attendance rate in U.K. companies has been just above 70% over the recent years. The average voting turnout at the FTSE 100 companies stood at 73% both during the 2016 and 2017 annual general meetings and increased to 75% in 2018; the overall voting level at the 2016-2018 annual general meetings of the FTSE 250 companies, due to more concentrated ownership structures, was at 77-78%.[54] This means that a shareholding of around 37-40% may give its holder an effective control over shareholder decision-making.[55] Accordingly, the top 10 shareholders, which are commonly institutional investors, with their average combined holdings above 40%, often control the majority of votes at the annual meetings of the FTSE companies; substantial role among these institutional investors belongs to the largest 20 asset managers.

The big asset managers differed in their dominant investment strategies (Figure 4). The largest index managers, which also appear to be the largest managers by total assets under management, are the U.S. giants—BlackRock, Vanguard, and State Street. Passive investing is less common outside the United States. The largest U.K.-based fund managers follow active investment strategies more often, with only a few managing large passive index tracker funds. Legal & General is one of the few U.K.-based managers with substantial passively-managed funds—at 47% of the total assets.

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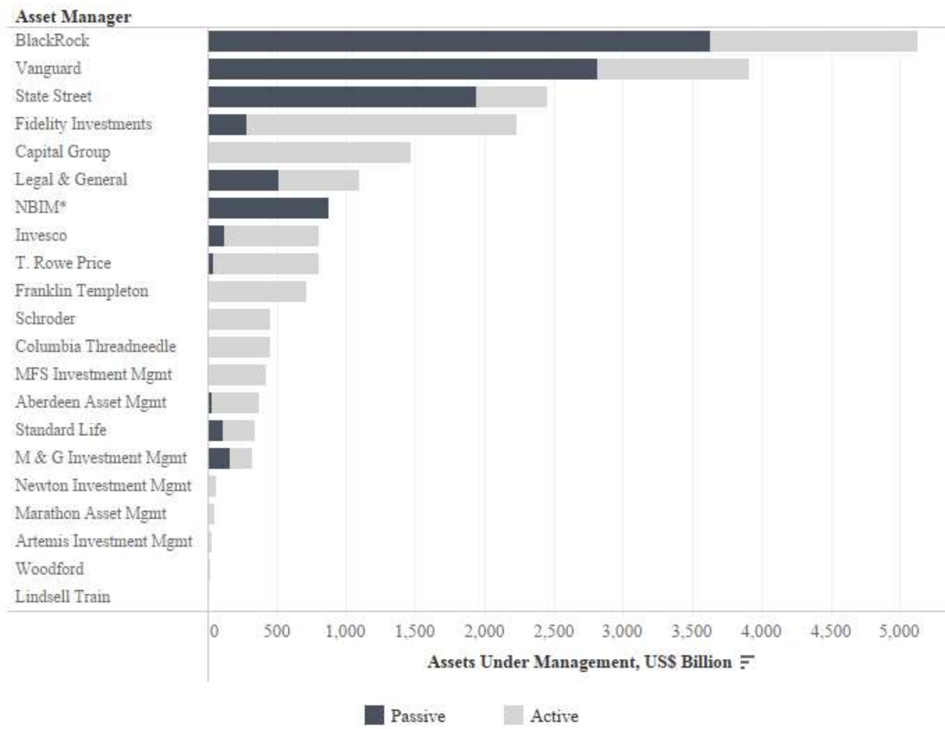
54. *See* KPMG, THE 2017 AGM SEASON—FINAL REVIEW 3 (Jan. 2018), https://assets.kpmg.com/content/dam/kpmg/uk/pdf/2018/01/makinson-cowell-review-of-the-2017-agm-season-january-2018.pdf [https://perma.cc/9TMU-TVBL]; KPMG, REVIEW OF THE 2018 AGM SEASON 3 (Sept. 2018), assets.kpmg/content/dam/kpmg/uk/pdf/2018/09/review-of-the-2018-agm-season.pdf [https://perma.cc/3HUW-AJ73]. Shareholder attendance rate in U.K. companies, perhaps driven by the concentration of shares in the hands of large institutional investors, has been increasing gradually over the last decade. Particularly, the average shareholder turnout of FTSE 100 companies was at 67.9% in 2010. *See* ANNE LAFARRE, THE AGM IN EUROPE: THEORY AND PRACTICE OF SHAREHOLDER BEHAVIOR 109 (2017).

55. Shareholder voting participation rates are similar in U.S. companies: total participation in all Russel 3000 firms between 2003-2013 was 77%. *See* Dragana Cvijanovic et al., *Free-Riders and Underdogs: Participation in Corporate Voting* 19, 45 (European Corporate Governance Institute, Finance Working Paper No. 649/2020, 2020), https://ssrn.com/abstract=2939744 [https://perma.cc/8HGR-CTB6].

Figure 4. Investment Strategies of the Big Asset Managers, Dec. 31, 2016[56]



Note: * NBIM is a special case with an investment approach that is a middle ground between index-based passive and active management. NBIM follows a fixed benchmark index, which is based on FTSE and Bloomberg Barclays Indices, but it also uses active investment strategies in picking stocks from the benchmark index.[57] NBIM's flexible approach to index-oriented investment aims largely to accommodate requirements and expectations of responsible and environment-related investments.[58]

56. Investment & Pensions Europe (IPE); Morningstar; asset managers.

57. In the asset manager's own words, its investment strategy is "wide-ranging and complex" as it "has an investment approach that is index-oriented but where all of the investment strategies are active." *See Letter to the Ministry of Finance: Review of Norges Bank's Management of the Government Pension Fund Global*, NBIM 12 (Dec. 15, 2017), https://www.nbim.no/contentassets/f74931522d4a48b4bfec23679b4a6f64/20171215-mof-review-of-fund-management-gpfg.pdf [https://perma.cc/56QL-4S7U].

58. *See Investment Strategy*, NBIM, https://www.nbim.no/en/the-fund/how-we-invest/investment-strategy/ [https://perma.cc/QY39-8Y89] (last visited July 24, 2018).

The next key question is how large fund families are using their voting power. Do these asset managers vote against management proposals, thereby challenging management on corporate decision-making? Or do they defer to management and thus suppress the vote of corporate dissidents? But before exploring these questions, the next part maps possible shareholder engagement strategies available to asset managers and discusses theoretical arguments as to whether large asset managers can be active shareholders.

III. THE EFFECT OF INVESTMENT FUND OWNERSHIP ON SHAREHOLDER ENGAGEMENT

A. Shareholder Engagement Strategies Available to Large Asset Managers

There are two traditional ways in which fund managers can engage with their portfolio companies, commonly called "investee companies" in the United Kingdom, in their capacity as shareholders.[59] One option is to "exit" an investment by selling shares when dissatisfied with the company's management. Informed trading can reward good management by increasing share prices and punish bad management by low share prices. Alternatively, asset managers can rely on voice-based strategies by either engaging directly with the management via various forms of behind-the scenes discussions or employing their voting rights to submit and support shareholder proposals or oppose management-sponsored governance initiatives.

1. Exit as an Engagement Strategy

Exit, or the "Wall Street walk," is the optimal way of engaging with portfolio companies for some investors. Weak voting rights give their owners only a little impact and leave minority shareholders with almost no real choice in decision-making.[60] The expected rational behavior of such shareholders then is casting their votes without investing heavily in becoming informed about the vote—for example, by following the third-party proxy advice—or ignoring the vote altogether.[61] By contrast, the shareholder has real influence when deciding to sell shares in one company and invest, instead, in another.[62] This, in turn, motivates the shareholder to make an extra effort to become better informed about the decision by evaluating the prospects of its existing and potential investments.[63] Liquidity of shares is the only major constraint on foot voting, but most publicly-traded companies have liquid share markets.

59. The third engagement option is litigation, but it is rarely practiced by major asset managers. *See* Alexander I. Platt, *Index Fund Enforcement*, 53 U.C. DAVIS L. REV. 1453, 1498–1503 (2020) (describing litigation practices of the largest three index fund managers); Sean J. Griffith & Dorothy S. Lund, *Toward a Mission Statement for Mutual Funds in Shareholder Litigation*, U. CHI. L. REV. (forthcoming 2020) (manuscript at 22–24), https://ssrn.com/abstract=3422910 [https://perma.cc/D2P5-VDCY] (describing litigation by the largest ten U.S. mutual funds); James D. Cox & Randall S. Thomas, *Letting Billions Slip Through Your Fingers: Empirical Evidence and Legal Implications of the Failure of Financial Institutions to Participate in Securities Class Action Settlements*, 58 STAN. L. REV. 411, 424 (2005) (reporting that less than 30% of eligible institutional investors filed claims in securities class action settlements litigated in the U.S. courts).

60. Ilya Somin, *Foot Voting, Decentralization, and Development*, 102 MINN. L. REV. 1649, 1655 (2018).

61. *Id.* at 1656–57.

62. *See id.* at 1658 (explaining that when a potential migrant decides where to live, their decision is highly likely to make a real difference to the outcome).

63. *Id.*

Not surprisingly, exit was historically the universal strategy in publicly traded companies with many minority investors.[64] When dissatisfied with management actions or company performance in general, shareholders have the option of selling their shares. But, as a result of several factors, foot voting is no longer a viable option for many large fund families today.

Larger shareholdings give asset managers more power to influence decision-making in portfolio companies.[65] This strengthens incentives to cast an informed vote instead of selling shares. But larger shareholdings also significantly increase the costs of selling shares, even in portfolio companies with deep and active share markets.[66] Large equity positions in portfolio companies thus effectively lock in big asset managers and leave them only with voice as a governance strategy. Moreover, many funds "abandon" their exit rights by choosing to mimic market indexes.[67] Such index funds must own shares in companies included in an index and have no exit option.[68] Exit, as a result, has been decreasing in importance as a governance strategy for many large fund complexes. When exit is in decline, shareholders increasingly rely on their voting power.[69]

2. Voice-Based Engagement Strategies

Shareholder voting is one of the distinctive features of the law of business organizations. A range of important corporate governance protections are based on shareholder voting.[70] First, shareholder voting rights aim to limit the effect of managerial opportunism on corporate decision-making in general by electing board members who shareholders trust with the delegation of power. Second, these voting rights also reduce the influence of directors on some fundamental decisions by giving decision-making rights to shareholders only. In addition to director elections, shareholders typically decide matters that are financially significant or may have a major impact on the company's business, involve strong conflict of interest, or affect shareholders' rights.[71] Specifically, shareholders may vote on issuances of new shares, appointment of auditors, mergers and acquisitions, adoption of antitakeover defences, creation of equity-based compensation plans for managers, approval of executive pay policy and pay report. Accordingly, as an alternative to selling shares, institutional investors can use voting power to promote changes in their portfolio companies.

The effectiveness of this arrangement in distributing corporate decision-making power between shareholders and managers hinges upon the ability and willingness of

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64. *See, e.g.*, Cotter et al., *supra* note 20, at 10; Alan R. Palmiter, *Mutual Fund Voting of Portfolio Shares: Why Not Disclose?*, 23 CARDOZO L. REV. 1419, 1430–31 (2002).

65. *See* Bernard S. Black, *Shareholder Passivity Reexamined*, 89 MICH. L. REV. 520, 567–68 (1990) (showing the prevalence of large shareholders).

66. John C. Coffee, Jr., *Liquidity versus Control: The Institutional Investor as Corporate Monitor*, 91 COLUM. L. REV. 1277, 1288–89 (1991).

67. *Id.* at 1339.

68. Palmiter, *supra* note 64, at 1429.

69. ALBERT O. HIRSCHMAN, EXIT, VOICE, AND LOYALTY: RESPONSES TO DECLINE IN FIRMS, ORGANIZATIONS, AND STATES 34–36 (1970) ("[T]he role of voice would increase as the opportunities for exit decline, up to the point where, with exit wholly unavailable, voice must carry the entire burden of alerting management to its failings.").

70. David Yermack, *Shareholder Voting and Corporate Governance*, 2 ANN. REV. FIN. ECON. 103, 104 (2010).

71. *See* DAVID KERSHAW, COMPANY LAW IN CONTEXT 190 (2012).

shareholders to exercise their voting rights. The rise of stewardship codes and international regulatory efforts, since the 2008 financial crisis, to give shareholders stronger participatory rights in executive pay decisions are premised on the idea that better shareholder engagement with companies can counterbalance the influence of executive directors.[72] These initiatives assume that increased shareholder power and participation in corporate affairs is a valuable corporate governance tool.[73]

There are three ways that investment managers can employ their voice-based engagement strategies. First, they can use strong voting rights as leverage in behind-the-scenes discussions with company managers to influence their behavior.[74] Closed-door negotiations are, indeed, a common instrument used by asset managers.[75] The second engagement strategy is submission of shareholder proposals for inclusion in the agenda of the shareholders' meeting.[76] However, since large diversified fund families hold shares in many companies, informed engagement with every portfolio company through private negotiations or submission of shareholder proposals is not feasible.[77]

The third voice-based governance strategy available to asset managers, the use of voting rights at shareholder meetings, is the main and most popular communication channel between managers and shareholders in publicly traded companies.[78] Fund managers often vote against company management to show their disagreement with the proposed decisions and courses of action.[79] Where voting outcomes are close, in other words, where votes cast in support are close to the threshold required for the proposal to pass, the reliance on voting rights becomes stronger.[80]

Evidence also shows that investors place greater emphasis on voting where selling shares, due to large holdings or absence of liquid and deep markets, is costly.[81] This is certainly the case with the big asset managers—given the size of their shareholdings and the wide use of indexing strategies, voting the shares of portfolio companies is often the only realistically available communication channel with corporate managers across the

72. *See* Jennifer G. Hill, *Good Activist/Bad Activist: The Rise of International Stewardship Codes*, 41 SEATTLE U. L. REV. 497, 506 (2018) (explaining "debate today is less about controlling shareholder power than about constraining board power by encouraging shareholders to exercise their legal rights and increase their level of engagement in corporate governance").

73. *Id.* at 505.

74. *See* Palmiter, *supra* note 64, at 1437–38 (discussing Vanguard and Fidelity's usage of a collectivized voice to advocate for changes).

75. *See* Joseph A. McCahery et al., *Behind the Scenes: The Corporate Governance Preferences of Institutional Investors*, 71 J. FIN. 2905, 2906 (2016).

76. *See* Peter Cziraki et al., *Shareholder Activism Through Proxy Proposals: The European Perspective*, 16 EUR. FIN. MGMT. 738, 739 (2010); Aaron A. Dhir, *Realigning the Corporate Building Blocks: Shareholder Proposals as a Vehicle for Achieving Corporate Social and Human Rights Accountability*, 43 AM. BUS. L.J. 365, 374 (2006).

77. *See* Willard T. Carleton et al., *The Influence of Institutions on Corporate Governance through Private Negotiations: Evidence from TIAA-CREF*, 53 J. FIN. 1335, 1342–47 (1998) (documenting that TIAA, a leading U.S. pension fund manager for education, research, and medical employees, targeted only 45 companies for private discussions during the period from 1992 through 1996).

78. *See* Bebchuk & Hirst, *supra* note 36, at 2045.

79. McCahery et al., *supra* note 75, at 2911–13.

80. *See* Ying Duan & Yawen Jiao, *The Role of Mutual Funds in Corporate Governance: Evidence from Mutual Funds' Proxy Voting and Trading Behavior*, 51 J. FIN. & QUANTITATIVE ANALYSIS 489, 504–05 (2016) (explaining the importance of voting by institutional investors during close votes because of the critical nature of the votes controlled by fund managers in such situations).

