PROXY ACCESS FOR BOARD DIVERSITY

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ABSTRACT

Proxy access, a long debated governance measure, was directed at reducing shareholder costs in nominating directors. However, since it was first initiated, proxy access raised vigorous opposition, and more important, signficnat and wide skepticism that shareholders will ever use it to nominate directors.

This Article studies the first systemic implementation of proxy access and finds that while proxy access was rarely used to nominate directors, it was used indirectly—as a bargaining tool—to improve board diversity. Accordingly, the study finds that firms with a low number or low proportion of female directors, and firms with all-male boards, were significantly more likely to be targeted by the NYC Comptroller's proxy access proposals.

While promoting diversity wasn't one of the goals that proxy access was designed to achieve, the resulting effects might not be remote from those intended. Given that institutions are not likely to nominate directors, diversity might provide an alternative, pragmatic channel to increase board independence, monitoring and accountability.

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INTRODUCTION

Motivated by the lack of shareholder nominated directors in annual elections, proxy access was initially designed to provide shareholders with voice and representation on firms' boards.[1] Yet, in the several occasions a proxy access rule was proposed, it triggered significant opposition, and when the rule eventually passed, it was struck down shortly after by a federal court. Furthermore, even those who did not object proxy access, doubted that shareholders will ever use it.[2]

This study documents the first systematic and unpredicatable use of proxy access: as a bargaining tool to promote board diversity. In recent years, with the leadership of Scott M. Stringer, the NYC Comptroller, proxy access was implemented extensively via shareholder proposals. Following its implementation, as skeptics predicted, proxy access has been rarely used to nominate directors. However, the NYC Comptroller relied on proxy access to pressure companies to improve their board diversity. Thus, proxy access was used, albeit indirectly, to affect board composition.

On November 6, 2014, NYC Comptroller Stringer launched the Boardroom Accountability Project ("Project 1"): a wide submission of proxy access proposals to seventy-five companies.[3] The office's proxy access proposals were successful, both in receiving support from shareholder votes in a majority of the firms and in having most of the companies implementing proxy access terms to their bylaws.[4] During the proxy seasons of 2015 and 2016, the Comptroller Office (the "Office") submitted additional proxy access proposals, and by 2017 the Office proposals were implemented by a total of 141 firms.[5] Other shareholders followed the Comptroller's initiative and submitted proxy access

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[1] *See generally* Lucian A. Bebchuk & Scott Hirst, *Private Ordering and the Proxy Access Debate*, 65 BUS. LAW. 329 (2010).

[2] *See generally* Marcel Kahan & Edward Rock, *The Insignificance of Proxy Access*, 97 VA. L. REV. 1347 (2011) (explaining why hedge funds, index funds and other institutions are not likley to use proxy access).

[3] *See* Press Release, Scott M. Stringer, Comptroller, N.Y.C., Comptroller Stringer, NYC Pension Funds Launch National Campaign to Give Shareowners a True Voice in How Corporate Boards Are Elected (Nov. 6, 2014), https://comptroller.nyc.gov/newsroom/comptroller-stringer-nyc-pension-funds-launch-national-campaign-to-give-shareowners-a-true-voice-in-how-corporate-boards-are-elected/ [https://perma.cc/2VYU-WV8R] (describing Boardroom Accountability Project).

[4] *See Boardroom Accountability Project: Overview*, N.Y.C. COMPTROLLER, https://comptroller.nyc.gov/services/financial-matters/boardroom-accountability-project/overview/ [https://perma.cc/ZGW3-CLX9] (last visited Apr. 17, 2019) ("The 75 shareowner proposals produced very strong results. Two-thirds of the proposals that went to a vote received majority support. And the vast majority of engaged companies had enacted proxy access bylaws within the following year, including Chevron, Hasbro, Occidental Petroleum, Staples and Priceline.").

