

August 22, 2018

Further to the Warren Bill, *The New Paradigm* and a Better Way

I've received a number of comments essentially raising the question, "If you are such a strong supporter of stakeholder corporate governance, how can you not favor Senator Warren's Bill?" As I said in both of my previous memos, [*Corporate Governance; Stakeholder Primacy; Federal Incorporation, August 15, 2018*](#), and [*Corporate Governance—The New Paradigm—A Better Way Than Federalization, August 17, 2018*](#), I reject federalization of all large corporations as too high a price to pay for stakeholder governance—particularly when it would do little to deter attacks by activist hedge funds. There are innumerable advantages to continued state incorporation and state corporate law that should not be sacrificed. My solution is the private sector solution advocated by the World Economic Forum, *The New Paradigm: A Roadmap for an Implicit Corporate Governance Partnership Between Corporations and Investors to Achieve Sustainable Long-Term Investment and Growth*. Growing support for *The New Paradigm*, as noted in my August 17 memo, would lead to it being *the* solution.

If a federal legislative solution is needed, I would prefer to promote a focus on the fundamental "Purpose" of the corporation (ESG, long-term sustainability and stakeholder interests) through legislation that does not effect state corporate law or state corporate governance jurisprudence. I would focus not on the corporation, but on the investor. The true power over corporate strategy, operations and management is in the investor and not the corporation. The vast majority of the S&P 500 corporations are majority-or near-majority owned by roughly 20 investors, with approximately 10% to 15% of the shares held by the three indexers, BlackRock, State Street and Vanguard. Almost all of the significant investors in the S&P 500 and other major public corporations are subject to filing and disclosure requirements pursuant to the Investment Company Act, the Investment Advisers Act and Section 13(f) [Form 13-F report] of the 1934 Exchange Act. Each of these Acts could be amended to require that each investor subject to any one of the Acts (1) disclose its policy with respect to Purpose, (2) explain each vote with respect to Purpose, and (3) explain any vote contrary to the recommendation of management—in effect a variation of the British "comply or explain" approach to governance and stewardship. By including stakeholder corporate governance in Purpose, this approach would also facilitate a corporation's ability to obtain approval of a charter amendment similar to the stakeholder provision in the Warren Bill and similar provisions in state stakeholder laws. While this approach would not eliminate attacks by active hedge funds, it would very substantially diminish their strength by reducing support from other investors. Importantly, it would not inhibit investors from engaging with corporations and seeking changes in strategy or management.

Martin Lipton

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