81. McCahery et al., *supra* note 75, at 2915–16.

board. The concern is that large asset managers simply lack any incentive to vote on an informed basis and, as a result, cannot carry out effective investment stewardship.[82]

B. Can Large Asset Managers Be Engaged Shareholders?

During the first half of the 20th century, the ownership structures of many U.K. listed companies were dominated by controlling families or were widely distributed among numerous individual investors.[83] This trend continued through the late 1950s and early 1960s.[84] Institutional investors owned less than one-fifth of all ordinary shares in this period.[85]

Voting in companies with a dispersed ownership structure involves classic collective action and free-rider problems.[86] Small individual shareholdings mean that shareholder votes matter where many small shareholders act as one voice. Even though shareholders might all benefit from monitoring and challenging managers, costs associated with taking action make it unlikely that any individual shareholder will move alone.[87] The costs of such action will be borne by the activist alone, whereas the benefits will be shared among all.[88] Hence, voting activism is a public good that is better accomplished if shareholders act collectively and share the costs.[89] But if there are costs to acting collectively, then there will always be free-riding shareholders who increase the costs shared by others and thus discourage such action.[90] Many small retail shareholders are thus rationally disinterested in shareholder voting. As a result, corporate boards were often the effective controllers of

82. Academic publications and media are full of negative narratives of shareholder power—blaming shareholders, or at least certain types of shareholders, in being short-sighted. This view questions shareholder engagement as it may have negative consequences for the company and its stakeholders in the long run. Hill, *supra* note 72, at 500–03.

83. *See* Julian Franks et al., *Spending Less Time with the Family: The Decline of Family Ownership in the United Kingdom*, *in* A HISTORY OF CORPORATE GOVERNANCE AROUND THE WORLD: FAMILY BUSINESS GROUPS TO PROFESSIONAL MANAGERS 588–90 (Randall K. Morck ed., 2005).

84. *See* Brian R. Cheffins, *Dividends as a Substitute for Corporate Law: The Separation of Ownership and Control in the United Kingdom*, 63 WASH. & LEE L. REV. 1273, 1286–87 (2006).

85. *See* Black & Coffee, Jr., *supra* note 20, at 2007. *See also* Paul Myners, U.K. SUSTAINABLE INV. & FIN. ASS'N, INSTITUTIONAL INVESTMENT IN THE UNITED KINGDOM: A REVIEW 27 (2001), http://uksif.org/wp-content/uploads/2012/12/MYNERS-P.-2001.-Institutional-Investment-in-the-United-Kingdom-A-Review.pdf [https://perma.cc/E8Z4-UH4T] (documenting the drop in individual ownership of shares in U.K. listed companies from 54% in early 1960s to just above 15% in 1999 and a corresponding increase in the holdings of institutional investors).

86. A collective action problem arises when there is a conflict between a behavior that maximizes the welfare of an individual and a behavior that maximizes the welfare of the group to which the individual belongs. *See* RUSSELL HARDIN, COLLECTIVE ACTION 8–9, 16–22 (1982); MANCUR OLSON, THE LOGIC OF COLLECTIVE ACTION: PUBLIC GOODS AND THE THEORY OF GROUPS 5–16 (1971).

87. *See generally* KEITH DOWDING, POWER 33–38 (1996); OLSON, *supra* note 86, at 5–16.

88. *See* OLSON, *supra* note 86, at 15.

89. *See id.*

90. *See id.* at 40–41.

U.K. listed companies.[91] Shareholders, meanwhile, were "absentee owners."[92]

The ownership landscape, as illustrated earlier, is very different today with institutional investors holding around 90% of shares of U.K. listed companies.[93] The rise of institutional investors combined votes of thousands of small investors in the hands of several large fund family managers.[94] This increased ownership concentration, however, does not automatically transfer into more active shareholder engagement. The intermediary nature of most institutional investors, which typically hold shares as fiduciaries of the beneficial investors, in addition to the existing agency problem between managers and dispersed shareholders,[95] adds another layer of agency problems—this time between the record holder of shares and the ultimate providers of capital, further complicating matters.[96] Fund managers act as agents of beneficiary investors in their relationships with the portfolio company managers, thereby creating a double set of agency relationships: between shareholders and managers of portfolio companies and between beneficial owners of fund assets and fund managers.[97] Although relatively large holdings of fund families mitigate the collective action problem, the additional layer creates various agency problems that may discourage active shareholder engagement by many institutional investors. The rest of this section describes the two problems of the agency-cost framework that influence shareholder stewardship by asset managers.

1. Incentives and Capability of Large Asset Managers to Vote

The first problem affects the incentives and capability of asset managers to be proactive monitors of their portfolio companies. A common argument is that the new agency layer exacerbates the free-rider problem because benefits from active shareholder

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91. The study of ownership structures of large U.K. firms in the first half of the 20th century shows how families influenced corporate decision-making through their positions on the boards, even though they had long diluted family controlling shareholdings in the result of new equity issuances. *See generally* Franks et al., *supra* note 83, 587–93. For the vivid illustration of this account, see PHILIP AUGAR, THE BANK THAT LIVED A LITTLE: BARCLAYS IN THE AGE OF THE VERY FREE MARKET 5–6 (2018) (describing how in the mid-20th century and up to 1980s the board of Barclays was dominated by family directors, although the bank had long been publicly traded and had a dispersed ownership; the board was more like a club with private benefits for directors and where all were "very nice to one another").

92. *See* Dodd, Jr., *supra* note 22 (defining absentee owners as investors who take no part in running business).

93. Hill, *supra* note 72, at 499; Paul Davies, *Shareholders in the United Kingdom*, *in* RESEARCH HANDBOOK ON SHAREHOLDER POWER 355, 357–59 (Jennifer G. Hill & Randall S. Thomas, eds., 2015).

94. Lucian A. Bebchuk et al., *The Agency Problems of Institutional Investors*, 31 J. ECON. PERSP. 89, 91–93 (2017); Black, *supra* note 65, at 567–68.

95. The delegation of decision-making power from shareholders to a centralized board of directors creates a risk that managers may engage in opportunistic behavior by promoting their own interests at the expense of the company's and its shareholders' interests. Kathleen M. Eisenhardt, *Agency Theory: An Assessment and Review*, 14 ACAD. MGMT. REV. 57, 58 (1989).

96. Jay Clayton, Opening Remarks to SEC-NYU Dialogue on Securities Markets No. 4: Shareholder Engagement (Jan. 19, 2018), https://www.sec.gov/news/speech/clayton-2018-01-19 [https://perma.cc/F5LW-87SL]; Leo E. Strine, Jr., *Can We Do Better by Ordinary Investors? A Pragmatic Reaction to the Dueling Ideological Mythologists of Corporate Law*, 114 COLUM. L. REV. 449, 455 (2014); 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, 876–78 (2013) (describing the shift from "ownership society" to an "agency society" where beneficial owners of equity confront two agency relationships: (1) between the portfolio company management and institutional record holder, and (2) between the record holder and the beneficial owner).

97. Gilson & Gordon, *supra* note 96, at 878.

engagement not only are shared among all shareholders of a target company but flow directly to the engaged asset manager's portfolio fund.[98] The asset manager itself receives only a small partial benefit indirectly through the fee it charges to the fund.[99]

Engagement incentives are further weakened in index funds which are competing based on relative performance and on charged fees. Any investment in shareholder engagement, provided it improves the target company performance, is expected to benefit the benchmark index in general and all competing funds that follow the same index.[100] The key aspect of competition between index funds, due to similar products,[101] is the ability of a fund provider to offer the lowest management costs.[102] Shareholder engagement meanwhile is costly, particularly for passively-managed funds which typically lack company-specific knowledge.[103] The engaged asset manager will thus fail to improve its own relative performance; to the contrary, it will become less competitive on charged fees.

These concerns are partially offset by reputational pressure to be active investment stewards. The increasing shareholdings of big asset managers in publicly-traded companies have put them in the corporate governance spotlight and created an expectation that they need to act as responsible investors.[104] These asset managers are not only the subject of a rapidly growing list of academic studies but are also the primary target of stewardship codes published in various jurisdictions.[105]

Rational asset managers are then expected to look for ways of reducing the costs of being engaged shareholders. One way of achieving this uneasy task, as explained by

98. *See* Bebchuk et al., *supra* note 94, at 96–97.

99. *See id.* The agency-cost framework somewhat overstates weak incentives of investment managers to invest in stewardship by assuming that the only factor that investment managers maximize is the net management fee. Disregarding non-pecuniary rewards, the financial rewards of investment managers also depend on the size of assets under management. For example, BlackRock's market capitalization, and accordingly management remuneration, is influenced both by its revenue from management fees and by capital inflows to the assets under management. This means that an asset manager has incentives to invest in stewardship more than what would be economically justified from the perspective of maximizing the net management fee as long as this additional investment will lead to more asset inflows to the funds affiliated with the manager.

100. Bebchuk et al., *supra* note 94, at 98; Paul H. Edelman et al., *Shareholder Voting in an Age of Intermediary Capitalism*, 87 S. CAL. L. REV. 1359, 1392–93 (2014); Gilson & Gordon, *supra* note 96, at 890.

101. There are, indeed, important parameters of indexed products which investors need to consider before deciding which product to buy. For example, funds may be distinguished by the way they select shares (value, growth, or sector specific) or an index to track; funds may also differ regarding the weight they give companies in the portfolio (proportional to market capitalizations of portfolio companies or equal). In practice, however, large asset managers have multiple products (funds) varying across the listed parameters and what really distinguishes passive asset managers from each other is the cost of management and the quality of client service.

102. Edward B. Rock, *The Logic and (Uncertain) Significance of Institutional Shareholder Activism*, 79 GEO. L.J. 445, 474 (1991).

103. *See* Dorothy S. Lund, *The Case Against Passive Shareholder Voting*, 43 J. CORP. L. 493, 511–12 (2018) (contrasting actively-managed funds, which make investment decisions based on extensive research of individual companies, to passive funds, which invest in the broad market and do not need to study individually each company in the portfolio).

104. *See* HORTENSE BIOY ET AL., PASSIVE FUND PROVIDERS TAKE AN ACTIVE APPROACH TO INVESTMENT STEWARDSHIP 3 (Dec. 2017), https://www.morningstar.com/content/dam/marketing/shared/pdfs/Research/Morningstar-Passive-Active-Stewardship.pdf [https://perma.cc/2KDR-T4UZ] (discussing the issue of index managers impact on corporate governance); Giovanni Strampelli, *Are Passive Index Funds Active Owners? Corporate Governance Consequences of Passive Investing*, 55 SAN DIEGO L. REV. 803, 816–17 (2018) (discussing reasons why passive index funds can and cannot play an active role in corporate governance).

105. *See* Walker, *supra* note 5.

Bernard Black and, more recently, Jill Fisch, Assaf Hamdani and Steven Davidoff Solomon, is to concentrate on those proposals that are similar across companies: this allows sharing the costs of voting among many portfolio companies.[106] Large asset managers can be active on matters that are not company-specific but are replicated in numerous companies. These matters include primarily corporate governance provisions[107]—like the structure of executive pay, routine decisions to issue new shares, or precautionary implementation of takeover defences—but may also cover activities that have social or environmental impact. In contrast, on company-specific matters, like voting on individual directors or operational matters, large asset managers will be less active because every vote requires incurring costs that cannot be shared across portfolio companies.[108] As observed by Ronald Gilson and Jeffrey Gordon, institutional investors, at most, might engage in "governance activism" but not in "performance activism."[109]

2. Conflicts of Interest Generated by the Business Model of Large Asset Managers

A separate stream of literature focuses on conflicts of interest inherent in the business models of asset managers that discourage active shareholder engagement. For example, possible business ties of large fund groups with their portfolio companies may create conflicts of interest during voting. Company managers may influence decisions where to invest employees' pension savings.[110] Corporate managers may threaten to change the company's existing financial services providers if asset managers affiliated with them do not support the management.[111] Managers may also provide selective access or send selective signals about valuable inside information to some of the company's large institutional shareholders.[112] These decisions, in turn, transform into possible influence over fund managers, who have incentives to remain loyal to company CEOs in order to maintain the existing business services and access to valuable information flows.[113] Empirical literature confirms the legitimacy of these concerns about the influence of business ties between large fund managers and their portfolio companies on shareholder voting.[114]

106. Jill E. Fisch et al., *The New Titans of Wall Street: A Theoretical Framework for Passive Investors*, 168 U. PA. L. REV. 17, 38 (2019); Black, *supra* note 65, at 589.

107. *See* Fisch et al., *supra* note 106, at 38–39 (discussing how some governance provisions will be relevant to multiple companies in a passive fund's portfolio); Black, *supra* note 65, at 589 (discussing economies of scale).

108. *See* Black, *supra* note 65, at 589 (discussing economies of scale).

109. Gilson & Gordon, *supra* note 96, at 889.

110. *See* Bebchuk et al., *supra* note 94, at 102 (discussing the business investment managers receive from pension funds); Cotter et al., *supra* note 20, at 9; Davis, *supra* note 39, at 20; Burton Rothberg & Steven Lilien, *Mutual Funds and Proxy Voting: New Evidence on Corporate Governance*, 1 J. BUS. & TECH. L. 157, 160 (2006).

111. Bebchuk et al., *supra* note 94, at 102; Rock, *supra* note 102, at 469–71.

112. *See* Rothberg & Lilien, *supra* note 110, at 160 (discussing the relationship between mutual funds and management). To be sure, disclosure and insider trading laws prevent managers from offering access to material information on a selective basis. *See, e.g.*, SEC Regulation FD, 17 C.F.R. §§ 243.100–.103 (2020). Nevertheless, "favorite" investors may be invited to regular meetings with managers before an expected disclosure of important corporate information, whereas others may not. In addition, managers may give covert signals during those meetings. *See* Martin Bengtzen, *Private Investor Meetings in Public Firms: The Case for Increasing Transparency*, 22 FORDHAM J. CORP. & FIN. L. 33, 108–10 (2017) (discussing private investor meetings).

113. *See* John C. Bogle, *Reflections on "Toward Common Sense and Common Ground?"*, 33 J. CORP. L. 31, 32 (2007) (discussing the relationship between fund managers and corporate managers).

114. *See, e.g.*, Dragana Cvijanović et al., *Ties That Bind: How Business Connections Affect Mutual Fund Activism*, 71 J. FIN. 2933, 2944–46 (2016) (showing that fund families with pension-related business ties are likely

In addition to external conflicts of interests with portfolio companies, the biggest asset managers combine under one roof various funds with different investment strategies and preferences, and thus also face internal conflicts of interest in deciding how to vote shares held by each fund.[115] For example, if the asset manager is affiliated with both equity and debt funds, the interests of investors of these funds can easily come into conflict on matters that encourage the company to take more risks or distribute more profits among shareholders. Refraining from active engagement may be the only option available to the manager that will avoid harm to the interests of its clients in such situations.[116]

In sum, the rise of large asset managers may have two opposite, perhaps counterbalancing, effects on shareholder engagement. On the one hand, larger holdings by fund families reduce the collective action problem and strengthen reliance on voting rights compared to the situation where many individuals hold shares independently. Ownership concentration also increases the burden of investor oversight that the public expects from large fund families. On the other hand, incentives of fund managers do not encourage them being proactive monitors. Moreover, large fund families are shareholders in hundreds of companies and do not necessarily have the resources to monitor each portfolio company individually.[117] In other words, large fund families may be too big to engage actively.[118] Accordingly, they are expected to vote in a standard manner across companies with more attention towards matters that are shared across companies. The question as to which effect prevails in practice can be answered only empirically.