[5] *See Focus Companies, Boardroom Accountability Project*, N.Y.C. COMPTROLLER, https://comptroller.nyc.gov/services/financial-matters/boardroom-accountability-project/focus-companies/ [https://perma.cc/NM8K-JC97] (last visited Apr. 17, 2019) (listing 151 firms).

proposals widely. As a result, by 2019 almost five hundred firms, and more than two-thirds of those in the S&P 500, have added proxy access to their bylaws.[6] Professors Bhandari, Iliev, and Kalodimos found a positive market response to the launching of Project 1.[7] Yet, puzzilingly, firms that stood to benefit more from proxy access were not more likely to be targeted by the NYC Comptroller (nor by other shareholder proponents).[8] Probably, they hypothesized, shareholders anticipated that these firms were more likely to resist.[9]

However, Bhandari, Iliev, and Kalodimos focused on targeting in relation to proxy access needs; as it turns out, proxy access implementation was not the Comptroller's ultimate goal. Rather, on September 8, 2017, the Comptroller Office (the "Office") launched Project 2, which built on the success of Project 1, and which targeted the same 151 firms but focused on one main goal: improving board diversity. In particular, on September 6, 2018, the Office sent letters to the 151 companies that were previously targeted, asking them to disclose information with respect to their directors' race, gender and skills, and to engage with the Office on how they promote diversity.[10] Project 2 thus sheds light on the motivation that underlies Project 1.

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[6] Stephen T. Giove, Arielle L. Katzman & Daniel Yao, Shearman & Sterling LLP, *Proxy Access Proposals*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (Oct. 19, 2018), https://corpgov.law.harvard.edu/2018/10/19/proxy-access-proposals-2/ [https://perma.cc/C6B7-EA22] ("In total, well over 500 companies, and over two-thirds of the S&P 500, have adopted proxy access by-laws.").

[7] Tara Bhandari, Peter Iliev & Jonathan Kalodimos, Governance Changes Through Shareholder Initiatives: The Case of Proxy Access 13 (Jan. 17, 2017) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2635695 (studying market response to Project 1).

[8] *Id.* at 17 ("Overall, we do not find evidence that shareholder proponents target the firms expected to benefit most from proxy access...we find some evidence suggesting that proponents may be less likely to target some firms at which proxy access would be particularly valuable ").

[9] *Id.* The idea that shareholders may be targeting "easier" firms is not new. Professors Choi, Fisch, Kahan, and Rock reached a similar conclusion with respect to the implementation of majority voting ("MV") terms. Stephen J. Choi et al., *Does Majority Voting Improve Board Accountability?*, 83 U. CHI. L. REV. 1119, 1119 (2016) ("Rather than targeting the firms that, by their measures, are most in need of reform, reform advocates instead seem to have targeted the firms that were already the most responsive. These advocates may then have used the widespread adoption of majority voting to create pressure on the nonadopting firms to conform."). *But see* Michal Barzuza, *Unbundling the Dynamics of MV Implementation: Voluntary Versus Reluctant Adoption of MV as a Source of an Omitted-Variable Bias*, 83 U. CHI. L. REV. ONLINE 242, 250 (2017) (arguing that timing of MV implementation may have been affected by management resistance rather than by shareholder targeting).

[10] *See* Press Release, Scott M. Stringer, Comptroller, N.Y.C., Comptroller Stringer, NYC Pension Funds Launch National Boardroom Accountability Project Campaign — Version 2.0 (Sept. 8, 2017), https://comptroller.nyc.gov/newsroom/press-releases/comptroller-stringer-nyc-pension-funds-launch-national-boardroom-accountability-project-campaign-version-2-0/ [https://perma.cc/FUK3-52SS] ("As part of today's launch, Comptroller Stringer sent letters to the boards of 151 companies—92% of which have 'proxy access' and 80% of which are in the S&P 500—calling on them to publicly disclose the skills, race and gender of board