IV. VOTING PRACTICES OF LARGE ASSET MANAGERS: EVIDENCE FROM SHAREHOLDERS' MEETINGS

A. Data Sources and Sample Descriptions

Notwithstanding their huge importance, we have surprisingly little knowledge about the stewardship role of the big asset managers in British listed companies. Information on shareholder voting in publicly traded companies was long unavailable to the public. Regulatory and soft-law measures adopted in various countries lately have improved disclosure of voting records by investment funds. There are, however, differences in the practices of disclosing fund voting records across jurisdictions. U.S. mutual funds are required to disclose their voting records in annual reports filed with the Securities and Exchange Commission (SEC).[119] These reports, called NP-X forms, can be accessed through the Mutual Fund Proxy Voting Records section of the SEC's EDGAR database.[120]

There is no mandated disclosure of voting records for U.K.-based funds; it is merely

to vote along management recommendations on shareholder-sponsored proposals).

115. John D. Morley, *Too Big to Be Activist*, 92 S. CAL. L. REV. 1407, 1412 (2019).

116. *See id.* at 1444–46 (illustrating the relationship between an asset manager's conflicts and the intensity of engagement).

117. *See* Bebchuk & Hirst, *supra* note 36, at 2077–80 (reporting the numbers of stewardships teams in the big three asset managers and estimating the limited time and resources these teams can spend on stewardship).

118. *See* KERSHAW, *supra* note 71, at 182–83.

119. *See* Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, Securities Act Release No. 8188, Exchange Act Release No. 47,304, 68 Fed. Reg. 6563, 6584 (2003).

120. The database can be accessed at https://www.sec.gov/edgar/searchedgar/n-px.htm. Alternatively, U.S. mutual fund voting records are available through the ISS Voting Analytics database.

a matter of best practice. The Stewardship Code, first published in 2010 and revised in September 2012,[121] recommends that institutional investors disclose publicly their voting records.[122] In reality, the practices of U.K.-based funds on voting record disclosure differ greatly. Some funds (fund managers) disclose full records voluntarily,[123] while a few even go as far as explaining the motivation for voting on specific proposals;[124] others, on the other hand, make voting records available only to their clients upon request.[125]

Data on votes cast by U.S. mutual funds at shareholders' meetings of U.K. companies were collected using the NP-X forms filed with the SEC. Publicly available disclosure web pages of asset managers were the main data source for U.K.-based institutional investors. Information on voting activity of those U.K.-based fund managers that is not available publicly was obtained from Proxy Insight Online.

Proxy Insight Online was also the source for voting recommendations of two leading proxy advisors—Institutional Shareholder Services (ISS) and Glass, Lewis & Co. (Glass Lewis). The choice of these two proxy advisors was motivated by ISS's dominant position in the market of voting recommendations;[126] of the other proxy advisory firms, only Glass Lewis has a meaningful impact on shareholder votes.[127]

The sample covers all FTSE 100 companies and includes every proposal submitted to a vote at a shareholders' meeting in the five-year period starting from 2013, the first full year after the introduction of the first revised Stewardship Code, and ending with 2017. The final sample includes 10,533 proposals and votes cast by the top 18 asset managers.[128]

121. The Financial Reporting Council published the second revised U.K. Stewardship Code in November 2019. *See generally* FIN. REPORTING COUNCIL, THE UK STEWARDSHIP CODE 2020 (Nov. 2019), https://www.frc.org.uk/getattachment/5aae591d-d9d3-4cf4-814a-d14e156a1d87/Stewardship-Code_Final2.pdf [https://perma.cc/UZ4Z-KW8T]. The new revised code took effect from January 1, 2020. This study covers shareholder voting practices between 2013 and 2017 and accordingly refers to the older version of the code unless indicated differently.

122. *See* FIN. REPORTING COUNCIL, THE UK STEWARDSHIP CODE, Principle 6 (Sept. 2012), https://www.frc.org.uk/getattachment/d67933f9-ca38-4233-b603-3d24b2f62c5f/UK-Stewardship-Code-(September-2012).pdf [https://perma.cc/C7AY-9ADH] [hereinafter STEWARDSHIP CODE 2012].

123. Examples of asset managers in this category include Aberdeen Asset Management, Columbia Threadneedle Investments (U.K.), M&G Investment Management, Newton Investment Management, Schroder Investment Management (SIM), and Standard Life Investments. *See*, *e.g.*, *Votes Cast by Proposal Category*, INSTITUTIONAL SHAREHOLDER SERVS., https://vds.issgovernance.com/vds/#/Mjc3NQ==/ (last visited July 18, 2018) (showing voting activity disclosure by Columbia Threadneedle Investments (U.K.)).

124. A notable example was voting activity disclosure by Standard Life Investments, currently Aberdeen Standard Investments, with explanations of the asset manager's motivation for "against" and "abstain" votes. *See Proxy Voting*, ABERDEEN STANDARD INV., https://www.aberdeenstandard.com/en/responsible-investing/proxy-voting [https://perma.cc/B8FV-ESHL] (last visited Feb. 17, 2020). Voting disclosure by Newton Investment Management includes limited information on voting motivation as well. *See Responsible Investment Quarterly Reports*, NEWTON INV. MGMT., https://www.newtonim.com/uk-charities/responsible-investment/responsible-investment-report-archive/ [https://perma.cc/FCJ3-36A9] (last visited Feb. 17, 2020).

125. Examples include Legal & General Investment Management, Lindsell Train, and Marathon Asset Management. Artemis Investment Management and Woodford Investment Management offer only general information on voting policy.

126. *See* Edelman et al., *supra* note 100, at 1398–99 (noting that ISS is the oldest, best-known, and the largest proxy advisory firm; Glass Lewis is the next); *see also* Stephen Choi et al., *The Power of Proxy Advisors: Myth or Reality?*, 59 EMORY L.J. 869, 894–95, 898 (2010) (showing that ISS is the most powerful proxy advisor with the biggest influence).

127. *See* Choi et al., *supra* note 126, at 898.

128. As noted earlier, few asset managers included in the top 20 list do not disclose their voting records. These are Artemis Investment Management, Lindsell Train, and Woodford Investment Management. The asset

The total number of votes cast is 147,440 votes. Table 2 below presents sample summary statistics. Most of the asset managers with the low frequency of voted proposals in the sample manage active funds which own shares in selected FTSE 100 companies only; investment managers associated with passively managed funds, on the other hand, are expected to vote every proposal in the sample.

managers covered are listed in Table 2. Most large fund families have a leading investment manager which votes shares on a coordinated basis. *See, e.g.*, Jan Fichtner et al., *Hidden Power of the Big Three? Passive Index Funds, Re-Concentration of Corporate Ownership, and New Financial Risk*, 19 BUS. & POL. 298, 316 (2017); COOK & SETHI, *supra* note 17, at 6–7. Invesco funds are an exception as some fund managers within the family voted differently on some proposals. This study relies on votes cast by Invesco PowerShares, the leading ETF manager of Invesco funds, which has the largest record of the FTSE 100 shares voted by Invesco funds.

Table 2. Sample Description

	Observations	Frequency %
Proposals Voted	10,533	100.00
Proposals by Meeting Type		
Annual	10,371	98.46
Special	153	1.45
Court	9	0.09
Voting Recommendations		
Company Management	10,533	100.00
ISS	10,171	96.56
Glass Lewis	10,270	97.50
Votes by Asset Managers		
BlackRock Inc.	10,428	99.00
The Vanguard Group, Inc.	10,377	98.52
M&G Investment Management Ltd.	10,166	96.52
State Street Global Advisors	10,108	95.97
T. Rowe Price Group, Inc.	10,078	95.68
Norges Bank Investment Management (NBIM)	10,042	95.34
Legal & General Investment Management Limited	9,899	93.98
Aberdeen Asset Management	9,660	91.71
Standard Life Investments Ltd.	9,540	90.57
Schroder Investment Management Ltd. (SIM)	9,488	90.08
Invesco PowerShares	9,421	89.44
Fidelity Investments	7,271	69.03
Columbia Threadneedle Investments (UK)	6,361	60.39
Capital Group	5,506	52.27
MFS Investment Management	5,276	50.09
Newton Investment Management Ltd.	5,185	49.23
Franklin Templeton Investments	4,879	46.32
Marathon Asset Management LLP	3,755	35.65
Total	147,440	

Table 3 presents the distribution of proposals over years, meeting type, and proposal sponsor and topic. Proposals are quite equally distributed over years. Most proposals were voted upon during annual shareholder meetings. All proposals were divided into seven categories based on their topics. Almost half of all voted proposals were related to the election of new and re-election of incumbent directors. Other big proposal categories were routine/business matters (21.76%),[129] capitalization (16.65%),[130] and compensation (8.93%).[131] Antitakeover proposals were, as a rule, standard formalities allowing the board to call shareholders' meetings with shorter, two weeks, notice in an unlikely case that the company becomes a takeover target and intends to adopt takeover defences. Less than 1% of proposals dealt with a major event in the company's life—mergers and reorganizations.[132] The number of proposals on social, health, and environmental topics was even lower.

129. Routine/business proposals include mostly trivial items, such as approval of financial accounts and dividend payments, and appointment of the company's auditor. But proposals in this group may also include more important matters like amendments of the company's articles or changes in the board structure.

130. Capitalization proposals include items like authorization of share buy-backs and issue of new equity.

131. Compensation proposals are mainly related to the approval of remuneration policy and remuneration report but may also include matters like approval of incentive plans.

132. This category also includes large asset sales and purchases.

Table 3. The Distribution of Proposals by the Year of Proposal and Category

The table shows the distribution of proposals included in the shareholders' meeting agendas of the FTSE 100 companies during 2013-2017. Panel A presents data on proposals by year of the meeting. Panel B divides all proposals into two groups: management- and shareholder-sponsored proposals. Additionally, proposals in each group are split into seven categories by the topic of the proposal. All proposals are distributed by the management, ISS, and Glass Lewis recommendations. The column "Against" combines both "against" and "abstain" votes; "Other" includes proposals with no or unknown recommendation.

	Obs.	Freq. %	Management Recommendation			ISS Recommendation			Glass Lewis Recommendation		
			For %	Against %	Other %	For %	Against %	Other %	For %	Against %	Other %
Panel A. Year of Proposal											
2013	1,937	18.39	99.95	0.05	0.00	92.51	1.03	6.45	87.71	6.45	5.83
2014	2,172	20.62	99.86	0.05	0.09	93.09	1.80	5.11	91.16	5.43	3.41
2015	2,089	19.83	99.81	0.00	0.19	96.55	0.77	2.68	92.05	5.22	2.73
2016	2,105	19.98	99.81	0.10	0.10	96.91	1.43	1.66	93.87	6.08	0.05
2017	2,230	21.17	99.69	0.18	0.13	95.61	1.57	2.83	97.04	1.88	1.08
Panel B. Proposal Sponsor and Category											
Management	10,520	99.88	99.90	0.00	0.10	95.04	1.25	3.71	92.56	4.89	2.56
Directors Related	5,073	48.16	99.94	0.00	0.06	96.08	1.03	2.90	95.68	2.35	1.97
Routine/Business	2,292	21.76	99.78	0.00	0.22	95.86	0.22	3.93	97.47	0.44	2.09
Capitalization	1,754	16.65	99.89	0.00	0.11	94.93	0.00	5.07	96.58	0.06	3.36
Compensation	941	8.93	99.89	0.00	0.11	87.78	7.23	4.99	86.08	9.46	4.46
Antitakeover Related	389	3.69	100.00	0.00	0.00	96.40	1.29	2.31	23.14	75.32	1.54
Reorganization and Mergers	71	0.67	100.00	0.00	0.00	85.92	2.82	11.27	77.46	2.82	19.72
Health/Environmental	0	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Shareholder	13	0.12	38.46	61.54	0.00	38.46	61.54	0.00	38.46	61.54	0.00
Directors Related	3	0.03	0.00	100.00	0.00	0.00	100.00	0.00	0.00	100.00	0.00
Routine/Business	2	0.02	0.00	100.00	0.00	0.00	100.00	0.00	0.00	100.00	0.00
Capitalization	0	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Compensation	0	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Antitakeover Related	0	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Reorganization and Mergers	0	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Health/Environmental	8	0.08	62.50	37.50	0.00	62.50	37.50	0.00	62.50	37.50	0.00
Total	10,533	100.00	99.82	0.08	0.10	94.97	1.33	3.70	92.49	4.96	2.55

One of the distinguishing features of shareholders' meetings of U.K. listed companies is the clear domination of management-sponsored proposals. During the five years covered by this study, shareholders' meeting agendas included only 13 proposals (0.12% of the total) sponsored by shareholders.[133] More than half of shareholder proposals were on environmental topics, but there were also three director proxy contests, all of which were unsuccessful. In contrast, shareholders of U.S. publicly-traded companies voted on 788 shareholder-sponsored proposals during the 2018 proxy season alone, according to a report by law firm Gibson, Dunn & Crutcher LLP.[134] One explanation for the almost total absence of shareholder proposals in British companies is that the U.K. Corporate Governance Code encourages corporate boards to be proactive and initiate changes themselves. Indeed, more than one-third of 2018 shareholder proposals in U.S. companies were on governance topics, including such as separation of the positions of a CEO and board chairman or removing staggered boards.[135] Both measures have long been promoted by the U.K. Corporate Governance Code.[136] But the large number of social and environmental proposals in U.S. companies, at 43%,[137] suggests that there may be also other reasons for contrast between the two countries, for example, less demanding rules for submitting shareholder-sponsored proposals in the United States.[138]

Table 3 also reports voting recommendations by the company's management, ISS, and Glass Lewis. Since almost all proposals were management-sponsored, management recommendations were mostly positive. The only 8 negative management recommendations were issued for shareholder-sponsored proposals. ISS and Glass Lewis followed management in issuing identical recommendations for shareholder proposals, but they vary on management proposals. On the surface, Glass Lewis was more likely to recommend voting against management recommendations than ISS—4.89% of cases as opposed to 1.25% of proposals, respectively. A more detailed examination, however, shows that many of Glass Lewis' negative recommendations were issued for standard

133. There was a slight increase in the number of shareholder proposals during 2016 and 2017—shareholders lodged nine proposals in total against only four proposals submitted in 2013-2015.

134. GIBSON DUNN, SHAREHOLDER PROPOSAL DEVELOPMENTS DURING THE 2018 PROXY SEASON (July 12, 2018), https://www.gibsondunn.com/wp-content/uploads/2018/07/shareholder-proposal-developments-during-the-2018-proxy-season.pdf [https://perma.cc/FD53-BG6M] (the sample covers all Russell 3000 companies; the "2018 proxy season" means the period between October 1, 2017 and June 1, 2018) [hereinafter *Shareholder Proposal Developments*]. *See also* Tatyana Shumsky, *Investor Proposals Garner Support*, WALL ST. J., July 18, 2018, at B5B.

135. *See Shareholder Proposal Developments*, *supra* note 134.

136. FIN. REPORTING COUNCIL, UK CORPORATE GOVERNANCE CODE 6 (2018) [hereinafter CORPORATE GOVERNANCE CODE]. *See also* Jennifer G. Hill, *The Trajectory of American Corporate Governance: Shareholder Empowerment and Private Ordering Combat*, 2019 U. ILL. L. REV. 507, 541 (2019) (explaining that U.S. institutional investors are becoming increasingly aware of shareholder rights in other jurisdictions and this, at least partly, explains the use of shareholder proposals to acquire rights common elsewhere).

137. *See Shareholder Proposal Developments*, *supra* note 134.

138. A shareholder that owns at least 1% or $2000 worth voting shares in a U.S. corporation for at least a year is permitted to submit a shareholder proposal. In the United Kingdom, by contrast, a proposal sponsor must own at least 5% of the voting shares or be a group of at least 100 shareholders with each owning no less than £100 worth shares. *See* Bonnie G. Buchanan et al., *Shareholder Proposal Rules and Practice: Evidence from a Comparison of the United States and United Kingdom*, 49 AM. BUS. L.J. 739, 754–55 (2012). Certain types of proposals, including matters relating to director elections or the company's ordinary business, are excluded from the easy access rules in the United States. This may explain the popularity of social and environmental proposals. *See id.* at 770.

antitakeover related proposals—293 negative recommendations or more than three-quarters of total vote recommendations for antitakeover proposals, almost all issued before 2017.[139] In other matters, both proxy advisory firms had comparable recommendations without major deviations.

B. Voting Practices of Big Fund Managers

Voting records of big asset managers reveal that institutional investors are, contrary to the established thought, using their voting rights. Unlike in the United States, where asset managers are obliged to vote their shares by legal rules,[140] institutional investors in the United Kingdom are not subject to any mandated voting requirements. Nevertheless, funds rarely abstain from voting their shares (Table 2). For example, the largest U.K. asset manager, Legal & General Investment Management, stresses that it has not abstained from voting on shares of U.K. companies for the last five years.[141] Lower voting frequency for some asset managers—Newton Investment Management and Marathon Asset Management voted 49.23% and 35.65% of the sample proposals, respectively—does not mean that the asset managers ignore shareholders' meetings. Less frequent voting is often because actively managed funds affiliated with these managers do not own shares in every FTSE 100 company.

The modern use of voting rights by asset managers diverges dramatically from the historical practices of U.K. institutional investors, which tended to vote their shares only rarely.[142] The introduction of the Stewardship Code[143] may have encouraged more active voting by institutional investors, but the change in investors' voting behavior occurred much earlier. Indeed, in the early 1990s, the largest investors had policies in place to vote every share or, at least, in situations where the shareholding was above a minimum threshold.[144]

But voting is not helpful if shareholders always vote according to management recommendations. This may, in contrast, weaken the voice of activist shareholders and entrench the position of the management.[145] This study relies on two measures for

139. Glass Lewis has stopped issuing negative voting recommendations for standard antitakeover proposals allowing the company board to call shareholders' meeting on shorter notice from the 2017 shareholders' meeting season.

140. *See* Edelman et al., *supra* note 100, at 1395–96; *but see* Lund, *supra* note 103, at 526–27 (arguing that asset managers wrongly believe that they are required to vote under SEC regulations).

141. LEGAL & GEN. INV. MGMT., ACTIVE OWNERSHIP: POSITIVE ENGAGEMENT TO ENHANCE LONG-TERM VALUE 40 (2016), http://www.lgim.com/files/_document-library/capabilities/cg-annual-report-2016-full.pdf [https://perma.cc/9MWQ-DZZF].

142. *See* Black & Coffee, Jr., *supra* note 20, at 2038 (contrasting the practice of U.K. investors not to vote shares with the situation in the United States where most institutional investors, even if they support management, at least vote their shares); Paul L. Davies, *Institutional Investors: A U.K. View*, 57 BROOK. L. REV. 129, 129–30 (1991) (noting that it was unusual for British institutional investors to exercise their voting rights; instead, they preferred discussions behind closed doors).

143. *See generally* STEWARDSHIP CODE 2012, *supra* note 122.

144. *See* Black & Coffee, Jr., *supra* note 20, at 2039–40; *but see* Gerrard McCormack, *Institutional Shareholders and the Promotion of Good Corporate Governance*, *in* THE REALM OF COMPANY LAW: A COLLECTION OF PAPERS IN HONOUR OF PROFESSOR LEONARD SEALY 131, 158–59 (Barry A. K. Rider ed., 1998) (noting that the Cadbury Code's emphasis on the role of institutional investors in enforcing better boardroom standards increased votes cast by institutional investors only marginally).

145. *See* Dick Weil, *Passive Investors, Don't Vote*, WALL ST. J.: OPINION (Mar. 8, 2018), https://www.wsj.com/articles/passive-investors-dont-vote-1520552657 [https://perma.cc/K8LS-P545]

examining possible differences in fund manager voting practices. The first measure is the frequency of votes cast against a management recommendation calculated as a percentage of "against" and "abstain" votes in the total number of proposals voted by an asset manager. This measure can be labelled "the disapproval rate".

The second measure is the so-called "similarity index," which compares the asset manager's vote with the corresponding voting recommendation by the company management or a proxy advisory firm. The similarity index may take values from zero (voting against recommendations on all occasions) to one (voting in full compliance with recommendations). The index can be easily presented as a percentage of how often an asset manager votes in accordance with management or proxy advisory voting recommendations. Thus, the similarity index is also the inverse of the disapproval rate in decimals but is more appropriate for comparing shareholder voting records with the recommendations of proxy advisors. Unlike management recommendations, shareholders do not vote in favor or against the recommendations of proxy advisory firms; rather, shareholders may follow or may vote differently from those recommendations. Additionally, the similarity index allows comparing pairs of voting records against a third benchmark. For example, the similarity index allows comparing how closely the votes of an asset manager resemble the recommendations of a proxy advisor when both data sets are presented in relation to management recommendations.

At first glance, voting records send a worrying message as approval rates of management-sponsored proposals by the big asset managers are strikingly high. Average voting results show that asset managers supported management recommendations for 97.78% of proposals (the disapproval rate of all management-sponsored proposals of 2.22% only).

A more detailed consideration of the voting records, however, shows that this high approval rate was due to the trivial or uncontroversial nature of many proposals, rather than the passivity of fund managers. This analysis also reveals several other important patterns. First, shareholder engagement by the largest asset managers has been growing over time. Second, asset managers approach certain types of management-sponsored proposals differently by casting "against" votes more often in relation to such proposals. Third, large asset managers vote similarly to the recommendations of proxy advisors less often than they used to; the proposal type is also associated with different levels of vote similarity in reference to the proxy advisor recommendations. Fourth, many big asset managers are unique in their voting decisions and do not fall into broader classifications, such as active versus passive fund managers or U.K.-based versus U.S.-based asset managers. The following sub-sections explore each of these observations in greater detail.

1. Changes in the Levels of Shareholder Engagement Over Time

The 2012 U.K. Stewardship Code states that institutional investors shall not automatically support the board by blindly voting in line with management

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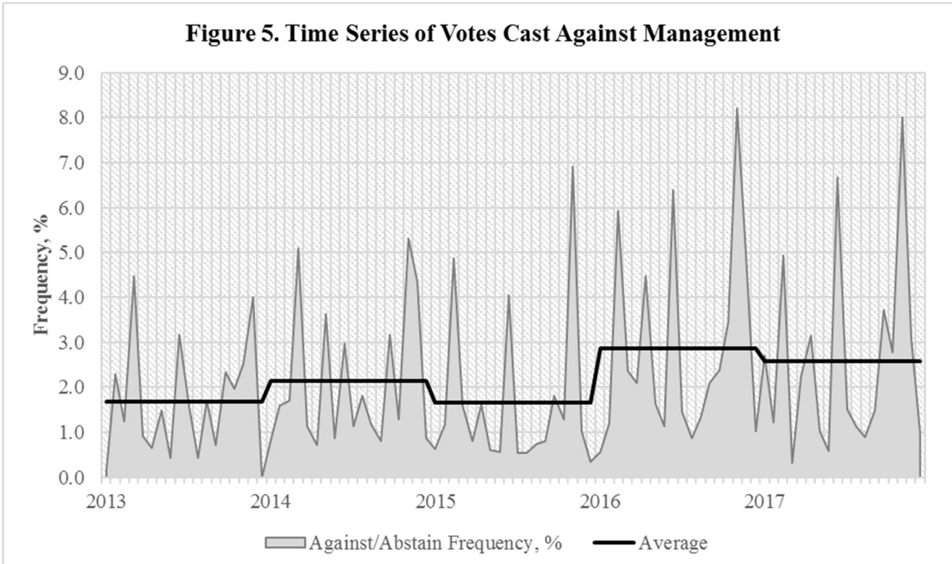
(advocating a change in SEC guidance to discourage passive investors from participating in shareholder votes); M. Todd Henderson & Dorothy Shapiro Lund, *Index Funds Are Great for Investors, Risky for Corporate Governance*, WALL ST. J.: OPINION (June 22, 2017), https://www.wsj.com/articles/index-funds-are-great-for-investors-risky-for-corporate-governance-1498170623 [https://perma.cc/Y9PU-Y9M6] (discussing three possible solutions to the corporate governance problems posed by passive shareholders).

recommendations.[146] Voting data indicate positive developments as shareholder engagement by the big asset managers has been growing during the past years. Almost all asset managers had lower disapproval rates for management proposals in 2013 compared to 2017. On average, less than 1.7% of votes were cast against management recommendations in 2013; this number reached almost 3% during the voting seasons of 2016 and 2017 (Figure 5). This may look like a small change but given the routine or trivial nature of many voted proposals, the increase is substantial.

146. *See* STEWARDSHIP CODE 2012, *supra* note 122 (outlining the information that institutional investors must disclose to their clients, preventing those organizations from merely reiterating a management board's recommendation).



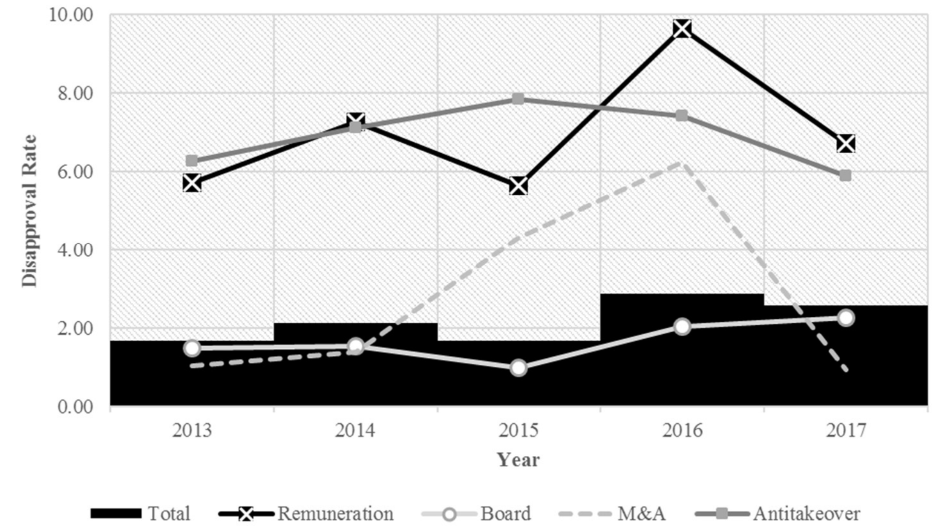
Note: The figure shows the share of votes cast "against" or "abstain" by the largest 18 asset managers during each year in the period 2013-2017. Each point represents the frequency of against/abstain votes cast by one of the asset managers during a given year. The figure also reports the average annual "against/abstain" frequency for all 18 asset managers.

Table 4 below compares differences in the average disapproval rates of different proposal categories at the beginning and the end of the study period. The values of the disapproval rates are often small and support of management recommendations above 90%, and even 95%, is the norm. Similarly, changes in against or abstain votes are, in general, economically minor, although some, depending on the proposal type or period of comparison, are statistically significant. But the division of votes by proposal category shows that indeed there are matters with economically larger disapproval rates and substantial changes over time. For example, votes against compensation proposals increased from 5.7% in 2013 to more than 9.6% in 2016.[147] But this gain more than halved in the result of a drop in 2017.[148] Generally, disapproval rates of all proposals, except for directors related proposals, decreased during 2017 from the levels of 2016 (see also Figure 6 below).

147. *See infra* Table 4.

148. The relatively lower percentage of votes against compensation proposals in 2017 can be partially explained by the larger number and type of compensation proposals voted on during 2017. Most FTSE companies had the first shareholder vote on the remuneration policy in 2014. Since shareholders vote on the remuneration policy once in three years, the second vote on remuneration policy in those companies took place in 2017, leading to more than 40% year-on-year increase in the number of remuneration proposals voted during the year.

Figure 6. Changes in Disapproval Rates for Selected Proposal Types



Note: The figure shows the average share of votes cast "against" or "abstain" by the largest 18 asset managers during each year in the period 2013-2017 for four different categories of proposals: compensation, directors related, reorganization and mergers, and antitakeover related. The figure also reports the average annual "against/abstain" frequency for all 18 asset managers.

Table 4. Changes in Votes Cast Against Management

The table shows comparative data on the average disapproval rates of 18 large asset managers over time. Panel A compares the disapproval rates during 2013 and 2016; Panel B compares the values of the disapproval rate in 2013 with the corresponding values in 2017. The results are reported for all proposals and for different categories of proposals. The mean results were tested using *t*-Test (assuming equal or unequal variance, as applicable) and the Wilcoxon Rank-Sum test. The latter drops outliers from the analysis where the distribution is not normal. The combination of both tests can thus offer better understanding of the results. The table reports only test values and significance. One asterisk indicates significance at the 10% level; two asterisks denote significance at the 5% level.

Panel A. Differences in Voting Against Management Over 2013-2016

Proposal Category	Mean Dissent 2013		Mean Dissent 2016		Difference in Mean	*t*-Test	Wilcoxon
	N	% Vote	N	% Vote			
Routine/Business	18	0.2986	18	0.3641	–0.0654	–0.392	–1.420
Compensation	18	5.7138	18	9.6351	–3.9213	–1.697*	–1.757*
Directors Related	18	1.4795	18	2.0287	–0.5492	–0.994	–0.854
Capitalization	18	1.4864	18	4.5398	–3.0534	–1.204	–1.772*
Antitakeover Related	17	6.2631	18	7.4047	–1.1416	–0.166	1.523
Reorganization & Mergers	16	1.0417	18	6.2315	–5.1899	–2.009*	–2.357**
All Proposals	18	1.6683	18	2.8632	–1.1949	–1.978*	–1.677*

Panel B. Differences in Voting Against Management Over 2013-2017

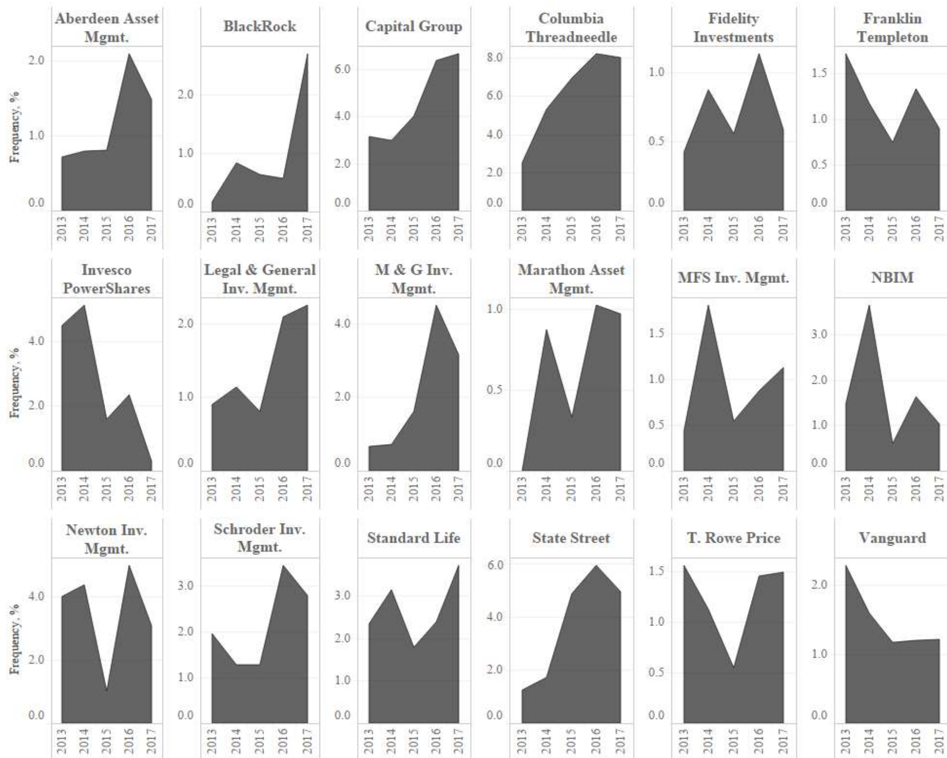
Proposal Category	Mean Dissent 2013		Mean Dissent 2017		Difference in Mean	*t*-Test	Wilcoxon
	N	% Vote	N	% Vote			
Routine/Business	18	0.2986	18	0.6369	–0.3383	–1.670	–1.961*
Compensation	18	5.7138	18	6.7044	–0.9906	–0.482	–0.602
Directors Related	18	1.4795	18	2.2561	–0.7765	–1.163	–0.854
Capitalization	18	1.4864	18	2.8400	–1.3536	–0.602	0.126
Antitakeover Related	17	6.2631	18	5.8718	0.3913	0.057	1.903*
Reorganization & Mergers	16	1.0417	18	0.9259	0.1157	0.083	0.085
All Proposals	18	1.6683	18	2.5759	–0.9076	–1.549	–1.171

The increasing trend of voting against management applied to almost every asset manager. Figure 7 clearly shows that only four asset managers, Franklin Templeton, Invesco PowerShares, NBIM, and Vanguard, objected to management-sponsored proposals more often during the earlier years of observations than lately.[149] Another fund manager, Newton Investment Management, had a relatively consistent record of votes cast against management over the five-year period of observations, with a noticeable drop in 2015 only.[150]

149. *See infra* Figure 7. Two asset managers, Invesco PowerShares and State Street, used to vote automatically against antitakeover proposals allowing the company's board to call shareholder meetings on short notice in takeover situations. Invesco PowerShares gradually reversed this practice, thus resulting in fewer votes cast "against" management over the five-year period.