Furthermore, as this study shows, already in 2014 the Comptroller's targeting was focused on firms with poor diversity. The seventy-five firms targeted in 2014 were poor in diversity on several measures. To begin with, these firms had a significantly higher proportion of all-male boards. While less than 20% of firms in the Compustat database had no female directors, more than 30% of the firms Project 1 targeted had no female directors. Though there is no clear optimal number or proportion of female directors on boards, it is hard for boards to justify having none of them. Accordingly, in 2017, State Street Global Advisors announced that they would vote against boards with no female directors.[11] Similarly, California recently banned all-male boards for California firms.[12] Second, targeted firms faired worse than average in the absolute number of female directors on board, with an average number of female directors of about 1, compared to almost 1.5 in firms that were not targeted. The absolute number of female directors has shown to affect their influence on boards.[13] Accordingly, BlackRock announced recently that it would require a minimum of two female directors on each board they invest in.[14] Similarly, by the end of 2021, California law requires a minimum of at least two (and for some firms, three) female directors for all firms.[15] Finally, the low number of females on targeted firms' boards is not a result of their boards being small. Rather, targeted firms also have a lower proportion of females—an average that is slightly higher than 10% relative to 15% in firms that were not targeted. To summarize, on all measures

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members and to discuss their process for adding and replacing board members, known as the 'board refreshment' process, with the Comptroller's Office.").

[11] *See* Joann S. Lublin & Sarah Krouse, *Push for Women on Boards—State Street to Demand Change at Companies Lacking Female Directors*, WALL STREET J., Mar. 7, 2017, at B6 ("Index-fund giant State Street Global Advisors on Tuesday will begin pushing big companies to put more women on their boards, initially demanding change at those firms without any female directors."). Institutional Shareholder Services is considering a policy of voting against all-male boards. *See* Bradley Keoun & Anders Keitz, *All-Male Boards Could Face New Pressure from Shareholder Adviser ISS*, THESTREET (Sept. 19, 2018, 12:16 PM), https://www.thestreet.com/investing/all-male-boards-could-face-new-pressure-from-shareholder-adviser-iss-14716455 [https://perma.cc/4HWR-BGSA] ("Institutional Shareholder Services, a top adviser to investors on corporate elections, is discussing whether to recommend 'no' votes against directors of companies without any women on their boards.").

[12] CAL. CORP. CODE § 3.01.3 (West 2019) (requiring boards in California to have minimum of one female director by end of 2019 and minimum of two or three female directors, depending on size of board, by end of 2021).

[13] *See* Miriam Schwartz-Ziv, *Gender and Board Activeness: The Role of a Critical Mass*, 52 J. FIN. & QUANTITATIVE ANALYSIS 751, 753 (2017).

[14] *See* Sarah Krouse, *BlackRock: Companies Should Have at Least Two Female Directors*, WALL STREET J. (Feb. 2, 2018, 2:06 PM), https://www.wsj.com/articles/blackrock-companies-should-have-at-least-two-female-directors-1517598407 ("The world's largest money manager is for the first time stating publicly that companies in which it invests should have at least two female directors.").

[15] CAL. CORP. CODE § 3.01.3; Vanessa Fuhrmans, *California Sets Female Board Quota—State Is the First to Order Companies to Hire Women Directors or Face Penalties*, WALL STREET J., Oct. 1, 2018, at B1.

it is clear that the Comptroller targeted firms that exhibit poor board diversity. Thus, the Comptroller's targeting was not random nor focused on easy firms, rather, the Office targeted the problematic firms on the measure that it aims to improve—board diversity.

These findings have several implications. To begin with, at first glance it seems like proxy access is not being used to promote the goal it was initally created for—shareholder voice and acocuntability. Yet, while promoting diversity might seem to be an unrelated goal, the resulting effects might not be remote from those intended. Diversity is likely to increase board turnover, independence, and monitoring functions.[16] Given that institutions are not likely to nominate directors, pressuring firms to increase diversity might be the most pragmatic channell to higher board accountability. Second, since firms that need a governance change are frequently less likely to pursue it,[17] the findings that the Office targeted firms with poor diversity suggest that the mechanism of shareholder proposals could improve firms' self-selection in corporate governance.