150. *Id.*

Figure 7. Times Series of Votes Cast Against Management by the Big Asset Managers



Figures 5 and 7 also demonstrate that some asset managers were more likely than others to vote against management. Columbia Threadneedle Investments, Capital Group, Newton Investment Management, and Standard Life were among the managers that consistently objected to management-sponsored proposals at higher rates than other asset managers.

These results suggest that there have been significant changes in the voting behavior of large institutional shareholders in the period after the 2008 financial crisis. Back then, large shareholders were accused of "being asleep at the wheel as businesses struggled;"[151] today, however, large shareholders are more active in using their voting rights. Recent high-profile instances of shareholder opposition to management proposals show the growing voice of large asset managers can also be heard outside private meeting rooms. Consider, for example, Unilever Plc's decision to abandon shareholder vote on simplifying the company's dual-listed Anglo-Dutch corporate structure after public criticism from large asset managers, such as Aviva Investors, Columbia Threadneedle, Legal & General, M&G Investment Management, Schroder, Lindsell Train, and Royal London Asset Management—which together control about 10% of Unilever's shares—and industry groups, such as Pensions & Investment Research Consultants, a leading pension funds advisor.[152]

The increasing levels of shareholder engagement over time can, to a certain extent, be explained by the ongoing debates on the role of large institutional investors. If previously the dominant expectation from asset managers was to keep management costs to a minimum, today large asset managers are also expected to be responsible investors.[153] Stewardship codes and broader discussion in media have developed a new societal norm over the last years. This, in turn, as this study shows, has led to behavioral changes in the asset management industry. Although asset managers' first concern is still cost optimization, particularly in passively managed funds, spending resources on good corporate governance of portfolio companies has become an important part of the equation.

2. Voting on Different Types of Proposals

Voting practices of asset managers may differ not only over time but also by proposal type. For example, asset managers may pay more attention to fundamental decisions, such as mergers, or to director elections, which may be perceived as a way to monitor or influence corporate decision-making. On the other hand, trivial proposals, such as standard approvals of financial accounts or of share issues to support possible capital needs, require less intensive scrutiny.

The analysis of voting records confirms that not all proposals attract similar attention from the big asset managers. But the engagement efforts of asset managers did not always target the most fundamental business-related decisions. Asset managers were likely to

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151. *See* Attracta Mooney, *Not-So-Gentle Unilever Rebuff Shows Investor Clout*, FIN. TIMES, Oct. 15, 2018, at 20 (UK ed.).

152. *See* Saabira Chaudhuri & Daphne Zhang, *Unilever to Keep U.K. Base*, WALL ST. J., Oct. 6-7, 2018, at B3; Leila Abboud & Attracta Mooney, *Unilever Chief Blindsided by Investor Revolt*, FIN. TIMES, Oct. 6-7, 2018, at 17 (UK ed.); Attracta Mooney, *Adviser Calls on Investors to Veto Unilever Move*, FIN. TIMES, Oct. 4, 2018, at 20 (UK ed.).

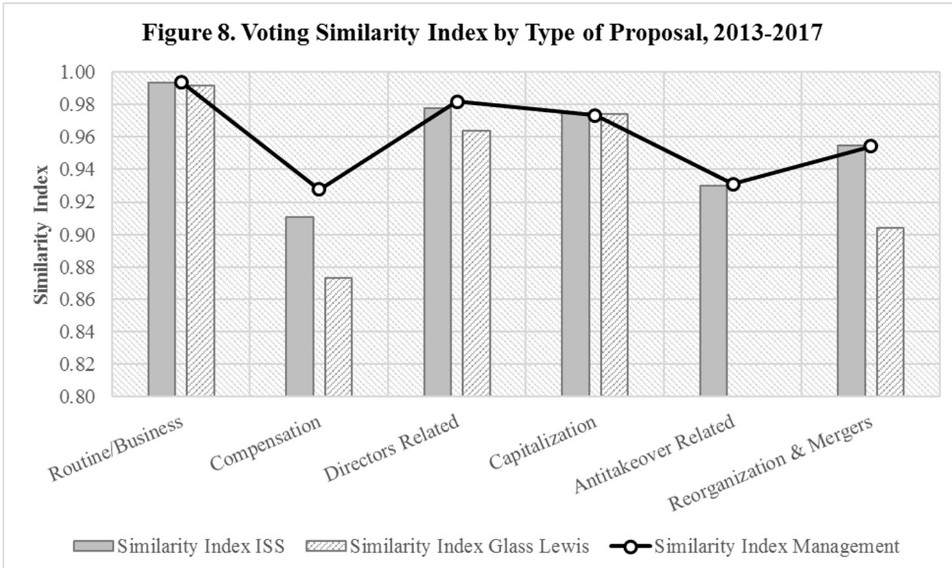
153. *See* Mooney, *supra* note 151 (referring to the 2012 Kay Review of U.K. Equity Markets and Long-Term Decision Making as a turning point in changing institutional investors' attitudes towards shareholder engagement).

approve management proposals on routine/business matters or capitalization related matters without much questioning. Routine/business and capitalization proposals received extremely high approval rates of around 99% and 98%, respectively.[154] On the other hand, some types of proposals have elicited far more “against” or “abstain” votes.

Voting opposition by fund managers was most pronounced in relation to management compensation proposals, where fund managers voted against management recommendations in almost 8% of cases. Proposals on mergers and reorganizations deal with a rare but important event in the company’s life and, not surprisingly, attract much attention with high levels of “against/abstain” votes too, although at a lower rate. Voting outcomes for these two categories of proposals also show lower similarity with the recommendations of proxy advisory firms. The highest deviation from the voting recommendations of the proxy advisory firms was for compensation-related proposals. The gap between the similarity indexes of voting results on compensation proposals in accordance with management and ISS recommendations means that the votes of large fund managers on compensation cannot always be explained by the influence of proxy advisors; part of these votes are possibly based on independent decision-making by large fund managers or simply following management recommendation.

These findings suggest that large asset managers pay attention to those proposals that are less trivial or may be linked to corporate governance. Routine and standard voting proposals—such as approval of financial accounts, dividend payments, appointment of an auditor, standard approvals for share issuances, and antitakeover defences—are less controversial and, accordingly, lead to a higher percentage of similarly cast votes, both with regard to management and proxy advisory recommendations.

154. *See infra* Figure 8 (showing that antitakeover proposals have lower approval rates, but most “against” votes are the result of automated voting by two asset managers, Invesco PowerShares and State Street, on proposals to allow boards to call shareholder meeting on short notice in the case the company is a takeover target).



Note: The figure illustrates the similarity index of the average votes cast by the biggest asset managers to the recommendations by the company management and two proxy advisory firms–ISS and Glass Lewis. Glass Lewis followed a policy of recommending votes against standard antitakeover defences until 2017, resulting in a similarity index of 0.27. The figure zeros in on the values of the similarity index above 0.8 and thus omits the results for Glass Lewis' voting recommendations on antitakeover related matters.

Perhaps the most important of the non-trivial shareholder votes, in terms of influencing corporate decision-making, is director election. The U.K. company legislation does not contain specific requirements on the election of company directors by shareholders.[155] The matter is left to private ordering by companies themselves under the terms of the company's articles of association. Nevertheless, influenced by the requirements of the Corporate Governance Code, the procedure for director election in U.K. listed companies is highly uniform. Companies with premium listing almost universally follow the Code's requirement of annual reelection of the entire board of directors.[156] Director candidates are proposed by the board (or the board's nomination committee). In addition, shareholders may propose their own candidates subject to procedural hurdles, including compliance with minimum shareholding and advance notice requirements.[157] Shareholders vote on each board candidate individually[158] by ordinary resolution,[159] meaning that a director must receive at least a simple majority vote to be appointed.[160] Shareholders participating in the meeting may cast votes in favor or against a proposed director, or abstain from voting.

As a rule, director elections were uncontested and although the biggest asset managers did not blindly follow company managers or proxy advisors, the similarity index is high on these proposals. Asset managers rarely voted against the candidates proposed by the management. As a result, aggregate outcomes often exceed 95% shareholder support in favor of the proposed board candidates. This suggests that asset managers tend to consider director election as a business matter that is better left to the management.

The drivers of voting by the largest asset managers in director elections are, instead, corporate governance considerations. Particularly, many "against/abstain" votes were not motivated by the merits of an individual candidate but were often driven by general corporate governance concerns. This results in highly standardized, or even automated, voting along with the asset manager's voting guidelines. For example, if the asset manager is not satisfied with the compensation proposal, they may also vote against all board candidates for the compensation committee or the committee's chairman. Similarly, failure to meet gender quotas may lead to voting against all board candidates for the nomination committee or the committee's chairman.[161]

3. The Role of Proxy Advisors

Along with the increasing attention towards shareholder engagement, the big asset managers also rely less on the services of proxy advisors for voting guidance. The similarity of asset managers' votes in comparison to the voting recommendations of proxy advisors remains high, but this cannot itself serve as evidence of the influence of proxy advisory firms. This is partially the result of the large number of trivial or uncontroversial

155. PAUL L. DAVIES & SARAH WORTHINGTON, GOWER'S PRINCIPLES OF MODERN COMPANY LAW 367–68, ¶¶ 14–24 (2016).

156. CORPORATE GOVERNANCE CODE, *supra* note 136, Principle 3, Provision 18.

157. Companies Act 2006, s. 338.

158. Companies Act 2006, s. 160(1).

159. Companies (Model Articles) Regulations 2008, sch. 3 (Model Articles for Public Companies), Art. 20(a).

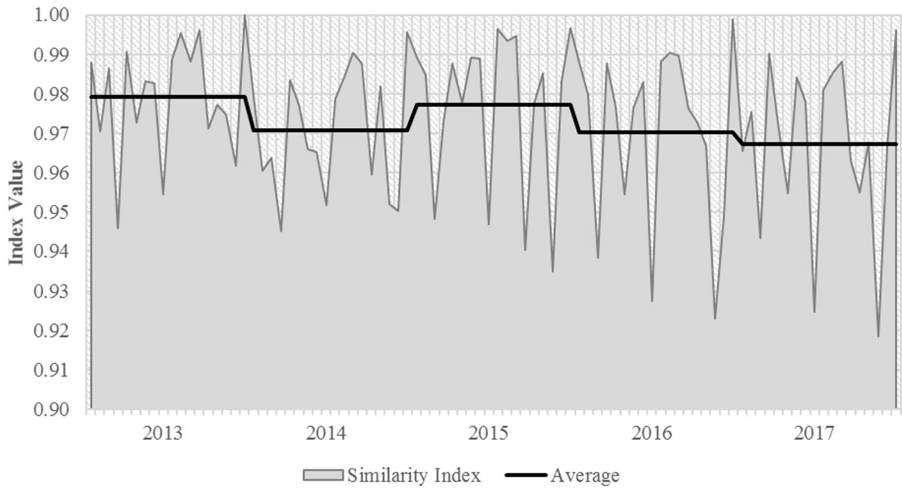
160. Companies Act 2006, s. 282(1).

161. There are, indeed, also rare instances where votes against a specific board candidate were motivated by the concerns about the individual candidate.

proposals included in the agendas of shareholders' meetings. More important is that the values of the similarity index of votes cast by the asset managers in line with the ISS recommendations, as illustrated by Figure 9, show a consistent declining trend.[162]

162. The values of the similarity index were lower for the recommendations by Glass Lewis with the averages below 0.93 in 2013. The index, similar to the ISS similarity index, was stable or decreased over years but then recorded a jump just above 0.96 in 2017. This increase happened mostly because of a technical change in the voting policy of Glass Lewis regarding its recommendations on standard antitakeover defence proposals. *See supra* note 139 and accompanying text.

Figure 9. Voting Along With the ISS Recommendations



Note: The figure shows how often the largest 18 asset managers (each point is a separate asset manager) voted along with the ISS recommendations. Higher values of the index indicate similar voting records. The figure also reports the annual average similarity index for all 18 asset managers.

At the individual asset manager level, the changes are not identical. Whereas some asset managers recorded significant changes in voting as compared to ISS recommendations, others had consistently high similarity of voting record with ISS recommendations. Aberdeen Asset Management started with a record of almost identical voting along with ISS recommendations in 2013 but was among the asset managers with the lowest similarity index in 2017—at 0.96. Columbia Threadneedle Investments saw the largest drop in the similarity index from 2013 to 2017—at 5.76%. The asset manager voted in accordance with ISS recommendation in less than 92% of cases in 2017. To the contrary, Marathon Asset Management voted in line with ISS recommendations (close to 100% of proposals over the entire five-year period). A few other asset managers, including Invesco PowerShares, Norway's NBIM, and Newton Investment Management, were more likely to vote along with the ISS recommendations in 2017 than in 2013.

It is widely believed that many asset managers heavily rely on proxy advisory services after the introduction of the 2003 mutual fund voting disclosure requirement in the United States.[163] Although proxy advisors are suggested to have weaker influence in the United Kingdom, they still play a significant role.[164] But this study shows that the dependence on proxy advisors, at least among the biggest asset managers, has decreased over time. Voting rights attached to larger shareholdings offer stronger incentives for independent voting. But smaller asset managers are expected to follow the recommendations of proxy advisors more often. Indeed, more large asset managers claim that instead of simply delegating voting, they rely more on research done by in-house investment stewardship teams.[165] These asset managers use analysis by proxy advisors and their recommendations as a useful input in their own decision-making over matters that each asset manager considers important.[166]

The ranks of fund managers voting in-house will continue to grow. At the same time, given the substantial share of trivial items on voting agendas, it is not reasonable to expect significant differences between the recommendations of proxy advisors and votes cast by asset managers.

4. Voting Practices and Asset Manager Characteristics

The results described above show that, notwithstanding the high share of trivial or uncontroversial voting proposals, there is a great deal of heterogeneity in voting decisions of the big asset managers. Some fund families are more management friendly than others. The question then is whether there are some general fund family characteristics that determine the friendliness of the fund's asset manager towards the management of their portfolio companies. For example, an earlier study relying on data from U.S. mutual funds found weak evidence that fund characteristics drive voting. In particular, funds with longer

163. *See* Cindy R. Alexander et al., *Interim News and the Role of Proxy Voting Advice*, 23 REV. FIN. STUD. 4419, 4423–24 (2010) (explaining the rise in proxy vote recommendation services).

164. *See* Andrew F. Tuch, *Proxy Advisor Influence in a Comparative Light*, 99 B.U. L. REV. 1459, 1479–81 (2019) (reporting industry perceptions about the influence of proxy advisors in the United Kingdom).

165. *See* Bioy et al., *supra* note 104, at 14 (reporting survey results that asset managers use proxy advisory services for research or for identifying important proposals, but they do not follow the recommendations blindly); Strampelli, *supra* note 104, at 821–22 (describing BlackRock's internal voting procedure).

166. *See* Daniel Thomas & Attracta Mooney, *Battle Brews Over Influence of Shareholder Advisers*, FIN. TIMES (Aug. 27, 2018), https://www.ft.com/content/0927edb4-c342-11e9-a8e9-296ca66511c9 (describing how fund managers use ISS recommendations).

time-horizons are more likely to support shareholder-sponsored proposals than funds with high turnover ratios.[167]

To test the relationship between asset managers' characteristics and their voting decisions, this study compares the mean results of the similarity index of asset manager votes and management recommendations by the country of origin of asset managers or the dominant investment strategy within the fund family. Table 5 below provides a breakdown of the values of the similarity index where a group of asset managers has a U.K. or U.S. origin or manages a family of funds with mostly passive or active investment strategy.

167. Angela Morgan et al., *Mutual Funds as Monitors: Evidence from Mutual Fund Voting*, 17 J. CORP. FIN. 914, 922–23 (2011).

Table 5. Voting Practices by Investment Management Style and Country of Origin

The table provides comparative data on the similarity index between asset manager votes and management recommendations for groups of asset managers by their country of origin and dominant investment style. Statistical tests were run for all proposals and for different categories of proposals. The mean results were tested using *t*-Test (assuming equal or unequal variance, as applicable) and the Wilcoxon Rank-Sum test. The latter drops outliers from the analysis where the distribution is not normal. The combination of both tests can thus offer better understanding of the results. The table reports only test values and significance. One asterisk indicates significance at the 5% level; two asterisks denote significance at the 1% level.

Group of Asset Managers	N	Mean: Variable 1 (UK or Active)	Mean: Variable 2 (US or Passive)	*t*-Test	Wilcoxon
All Proposals					
UK vs US	17	0.9736	0.9778	–0.547	–0.577
Active vs Passive	18	0.9755	0.9773	–0.249	0.317
Routine/Business Proposals					
UK vs US	17	0.9931	0.9944	–0.629	–0.192
Active vs Passive	18	0.9932	0.9948	–0.773	–0.408
Compensation Proposals					
UK vs US	17	0.8858	0.9612	–2.792*	–2.694**
Active vs Passive	18	0.9120	0.9527	–1.657	–1.132
Directors Related Proposals					
UK vs US	17	0.9756	0.9862	–1.202	–0.192
Active vs Passive	18	0.9805	0.9836	–0.511	0.317
Capitalization Proposals					
UK vs US	17	0.9802	0.9646	0.479	0.289
Active vs Passive	18	0.9679	0.9817	–0.488	–0.045
Antitakeover Related Proposals					
UK vs US	17	0.9920	0.8705	1.481	0.682
Active vs Passive	18	0.9914	0.8360	1.508	2.242*
Reorganization and Mergers Proposals					
UK vs US	17	0.9636	0.9440	0.858	0.290
Active vs Passive	18	0.9501	0.9605	–0.523	0.499

The breakdown of asset managers by the dominant investment style relies on data from Figure 4 above. Tests of the influence of the management style on voting decisions include NBIM as a passive asset manager, but NBIM was excluded from tests by the country of origin of asset managers as it is neither U.K., nor U.S.-based.[168] The results do not change significantly when NBIM is dropped from the analysis altogether.[169] On the other hand, although Fidelity Investments is one of the largest managers of index funds, it is still heavily exposed to active management. In addition, Fidelity's passive funds are managed by Geode Capital Management, thus Fidelity Investments was classified as an active manager. Similarly, Invesco's passive funds have a separate manager—Invesco PowerShares. Since the study relies on voting decisions cast by Invesco PowerShares, Invesco was treated as a passive manager.[170]

The results show that there is very little difference between the management "friendliness" of asset managers based in the United Kingdom or the United States. Similarly, voting decisions of asset managers with active or passive investment strategies do not differ significantly. Under all four scenarios, asset managers voted in line with management recommendations in more than 97% of total proposals.

The situation changes on closer inspection of specific proposal types. U.K.-based large asset managers tended to vote against compensation proposals more often than U.S.-based asset managers. The mean similarity index on compensation proposals for the group of U.K. asset managers stands at 0.8858, whereas the mean similarity index for U.S. asset managers is 0.9612. This indicates that U.K. asset managers voted against compensation proposals in almost 12% of cases, whereas U.S. managers opposed less than 4% of compensation proposals. The difference is statistically significant in both *t*-Test and Wilcoxon Test at 5% and 1% levels, respectively.[171] There can be several reasons explaining different practices of voting on executive pay by large asset managers across the Atlantic, including that U.S. shareholders are more accustomed to higher executive pay and only pay attention to instances where pay is not aligned with performance. On the other hand, high pay itself may provoke shareholder opposition among U.K.-based shareholders.[172]

Likewise, on most types of proposals, passive and active asset managers tended to vote similarly. On some proposals, including compensation related proposals, passive asset

168. For the explanation of the decision to classify NBIM as a passive asset manager, see *supra* notes 57–58 and accompanying text.

169. Unreported tests are on file with the author.

170. Other passive managers in the analysis were BlackRock, Vanguard, State Street, Legal & General, and M&G Investment Management. Active managers include Fidelity Investments, Capital Group, T. Rowe Price, MFS Investment Management, and Franklin Templeton from the United States and Aberdeen Asset Management, Standard Life, Schroder, Columbia Threadneedle, Newton Investment Management, and Marathon Asset Management from the United Kingdom.

171. U.K.-based asset managers also tended to vote marginally more often against management supported board nominees than U.S. asset managers, although this difference is not statistically significant. On other types of proposals, U.S. asset managers are less management friendly, but again, none of the results is statistically significant.

172. *See, e.g.*, Lex., *Persimmon/UK Exec Pay: Help to Bye*, FIN. TIMES, Nov. 8, 2018, at 12 (UK ed.) (explaining the removal of Persimmon PLC's CEO because of negative attention over the scandal involving £110 million bonus payment by changes in the perceptions of shareholders: the mantra that "big rewards are merited by big returns" was abandoned; the size of executive pay has begun to matter since around 2015). *See also* Naomi Rovnick et al., *Persimmon Forces out Chief as £110m Bonus Becomes Key Figure in Pay Row*, FIN. TIMES, Nov. 8, 2018, at 1 (UK ed.).

managers voted against management more often than active managers. On others, like reorganization and mergers, active asset managers were less management friendly. The differences between the similarity indexes for passive and active asset manager groups are not, however, statistically significant. Only in relation to antitakeover related proposals were passive managers much more likely to vote against management recommendations than active managers (statistically significant result for one of the tests). This result can essentially be explained by the voting practices of two U.S.-based passive asset managers—Invesco PowerShares and State Street—which long practiced automatic voting against proposals to call shareholders' meetings on shorter notice in the case of takeovers. One of the managers has reversed this practice since the 2017 shareholders' meeting season.[173]

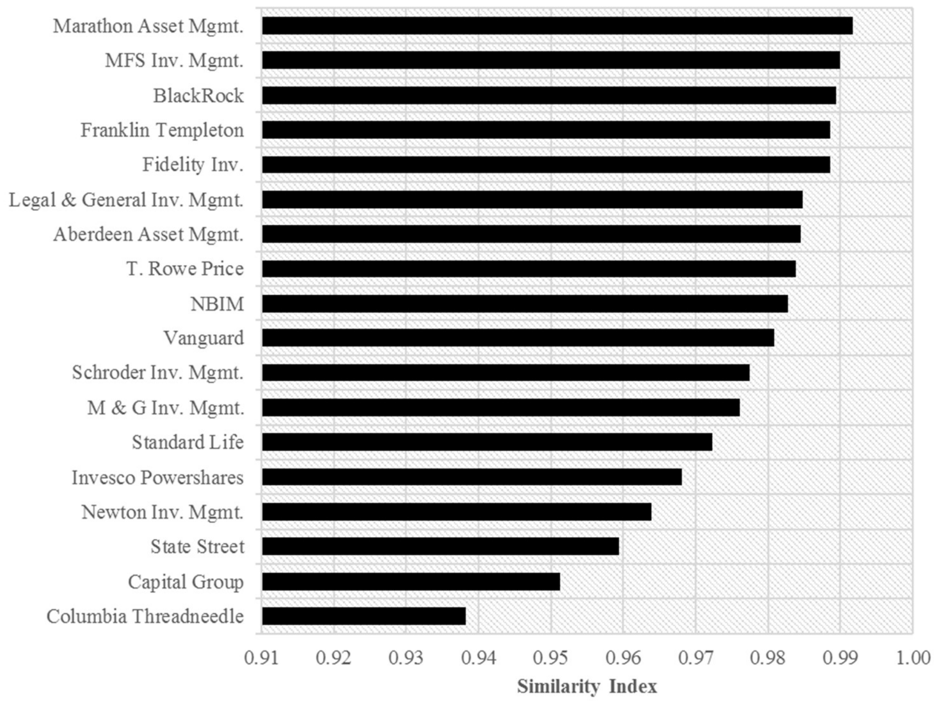
In sum, there is little evidence of any dichotomy between passive versus active, or between U.K. versus U.S., asset managers. The origin of an asset manager or its dominant investment strategy do not have a defining influence on the manager's decision to vote shares in a specific way. Apart from compensation related proposals—where U.K.-based assed managers are more likely to vote against management—differences are small-scale on all other proposals. There is indeed variation in voting practices, as demonstrated in Figure 10,[174] but this variation seems to be driven more by manager-specific factors than by general characteristics applicable across asset managers. The most management-friendly manager in the sample that was also most likely to vote in accordance with the ISS recommendations is Marathon Asset Management, an investment manager affiliated with actively managed funds.[175] Clearly, some asset managers are more proactive shareholders than others. This is a careful choice made by an asset manager considering various factors, such as the costs of informed voting, available resources, the manager's business model, the image of the manager among industry professionals and the public, and, perhaps, also the personal preferences and beliefs of the manager's top officers.

173. *See supra* notes 149 & 154 and accompanying text (noting the shift for Invesco Powershares).

174. Similarly, voting records show variation in the voting behavior of the largest asset managers at the shareholders' meetings of U.S. companies. Matthew J. Mallow, Asset Management, Index Funds, and Theories of Corporate Control 22–24 (Dec. 22, 2019) (unpublished manuscript), *available at* https://ssrn.com/abstract=3483573 [https://perma.cc/T95T-CKFX].

175. *See supra* Part IV.B.3; *see also infra* Figure 10 (displaying Marathon Asset Management's strong tendency to follow management recommendations).

Figure 10. Similarity Index of Votes Cast and Management Recommendations



More broadly, the literature often overstates the role of foreign ownership among large institutional investors of U.K. companies and the division of large fund families into active and passive based on the dominant investment style. Many foreign fund families manage their U.K. investments through locally formed investment advisors, which can also participate in local trade groups and have substantial presence in the City of London.[176] Therefore, although formally foreign, some fund families, due to strong local presence, may act more like other U.K.-based asset managers than their U.S. peers.[177] This means that the division of large asset managers based on nationality can be provisional.

Similarly, often it is also too simplistic to classify large fund families into purely active or passive categories. Large fund families combine many investment funds with various investment strategies under one roof.[178] These funds are, as a rule, managed by a single asset manager which must consider the interests of both active and passive funds within the family of funds in deciding how to vote the shares of portfolio companies owned by those funds.[179] This means that the final voting decisions are often a compromise between the interests of funds with different investment strategies.

Another note of caution is that low disapproval rates of management-sponsored proposals does not automatically mean that the asset manager is more pro-management. For the full picture, voting by asset managers needs to be considered in combination with engagement behind closed doors. As suggested by a recent study, BlackRock will first try to promote change through closed-door negotiations with the company management and will only cast a negative vote if the management is unresponsive or slow in addressing requested changes.[180] Similarly, an early study of shareholder engagement by TIAA found that the manager reached an agreement with the majority of companies that it had targeted with governance proposals and thus did not need to vote against management in public.[181] By contrast, other asset managers may be less reliant on private negotiations and will instead apply strictly standard voting guidelines without prior engagement.[182]

Reliance on publicly available voting data alone may thus understate shareholder engagement efforts by some big institutional investors. However, it is difficult to discern which of the biggest asset managers covered in this study were active behind closed doors and how often their targets for private negotiations were the FTSE 100 companies. Private negotiations are certainly an important part of shareholder engagement but voting remains the main channel through which shareholders interact with managers in publicly traded companies.[183]

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176. For example, BlackRock provides investment management services in the United Kingdom through its U.K. subsidiaries, including BlackRock Investment Management (UK) Limited, which is headquartered in London. *BlackRock Investment Management (UK) Limited*, FIN. CONDUCT AUTH., BANK ENG. PRUDENTIAL REG. AUTH. (2019), https://register.fca.org.uk/ShPo_FirmDetailsPage?id=001b000000MfFNsAAN [https://perma.cc/JDM7-UHEC].

177. *See* Tuch, *supra* note 164, at 1502–03 (explaining which trends hold true or are effected by home and location).

178. Morley, *supra* note 115, at 1416.

179. *See id.* at 1416–17 (outlining the manager's fiduciary duties).

180. Bioy et al., *supra* note 104, at 13.

181. *See* Carleton et al., *supra* note 77, at 1343–48 (showing TIAA-CREFF using targeting techniques).

182. *See* Bioy et al., *supra* note 104, at 13 (discussing Amundi, a company that follows a strict voting policy).

183. *See supra* notes 79–80 and accompanying text (showing strong reliance on voting).

V. Discussion of the Results and Implications

The findings of this study both contribute to the growing literature on the rise of large fund families and have implications for policy discussions on the stewardship role of institutional investors. This part starts by the discussion of the results in light of the existing academic literature. The voting evidence from the United Kingdom offers support for the predictions made in the literature regarding the limits of stewardship by large fund managers. But the results also indicate growing incidence of engagement and differences across fund managers, which cannot be fully explained by the dominant agency-cost account of stewardship by large fund managers. The second part briefly outlines some policy implications of the study, particularly on restrictions on the voting rights of large fund families, on voting cooperation between asset managers, on the role of activist shareholders and interactions between activists and large fund families, on voting record disclosure, and on the possible effects of common ownership on competition.

A. Discussion of the Results

The evidence presented above indicates that large asset managers are taking an increasingly active role in engaging with their U.K. listed portfolio companies.[184] If, previously, many fund managers effectively delegated voting to external proxy advisory firms by following their recommendations, today more funds deviate from these recommendations. The largest fund managers have their internal corporate governance team[185] that reviews and proposes "in-house" proxy recommendations concerning how to vote and engage with some portfolio companies.