The Article proceeds as follows. Section I.A describes Project 1 and research on the Project. Section I.B discusses Project 2. Part II analyzes targeted firms in terms of their diversity along the three dimensions discussed above. This Article then concludes.

I. NEW YORK CITY COMPTROLLER'S BOARD ACCOUNTABILITY PROJECTS

A. *Project 1: Proxy Access*

Proxy access, which provides a non-costly way for an investor to nominate candidates to the board, has been a subject of heated debate for more than a decade. More than once, the Securities and Exchange Commission ("SEC") considered passing a proxy access rule allowing large shareholders to add their director nominees to the firm's proxy materials. Then, after the 2008 crisis and with the leadership of Mary Schapiro, the SEC passed the proxy access rule, which the U.S. Court of Appeals for the D.C. Circuit shortly struck down.[18]

What the regulation did not do, however, shareholders did. Scott Stringer was nominated to the NYC Comptroller position in 2013.[19] The Office manages the pension funds of all NYC employees, totaling approximately $170 billion.[20] In

[16] *See generally* Renée B. Adams & Daniel Ferreira, *Women in the Boardroom and Their Impact on Governance and Performance*, 94 J. FIN. ECON. 291 (2009) (finding that female directors increase monitoring).

[17] *See* Barzuza, *supra* note 9, at 252.

[18] *See* Bus. Roundtable v. Sec. & Exch. Comm'n, 647 F.3d 1144, 1148 (D.C. Cir. 2011) (deciding that SEC acted arbitrarily and capriciously by not having sufficient evidence to support rule).

[19] *About Scott M. Stringer*, N.Y.C. COMPTROLLER, https://comptroller.nyc.gov/about/about-scott-m-stringer/ [https://perma.cc/PSC2-E6G7?type=image] (last visited Apr. 17, 2019).

[20] *See* Press Release, Scott M. Stringer, *supra* note 3 ("Comptroller Stringer serves as the

his position, the Comptroller can act as a shareholder, including submitting shareholder proposals to amend a firm's bylaws.[21] Shortly after he was elected, Comptroller Stringer launched Board Accountability Project 1. In a press release on November 6, 2014, the Comptroller announced that, in his capacity as a shareholder, he had filed seventy-five proxy access shareholder proposals.[22] The proposals, which will be subject to shareholder votes, "request a bylaw to give shareowners who meet a threshold of owning three percent of a company for three or more years the right to list their director candidates, representing up to 25 percent of the board, on a given company's ballot."[23]

Owners of the company, the Office argues, should be able to influence their board composition: "By giving substantial, long-term owners a meaningful say in electing the directors who oversee companies on our behalf, proxy access will help us to provide these hardworking men and women with a secure retirement . . . ."[24]

Project 1 was successful, both in receiving support from shareholder votes in a majority of the firms and in having most of the companies implement proxy access terms.[25] The Office did not stop there. During the proxy seasons of 2015 and 2016, the Office submitted additional proxy access proposals, which were implemented by a total of 151 firms.[26] In addition, other shareholders followed, submitting proxy access proposals to more firms. By now, more than five hundred listed firms and more than two-thirds of S&P 500 firms have added proxy access to their bylaws.[27]

Project 1, was supported by studies suggesting that proxy access would increase firm value.[28] Indeed, as Professors Becker, Bergstresser, and Subramanian found, firms that were likely to be affected by the rule exhibited a positive market response when the rule passed.[29] Furthermore, right after the rule was passed, it was challenged by the Business Roundtable and the Chamber of

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investment advisor to, and custodian and a trustee of, the New York City Pension Funds. The New York City Pension Funds are composed of the New York City Employees' Retirement System, Teachers' Retirement System, New York City Police Pension Fund, New York City Fire Department Pension Fund and the Board of Education Retirement System.").

21 *See, e.g.*, *Corporate Governance*, OFF. N.Y. ST. COMPTROLLER, https://www.osc.state.ny.us/pension/corporategovernance.htm [https://perma.cc/7Q7V-L2CD] (last visited Apr. 17, 2019).