Although there remains high similarity between the recommendations of proxy advisors and the votes of large asset managers, this can primarily be explained by the trivial nature of many voting agenda items. It is also not clear the extent to which large institutional investors may influence, perhaps indirectly, the recommendations of proxy advisors. As a result, proxy advisors may be simply aggregating the majority view or the view of the most influential asset managers in their voting recommendations. As Andrew Tuch explains, U.K. institutional investors, acting collectively through institutional investor trade groups, have traditionally had bigger influence over the voting guidelines of proxy advisors, than investors in the United States.[186] Particularly, until 2015, ISS used the policy and voting guidelines of the Pension and Lifetime Savings Association (PLSA), a pension funds' trade group, as their reference.[187] After 2015, ISS's voting guidelines for U.K. companies have mostly been consistent with those of the PLSA and also relied heavily on guidelines of other trade groups.[188]

The growing attention to shareholder voting by large asset managers is a sign of strengthening shareholder engagement, albeit with a special focus. Although voting decisions by asset managers may occasionally be affected by weak business results, more

184. For similar developments in the United States, see Ian R. Appel et al., *Passive Investors, Not Passive Owners*, 121 J. FIN. ECON. 111 (2016).

185. *See* DOWNES ET AL., *supra* note 39, at 19 (finding that large institutional investors have developed in-house proxy administration departments).

186. *See* Tuch, *supra* note 164, at 1485–86.

187. *See id.* at 1485.

188. *See id.*

often the target of interventions are weak or unconventional corporate governance arrangements and management's failure to deal with commonly accepted global challenges such as diversity or inequality. This is evidenced by strong attention to management compensation proposals when they differ from accepted practices. Meanwhile, director elections, the primary means by which shareholders can influence corporate decision-making, attract attention mostly in combination with corporate governance matters, like concerns with board members responsible for problematic compensation or nomination policies.

As a result, large asset managers are acting as the promoters of the universal governance standards across portfolio companies.[189] Large fund managers have relationships with companies in many industries and in different parts of the world which puts them in a strong position to identify broad corporate governance needs of companies and common societal challenges that companies are expected to deal with. Fund managers then use their voting power to promote the best governance practices and activity regarding global challenges across the entire portfolio.[190] Shareholder engagement by large fund managers is thus influencing corporate governance and social aspects but may have only indirect impact on improved business performance—only to the extent that (and if) stronger governance oversight can also lead to better corporate performance.

But engagement with a distinct governance inclination limits not only the scope of matters subject to greater scrutiny by large fund managers but also the effectiveness of such limited investor oversight. The universal promotion of best practices and activities can disregard the idiosyncratic needs of portfolio companies. Very often, large investment fund stewardship is based on one-size-fits-all approach where the manager's voting guidelines are applied automatically to every portfolio company without considering detailed company-specific information.[191] This may lead to strengthening corporate governance in portfolio companies and promoting solutions for global challenges by ticking the boxes of best governance practices without necessarily improving the governance needs of each individual company.[192]

The focus on corporate and social governance accords with the prediction that economies of scale would encourage greater shareholder engagement by institutional investors on matters that are shared across many portfolio companies as opposed to voting on items that are company specific.[193] Constraints on organizational capabilities of asset managers do not allow them to tailor votes to firm-specific information in every portfolio company. Because large fund families own shares in hundreds of companies in different countries and most of those companies hold their annual meetings during April and May

189. *See* Appel et al., *supra* note 184, at 134 (explaining that similar results have been found in a prior study of shareholder engagement by passive investors in U.S. companies).

190. For a related argument that large fund managers can promote better corporate compliance practices across portfolio companies, see Asaf Eckstein, *The Virtue of Common Ownership in an Era of Corporate Compliance*, 105 IOWA L. REV. 507, 538–63 (2020).

191. An earlier study offers similar evidence regarding voting by large investment managers in U.S. publicly traded companies. *See* Gerald F. Davis & E. Han Kim, *Business Ties and Proxy Voting by Mutual Funds*, 85 J. FIN. ECON. 552, 563–64 (2007) (finding that mutual funds' votes are explained by policies, not by business ties).

192. *See* Morgan et al., *supra* note 167, at 922–23 (finding that funds are more likely to support proposals that target firms with weaker governance); Appel et al., *supra* note 184, at 124–26, 134 (finding similar evidence for passively-managed funds but questioning whether passive investors attempt to determine individual governance needs of each portfolio company or follow a low-cost "check-the-box" approach to governance).

193. *See supra* notes 106–109 and accompanying text.

every year, the stewardship teams of asset managers must concentrate immense resources in a very short time frame in order to analyze all voting items carefully and cast informed votes.[194] As a result, no matter how large the manager's internal corporate governance team is, it cannot prepare tailored recommendations for every company.

In sum, voting practices of large fund managers in U.K. publicly-traded companies share many similarities with the empirical findings of a study by Bebchuk and Hirst on passive fund voting in U.S. companies.[195] But this study also identifies certain patterns, such as growing engagement via voting or substantial differences in engagement levels among fund managers with similar investment strategies and business models, that cannot be explained solely by the agency-cost framework of asset manager behavior.[196] In addition to maximizing financial gains, stewardship efforts of large fund managers can be influenced by individual beliefs of managers and broader viewpoints dominating in markets where fund managers operate. As a result, some fund managers may follow much more active position on investor stewardship than their close peers. This also means that the overall stewardship role of large fund managers may be more positive than the agency-cost model predicts.[197]

Furthermore, large asset managers take stewardship decisions in a dynamic environment where actions by one manager can influence the decisions by others. Increased use of voting rights by some large asset managers can also have positive peer-effects for other institutional investors, thereby further strengthening shareholder engagement. Institutional investors long refrained from voting against management proposals to avoid costs associated with direct confrontations, such as damaged business ties with portfolio companies. The willingness of each investor to vote against a management proposal may be constrained by the equilibrium: if all other shareholders are likely to support management, the motives of separate shareholders to deviate are weakened.[198] A handful of "against" votes are not only costly, but they will also have no meaningful effect on the voting outcome. But if more shareholders vote against the proposal, then the ability of management to retaliate against many other shareholders is limited.[199]

Evidence on shareholder voting supports the role of peer-effects. A study of peer-effects on mutual fund voting during director elections shows that mutual funds are more likely to vote "for" a director if they think other funds are more likely to register the same

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194. Japan is notoriously famous for the concentration of annual shareholders' meetings on a single day at the end of June. Particularly, 725 companies, or 30.9% of all listed companies, held their 2018 annual shareholders' meeting on Thursday, June 28, 2018. Tokyo Stock Exch., *Statistics on Dates of Annual General Shareholders Meetings of Companies Whose Fiscal Years Ended in March 2018*, JAPAN EXCHANGE GROUP (June 8, 2018), https://www.jpx.co.jp/english/news/1021/20180608-10.html [https://perma.cc/V3AM-TV23]. *See also Voting in Japan*, INV. COMM. JAPAN, http://www.icj.co.jp/en/voting/ [https://perma.cc/5HN7-FNTH] (last visited Feb. 24, 2020); Leo Lewis, *Japan's AGM Season Set for Lively New Era*, FIN. TIMES (June 22, 2015), https://www.ft.com/content/21852fb0-18cf-11e5-8201-cbdb03d71480.

195. *See* Bebchuk & Hirst, *supra* note 36, at 2088–91, 2095–101.

196. For the overview of the agency-cost model of stewardship by large institutional investors, see *supra* Part III.B.

197. For a positive account of the role of large fund managers, see Fisch et al., *supra* note 106.

198. *See generally* Mark Granovetter, *Threshold Models of Collective Behavior*, 83 AM. J. SOC. 1420, 1424–25 (1978) (showing that for explaining outcomes of collective actions, in addition to individual preferences of all actors, we need to know how these individual preferences interact).

199. *Id.* at 1422.

vote.[200] The recent example of Unilever discussed above illustrates the influence of peer-effects.[201] With more large investors going public with their disagreement over the change of the company's domicile, the costs of opposing the management lessened. As a result, shareholder dissent grew gradually over time and then escalated quickly.[202]

All this means that various factors come together to influence stewardship practices of large fund managers. To make things more complicated, occasionally large fund managers go beyond governance oversight and exercise much more detailed scrutiny of a small number of portfolio companies. More focused monitoring resources are believed to be usually allocated to portfolio companies that are strongly underperforming or are involved in highly-publicized scandals.[203] Given the significant stakes associated with the power, or lack thereof,[204] of large asset managers with common shareholdings, we need more studies to understand better the circumstances in which institutional investors decide to intervene in the management of portfolio companies on more custom-made basis.

B. Implications of the Findings

"In-house" teams of large asset managers—notable examples are BlackRock, Vanguard, NBIM, State Street, and Legal & General—are becoming important actors in corporate governance, and company managers, whether willingly or unwillingly, must respond to them. Other managers of large fund families may not have specialized shareholder engagement teams, but all have voting guidelines that reflect the expectations of their investors. Although managing companies in this group may delegate voting to proxy advisory firms or follow their voting recommendations, this does not necessarily mean they have a weak voice in corporate governance. To the contrary, proxy advisors may base voting recommendations on criteria that are important for asset managers. Accordingly, the voting guidelines of asset managers may have a strong influence on the recommendations of proxy advisory firms.[205]

Certainly, there are concerns that company CEOs may influence fund managers and distort their voting decisions.[206] The largest fund families, however, are among the top shareholders in many publicly-traded companies and, as a result, have huge and growing

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200. *See* Gregor Matvos & Michael Ostrovsky, *Heterogeneity and Peer Effects in Mutual Fund Proxy Voting*, 98 J. FIN. ECON. 90, 97, 99–100 (2010).

201. *Supra* note 152 and accompanying text.

202. This draws parallels with Ernest Hemingway's famous description of the process of bankruptcy in the novel *The Sun Also Rises*. "'How did you go bankrupt?' Bill asked. 'Two ways,' Mike said. 'Gradually and then suddenly.'" *See* ERNEST HEMINGWAY, THE SUN ALSO RISES 136 (1926). This is exactly how peer-effects may accelerate shareholder public opposition to management proposals.

203. Black & Coffee, Jr., *supra* note 20, at 2069. For supporting empirical evidence, see Lilian Ng et al., *Firm Performance and Mutual Fund Voting*, 33 J. BANKING & FIN. 2207, 2211–12 (2009).

204. *See, e.g.*, Bebchuk & Hirst, *supra* note 36, at 2059–70 (warning that the agency problems of index managers make them excessively deferential to corporate managers); Lund, *supra* note 103, at 510–12 (explaining that passive funds face strong agency conflicts that make their "thoughtful participation" in governance unlikely).

205. *See* Choi et al., *supra* note 126, at 899 (offering evidence that proxy advisory firms do not direct voting by institutional investors but rather aggregate voting preferences of institutional investors); Stephen Choi et al., *Director Elections and the Role of Proxy Advisors*, 89 S. CAL. L. REV. 649, 696–97 (2009) (the same); Cotter et al., *supra* note 20, at 56 (offering evidence that mutual fund managers vote consistently with ISS recommendations but speculating that the expectations of fund managers may in fact influence the proxy recommendations of ISS).

206. *Supra* Part III.B.2.

influence, which they are increasingly willing to use. It is thus questionable who has more influence: corporate managers over large fund managers or the other way around.

Differences in voting practices across large asset managers therefore have important implications for publicly traded companies. If, indeed, some asset managers are more active in opposing corporate managers than others, then the company's shareholders will be highly relevant. It is important, not only for corporate managers, but also for other shareholders and activists, who may receive different levels of support for their proposals. The increasing power of large asset managers poses also some questions for policymakers regarding possible reforms that may strengthen stewardship. Several significant implications of the study are briefly discussed below.

1. The Value of Monitoring Corporate Governance and Whether Some Institutional Investors Should Not Vote

The value added by some corporate governance proposals, as well as the reasonableness of blind application of corporate governance solutions to all companies, is open to criticism. Numerous studies looked at the effect of corporate governance in general and specific governance proposals on firm performance, and the evidence is contradictory.[207] Perhaps, companies vary in their needs of good corporate governance—companies at different stages of their life cycles will rely more, or less, on corporate governance. Furthermore, the concept of good corporate governance itself is not clearly established and is continually evolving. Channels through which corporate governance adds value will certainly change over time. With growing experience, proposals that were considered *de rigueur* yesterday, may lose their appeal today and be replaced by others tomorrow.

Uncertainties regarding the value of some corporate governance proposals certainly do not justify depriving the major promoters of good corporate governance standards of their voice.[208] This is not a superior solution to blind application of one-size-fits-all corporate governance standards across all publicly traded companies. Even though the value of corporate governance for a given company is not certain, engagement efforts of large asset managers have been significant contributions towards advancing corporate governance standards across all publicly-traded companies, including in matters of board diversity and executive pay.[209] Without such efforts, a key driver of good corporate

207. It is an open question whether good corporate governance leads to improved company performance. One complication in measuring this effect is that proposals aimed at strengthening corporate governance do not have immediate effects on performance. Carleton et al., *supra* note 77, at 1351.

208. Dorothy Lund argues that passive investing weakens incentives of informed voting and may thus do more harm than good. To correct this market failure, she proposes government intervention by eliminating passive fund voting. The proposal, as argued, will strengthen the vote of more informed shareholders—primarily, actively-managed fund managers and activist hedge funds. *See* Lund, *supra* note 103, at 524–25, 528–30; *see also* Weil, *supra* note 145 (explaining that passive fund managers lack incentives to cast informed votes and increasingly are crowding out the influence of smaller peers; they thus need to abstain from voting their shares); Bernard S. Sharfman, *Mutual Fund Advisors' "Empty Voting" Raises New Governance Issues*, CLS 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/36AL-NYWY] (discussing the decoupling of share ownership and voting rights in the mutual fund industry and suggesting that voting rights of fund managers needs to be limited); Henderson & Lund, *supra* note 145 (arguing that passive fund managers must abstain from voting).

209. As explained above, large asset managers may lack information to cast informed votes on each director candidate, but often votes are cast against all candidates responsible for promoting good governance standards if

governance will be weakened. Furthermore, it is far from clear that actively managed fund groups are generally better in investor oversight over non-standard corporate performance matters.

The argument that standard voting practices of large institutional investors cannot constitute a perfect form of monitoring is beyond question.[210] But instead of taking away their voting rights, we need better engaged asset managers. If large asset managers fail to propose company-specific solutions or be effective monitors of corporate performance, then we need to put in place mechanisms which create the right incentives to improve monitoring at both an operational and governance levels. This requires taking a broader and more systematic view on mechanisms of shareholder monitoring and on various market participants that may contribute to this process.

2. Sharing the Costs of Informed Voting Among Large Asset Managers

Institutional investors can improve access to firm-specific information and reduce individual costs of obtaining such information by establishing shared stewardship teams with bigger staff.[211] Joined actions may reduce not only the costs of engagement, but also mitigate the business conflicts that individual asset managers may face in case of opposing corporate managers.[212] One concern with this proposal is that it may violate competition laws of various jurisdictions by coming under acting in concert rules or may trigger disclosure rules for shareholder groups seeking to influence a company; in the European Union, in addition, this proposal may also potentially trigger the mandatory bid rule of takeover regulations.[213] This is, however, more a technical problem with possible solutions.[214]

Historically, trade groups of institutional investors in the United Kingdom played a much bigger role than in the United States.[215] Consider, for example, the activities of the Investor Forum, a community interest company set up in 2014 on the recommendation of the Kay Review of U.K. Equity Markets to improve shareholder engagement.[216] The Forum, which counts among its members some of the largest institutional investors of U.K. companies,[217] delivers the concerns of investors to corporate boards as a single cohesive

the company fails to comply. *Supra* note 161 and accompanying text.

210. *See* Lund, *supra* note 103, at 510 (arguing that an automated approach to governance pursued by passive investors is not in the best interest of their portfolio companies).

211. The original idea was proposed back in 2002 by Vanguard's Jack Bogle in a meeting with several index fund managers. Bogle, *supra* note 113, at 37–38.

212. *See* Tuch, *supra* note 164, at 1482 (describing how engagement through institutional investor groups reduces business conflicts).

213. *See* Strampelli, *supra* note 104, at 849. Evidence suggests that large institutional investors take rules on acting in concert seriously and consider them as one of the important impediments that discourages cooperation on matters related to shareholder engagement. *See* McCahery et al., *supra* note 75, at 2922.

214. *See, e.g.*, Tuch, *supra* note 164, at 1486 (describing the practices of one of the institutional investors' trade groups in the United Kingdom to develop an engagement strategy based on the views of its members, but without seeking to form an agreement among members to avoid triggering various rules).

215. *See id.* at 1481–89 (describing the past influence of institutional investor trade groups in the United States and United Kingdom).

216. Attracta Mooney, *Andy Griffiths: The Cheery Scrapper Who Keeps UK Plc in Line*, FIN. TIMES (Oct. 24, 2018), https://www.ft.com/content/4cb95afa-1861-3793-bd2d-fc33a71949df; *Corporate Governance: Passive, Aggressive*, ECONOMIST, Sept. 1, 2018, at 55 (USA ed.).

217. The Investor Forum's members include Aberdeen Standard Investments, Artemis Investment

voice.[218] Membership in the Forum does not prevent its members from acting individually, but collective representation certainly strengthens the voice of institutional investors in private discussions with corporate boards.[219]

A bigger problem, one that is less likely to be solved easily, is that shared voting analytics will put an end to voting plurality by unifying the voice of the largest shareholders. This may lead to groupthink in decision making and failure to consider alternative courses of action. Moreover, it is likely that this shared analysis will remain the same standard one-size-fits-all approach that focuses on governance but rarely on corporate performance. Even if shareholder stewardship teams double or triple in size, they cannot engage with every portfolio company on an individual basis; neither will they have enough expertise for going beyond governance engagement.

3. The Role of Activist Hedge Funds

The combined value of monitoring by large asset managers and hedge fund activists opens better prospects for strengthening shareholder engagement on an individual basis and with stronger focus on corporate performance.[220] Large asset managers can use activists' operational demands—like proposals to divest businesses, return cash to shareholders, replace the company CEO or board members—as a source of high-quality company-specific information that may assist in better decision-making over the ways of casting their votes. Importantly, the final decision remains with large institutional investors. To be clear, large fund managers do not need to, and probably cannot, become activist shareholders. But company-specific analysis by activist shareholders can broaden the scope and improve the quality of engagement by large fund managers.

Professors Gilson and Gordon call institutional investors "latent" activists who are ready to be proactive monitors of portfolio companies but need someone to supply expert evidence that will assist in casting informed votes.[221] Operational activism requires acquiring company-specific information and can thus be performed by those shareholders who have sufficient resources to invest in information acquisition and, also, large enough shareholding to justify the costs of acquiring information.[222] Activist hedge funds are in the position to do this. Compare, for example, Pershing Square Capital Management LP, an activist hedge fund, that has an investment team of nine and various other employees that focus on a portfolio of about a dozen companies to large passive investors, like BlackRock, Vanguard, and State Street, that employ teams of 10-25 employees for

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Management, BlackRock, Capital Group, Columbia Threadneedle Investments, Invesco, Legal & General, M&G Investments, Schroder Investment Management, T. Rowe Price, and others. The full list is available at https://www.investorforum.org.uk/our-members/#members [https://perma.cc/7GQ3-V6HD] (last visited Sept. 17, 2018).

218. Some examples of collective interventions are described on the Forum's website. *See Case Studies*, INV. F., https://www.investorforum.org.uk/activities/collective-engagement/case-studies/ [https://perma.cc/7LFA-Z56P] (last visited Sept. 17, 2018).

219. *See* ECONOMIST, *supra* note 216.

220. *See* Fisch et al., *supra* note 106, at 52.

221. *See* Ronald J. Gilson & Jeffrey N. Gordon, *Agency Capitalism: Further Implications of Equity Intermediation*, *in* RESEARCH HANDBOOK ON SHAREHOLDER POWER 32, 50 (Jennifer G. Hill & Randall S. Thomas eds., 2015) (describing investors as reticent and needing "market actors to invoke their sophistication"); Gilson & Gordon, *supra* note 96, at 895.

222. Lucian A. Bebchuk, *The Myth that Insulating Boards Serves Long-Term Value*, 113 COLUM. L. REV. 1637, 1658–59 (2013).

analyzing governance in thousands of portfolio companies.[223]

Activist-produced information, indeed, risks being one-sided. But instead of viewing every activist demand as dangerous from the outset, large asset managers can approach each case individually and support good initiatives, while rejecting bad ones.[224] In this way, large asset managers will receive crucial company-specific information and can also engage with their portfolio companies on strategy, performance, and operational matters. Activist hedge funds, meanwhile, will get incentives to make demands that are appealing to a broad group of shareholders, including those large asset managers that are investing for longer. Interactions between large asset managers and hedge fund activists can thus be mutually beneficial.

4. Promoting the Long-Term Value of Proposals by Activist Hedge Funds

The combination of the efforts of large asset managers and activist hedge funds may also correct the short-termism concerns that some assign to the demands of activist hedge funds. Activist hedge funds often cannot succeed in their campaigns without the support of the increasingly influential large asset managers. The average activist holding in a target company is about 8%.[225] Therefore, successful activism requires securing the support of major asset managers by aligning activist demands with the preferences of large asset managers.[226] The top 20 asset managers, which control around 22% of votes of companies in both FTSE 100 and FTSE 350 companies,[227] are often the swing voters that determine the outcomes of activist demands.[228]

The dominance of large asset managers, which are mostly long-term investors, in the capital of listed companies means that the costs of launching a short-term oriented activist demand are not justified. According to some estimates, minimum costs of an activist campaign start from an average of about $3 million (USD) and increase along with moving forward through the stages of the campaign.[229] The costs of a full activist campaign average at about $11 million (USD).[230] Given these costs, activists are expected to put forward proposals that are likely to receive broad support from shareholders—particularly from a group of influential large asset managers. Many activists have already changed their strategies to focus more on proposals that put greater emphasis on long-term strategy and

223. *See* Krouse et al., *supra* note 1, at A12 (reporting the size of stewardships teams of the largest asset managers); David Benoit, *Activist Meets Index Fund*, WALL ST. J., Oct. 25, 2016, at A12.

224. This is the main message Paul Singer, the founder and co-CEO of the activist Elliot Management Corp., communicated in a Wall Street Journal piece. *See* Paul Singer, *Efficient Markets Need Guys Like Me*, WALL ST. J., Oct. 20, 2017, at A15 (arguing that with the increasing share of passive investors, the markets will need the contribution of activists in analyzing company-specific information).

225. Nickolay Gantchev, *The Costs of Shareholder Activism: Evidence from a Sequential Decision Model*, 107 J. FIN. ECON. 610, 622 (2013).

226. *See* Gilson & Gordon, *supra* note 96, at 896–97 (describing specialization between activists and institutional investors).

227. *See supra* Part II (Figure 1, Figure 3).

228. *See* Hill, *supra* note 136, at 539–40 (noting that large institutional investors have become the swing voters that "all sides are now out to woo").

229. Gantchev, *supra* note 225, at 623 (these costs refer to mounting an activist campaign in the United States).

230. *Id.*

governance.[231] Activist initiatives are also becoming more collaborative.[232]

5. Can the Mandated Disclosure of Voting Records Help?

U.K.-based investment funds, unlike their U.S. peers, are not required to disclose voting records by the law. Voting record disclosure in the United Kingdom is voluntary as part of the best practice guidelines required by the Stewardship Code.[233] In 2016, the Financial Reporting Council, the United Kingdom's regulator for promoting high quality corporate governance, introduced a ranking of asset managers based on the quality of their stewardship compliance statements.[234] The aim of this initiative was to improve the quality of compliance with the Stewardship Code and reporting. Although important, this ranking is not likely to ensure uniform high disclosure practices across the asset management industry. To date, fund returns play much more important role in marketing investment fund products than strong stewardship. Rational fund investors may even pick funds that are less likely to be active stewards because this may, at least in theory,[235] save on the costs of managing the fund.[236]

Indeed, there are wide variations in reporting practices among the U.K.-based large asset managers.[237] But it is questionable whether mandated disclosure can improve shareholder engagement. As shown in this study, there is no evidence that U.K.-based asset managers are less active in shareholder engagement through voting than their U.S.-based peers, which are subject to mandated disclosure rules.[238] This result is consistent with an earlier finding that U.S. mutual fund voting behavior remained unchanged after the introduction of the mandated mutual fund vote disclosure requirement in the United States.[239] Mandated disclosure can thus improve access to uniform information, but it is far from obvious that disclosure can strengthen shareholder engagement as well.

231. *See, e.g.*, Strampelli, *supra* note 104, at 830–33; Cara Lombardo, *Activist Elliot Tries Softer Tack*, WALL ST. J., Oct. 9, 2018, at B6 (describing efforts by Elliott Management Corp., one of the most combative activist hedge funds, to improve its relations with large investors and target companies).

232. *See* Lombardo, *supra* note 231.

233. *See* STEWARDSHIP CODE 2012, *supra* note 122 and accompanying text. The Shareholder Rights Directive II, which came into force in June 2019, requires institutional investors and asset managers to "explain the most significant votes" but falls short of requiring voting record disclosure. Shareholder Rights Directive II, *supra* note 6, art. 1(3), at 16. This requirement was implemented in the United Kingdom without changes. FIN. CONDUCT AUTHORITY, CONDUCT OF BUSINESS SOURCEBOOK, RELEASE 47 (Feb. 2020), s. 2.2B.7(1), https://www.handbook.fca.org.uk/handbook/COBS.pdf [https://perma.cc/MV7N-AXJU].

234. *See Tiering of 2012 Stewardship Code Signatories: Asset Managers*, FIN. REPORTING COUNCIL, https://www.frc.org.uk/investors/uk-stewardship-code/uk-stewardship-code-statements/asset-managers [https://perma.cc/UY76-B5QB] (last visited July 18, 2018).

235. In practice, the saved money may be used to increase the remuneration of fund advisors.

236. Palmiter, *supra* note 64, at 1474.

237. *See supra* notes 123–125 and accompanying text (showing that voting results of some of the asset managers are not available publicly; others, on the other hand, disclose more information than is required in the United States).

238. It is certainly possible that non-disclosing U.K.-based asset managers are the ones that do not engage with portfolio companies at all. Hence, a universal requirement to disclose voting records may drive asset managers towards more active engagement or at least creating an appearance of engagement.

239. *See* K.J. Martijn Cremers & Roberta Romano, *Institutional Investors and Proxy Voting on Compensation Plans: The Impact of the 2003 Mutual Fund Voting Disclosure Rule*, 13 AM. L. & ECON. REV. 220, 234, 239–42 (2011).

6. Common Ownership and Anticompetitive Problems

Large asset managers' standard voting practices driven by economies of scale cast doubt on some of the results of a growing and influential stream of literature that studies the effects of common ownership. This literature acknowledges the role of voting for large fund families, but casts doubt on the value of such voting because the voting preferences of fund managers may be distorted. Because of the shared common ownership, a fund family owns shares in the entire market or industry, and not just in one company. Accordingly, the voting preferences of fund managers may be distorted towards the market. This claim has important implications for corporate acquisitions,[240] executive compensation,[241] and, perhaps most importantly, for anticompetitive market behavior.[242]

Weak incentives of large asset managers to invest in company-specific decision-making and the resulting practice of standard voting weaken concerns that common ownership creates anticompetitive problems. Interventions by large asset managers are mostly limited to promoting good governance standards along with the voting guidelines of the manager. Thus, it is unlikely that large asset managers will intervene to drive portfolio company performance to adopt an anticompetitive manner in general. But voting on specific proposal types that attract more attention from the largest asset managers, like takeovers or say-on-pay, may be a cause for concern. The common ownership argument thus needs a theory about the possible channels, if any, through which engagement practices of large fund managers can influence competitive behavior.

VI. CONCLUSION

It is time to rethink some common beliefs about institutional investors. This study offers evidence that shareholder voting engagement by large fund managers has been strengthening over the past years. As they have grown in importance as the world's largest shareholders, the biggest asset managers have come under increased pressure to strengthen shareholder engagement and take a stance on key corporate decisions. They are addressing this expectation in a slow, but growing, manner. We therefore need to reassess the prevailing view that large fund families avoid active engagement with companies in which they hold shares.

The growing engagement by large institutional investors is not necessarily all positive news. The size of the largest asset managers and market incentives impose significant limits on their shareholder engagement efforts. The largest fund families are too big to be actively engaging in all situations; they also face the competitive pressure of cutting fund management costs.

Large asset managers have responded by focusing shareholder engagement efforts on corporate governance and activities dealing with global social challenges. More recently, there has also been an increased attention towards climate risks. Importantly, however, this focus is often based on a standard framework of good governance, which is then imposed

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240. *See* Gregor Matvos & Michael Ostrovsky, *Cross-Ownership, Returns, and Voting in Mergers*, 89 J. FIN. ECON. 391, 399 (2008) (showing that cross-shareholdings in merging companies weaken incentives of mutual funds to vote against bad mergers in acquiring companies—the fund can cover losses at the acquiring company by a portion of merger gains through its holdings in the target).

241. *See* Miguel Antón et al., *Common Ownership, Competition, and Top Management Incentives* (ECGI Finance, Working Paper No. 511/2017), https://ssrn.com/abstract=2802332 [https://perma.cc/NE4E-RAYR].

242. *See, e.g.*, Einer Elhauge, *Horizontal Shareholding*, 129 HARV. L. REV. 1267 (2016).

on portfolio companies. What seems to be lacking is company-specific monitoring. Furthermore, attention to governance and social problems leaves aside corporate strategy, performance, and operational monitoring. Large fund managers, whether passively- or actively managed, have neither expertise, nor incentives for studying company-specific performance data and proposing possible solutions, for example, by voting individually on every board candidate. This is an important limitation that needs to be recognized during efforts in different parts of the world to build regulatory frameworks for effective shareholder stewardship. At minimum, imposing unrealistic engagement requirements on large institutional investors risks undermining their primary task of delivering returns for beneficiary investors. Moreover, if large institutional investors are expected to engage actively with portfolio companies on business matters, many—given the lack of expertise and resources—will be forced to apply the same standard approach across companies. This kind of regulatory efforts can do more harm than good and can lead to unintended consequences by creating inflated expectations from shareholder stewardship in situations where other regulatory means would be more appropriate. Also, impractical engagement requirements can generate additional costs for all parties involved, including ultimate investors saving for education or retirement.

This study also shows that the distinction between actively managed and passive index (tracker) funds or U.K. versus foreign funds matters less than expected, at least in the context of engagement through voting shares by the largest fund families. U.K.-based asset managers are likely to be more engaged only on compensation-related proposals. If there are differences in engagement practices of large asset managers, then these differences are manager-specific rather than based on broader shared characteristics of managers. Hence, concerns about "home bias" in engagement or "engagement passivity" of passive funds may be overstated. The negative effects of the increasing share of foreign institutional ownership at the expense of local investors or passive funds at the expense of actively managed funds may well not be as worrying as we predict.

Many interesting questions on shareholder engagement by large institutional investors remain unanswered. Some of those questions have been touched upon briefly in this study. In particular, future research will focus on identifying the factors that motivate large institutional investors to engage with specific portfolio companies on an individual basis, on interactions between shareholder activists and large institutional investors and more specifically on the effect of activist demands on voting decisions of large fund families, on private engagement efforts of large institutional investors through means other than voting, and on channels, if any, through which large institutional investors with common ownership can influence anticompetitive behavior in markets.