22 Press Release, Scott M. Stringer, *supra* note 3.

23 *Id.*

24 *Id.*

25 *See Boardroom Accountability Project: Overview*, *supra* note 4.

26 *Id.*

27 *See* Giove, Katzman & Yao, *supra* note 6 ("In total, well over 500 companies, and over two-thirds of the S&P 500, have adopted proxy access by-laws.").

28 *See, e.g.*, Bo Becker, Daniel Bergstresser, & Guhan Subramanian, *Does Shareholder Proxy Access Improve Firm Value? Evidence from the Business Roundtable's Challenge*, 56 J.L. & ECON. 127, 157 (2013).

29 *Id.*

Commerce, to which the SEC, surprisingly, responded by placing the rule on stay until judicial resolution.[30] Both the challenge, and more importantly, the surprising decision to place the rule on stay, triggered a negative market response for firms that were likely to be affected by the rule.[31]

Project 1 and the proxy access shareholder proposals that followed were also utilized to research the value of proxy access for firms. Bhandari, Iliev, and Kalodimos found that market value of the 75 firms targeted increased in 53 basis points in response to the launching of project 1. The researchers then tested whether the market response to the SEC rule and the decision to place it on stay varied across firms. They found that some firms exhibited higher positive reactions to the passage of the rule, and accordingly, larger negative market stock reactions to the following stay. Thus, investors believed that some firms stood to benefit more than others from proxy access.[32] The authors then posed an interesting question: Which firms did shareholders (the NYC comptroller included) target? Did they target those firms that the market thought would benefit most from proxy access? This question was a building block in the larger research question of how private ordering works. It is commonly asserted that one size does not fit all in corporate governance, and the proxy access rule was criticized for applying one size to all firms.[33] Yet, there is little evidence that under private ordering, firms indeed choose their "right size."[34] To shed light on

[30] *See id.* at 128 ("In a move that surprised most observers, the SEC announced on October 4 that it would delay implementation of the new rule until the Business Roundtable's challenge was resolved."); *see also* Bus. Roundtable, Exchange Act Release No. 63,031, 99 SEC Docket 1689 (Oct. 4, 2010) (granting stay).

[31] *See* Becker, Bergstresser & Subramanian, *supra* note 28, at 129 ("Using a 1-day event window around October 4, 2010, we find that share prices of companies that would have been most vulnerable to the rule declined significantly compared to share prices of companies that would have been most insulated from the rule.").

[32] Bhandari, Iliev & Kalodimos, *supra* note 7, at 4.

[33] *See, e.g.*, Joseph A. Grundfest, *The SEC's Proposed Proxy Access Rules: Politics, Economics, and the Law*, 65 BUS. LAW. 361, 362 (2010) ("Because I (and you) do not know how to structure a proxy access regime that is suitably tailored to address the individual circumstances of the almost 12,000 publicly traded corporations in the United States, it makes sense to support a fully enabling approach to proxy access that allows every publicly traded corporation, easily and cheaply, to determine by majority vote the rules governing shareholder access to the corporate proxy."); David A. Katz & Laura M. McIntosh, *Populists' Wish Lists Offer Legislative Parade of Horribles*, LAW.COM (July 23, 2009, 12:00 AM), https://www.law.com/almID/1202432451430/ ("Delaware's private-ordering approach, which can be effected by carefully drafted company bylaws, enables companies and their shareholders to tailor proxy access to their own specific circumstances and keeps the issue of proxy access in the proper realm of state law.").

[34] *See* Barzuza, *supra* note 9, at 245 n.11 (showing theoretically and empirically that firms that could benefit most from governance constraints are least likely to adopt them); *cf.* Barry D. Baysinger & Henry N. Butler, *Race for the Bottom v. Climb to the Top: The ALI Project and Uniformity in Corporate Law*, 10 J. CORP. L. 431, 459 (1985) ("[C]orporate law will play a relatively more important role in those corporations in which market-oriented governance mechanisms are relatively less important or influential, and *vice versa*."); Frank H.

this question, Bhandari, Iliev, and Kalodimos checked which firms were more likely to be targeted by proxy access proposals.[35] They found that firms that, in the market's eyes, stood to benefit more from proxy access (as evidenced by a strong market price change for these firms around the relevant announcements) were not more likely to receive proxy access proposals.[36] The results were the same when they tested for all proxy access proposals and for those that the Office submitted.[37] The authors concluded that in submitting proxy access proposals, shareholders "seem to select firms without much regard to the variation in expected benefits, targeting firms where proxy access may be quite valuable as well as firms that the market does not expect to benefit from proxy access."[38]

The authors then took another step to inquire into the self-selection process: looking into management resistance to shareholder proxy access proposals. Managers may ask the SEC to exclude a shareholder proposal if they think it falls into one of the exceptions of Rule 14a-8(i), the shareholder proposal rule.[39]

Easterbrook & Daniel R. Fischel, *The Corporate Contract*, 89 COLUM. L. REV. 1416, 1426 (1989) ("The agreements that have arisen are wonderfully diverse, matching the diversity of economic activity that is carried on within corporations.").

[35] Bhandari, Iliev & Kalodimos, *supra* note 7, at 17.

[36] *Id.*

[37] *Id.* at 16 ("In unreported tests, we find similar results when separately considering the firms targeted by the NYC Comptroller and those targeted by other proponents separately.").

[38] *Id.* at 17.

[39] *See* 17 C.F.R. § 240.14a-8 (2018). For example, Whole Foods's management was seeking to exclude a proxy access proposal based on Rule 14a-8(i)(10), according to which a shareholder may not submit a shareholder proposal if there is already a conflicting management proposal for the same meeting. *Id.*; *see* Letter from Matt S. McNair, Special Counsel, Div. of Corp. Fin., Sec. & Exch. Comm'n, to Martin P. Dunn, Senior of Counsel, Morrison & Foerster LLP (Nov. 3 2016), https://www.sec.gov/divisions/corpfin/cf-noaction/14a-8/2016/jamesmcritchiewhole110316-14a8.pdf [https://perma.cc/YB9J-RJC6]. When the shareholder proxy access proposal was submitted to Whole Foods, the firm did not have a management proposal in place. Yet, Whole Foods's management sat to draft a new management proxy access proposal. Unlike the shareholder 3*3 proxy access proposal, management drafted a 9*5 proxy access proposal—that is, only a shareholder who held at least 9% of the company shares for at least five years could use the company materials to nominate a director to the board. Whole Foods's management requested and received a no-action letter from the SEC, stating the SEC would not act against management for excluding the proposal. *See* Whole Foods Market, Inc., SEC No-Action Letter, 2014 WL 5426272 (Dec. 1, 2014). Following the SEC no-action letter to Whole Foods, twenty-five additional companies, including Chipotle, submitted a similar request to the SEC based on newly drafted, more lenient management proxy access proposals. *See, e.g.*, Letter from Michael McGawn, Corp. Compliance Counsel, Chipotle Mexican Grill, Inc., to Office of Chief Counsel, Div. of Corp. Fin., Sec. & Exch. Comm'n (Jan. 2, 2015), http://www.sec.gov/divisions/corpfin/cf-noaction/14a-8/2015/comptrollernewyork010215-14a8-incoming.pdf [https://perma.cc/T62A-ZBV8] (informing SEC of Chipotle's intent to omit shareholder proposal and requesting no-action letter from SEC). Eventually, however, the SEC retracted the Whole Foods no-action letter, narrowing the applicability of the exception. *See* SEC Staff Legal Bulletin No. 14H (CF) (Oct. 22, 2015) https://www.sec.gov/interps/legal/cfslb14h.htm [https://perma.cc/5HSB-J3XV] (providing guidance on Rule 14a-8).

Looking at the type of firms whose managers fight shareholder proposals, the authors found that managers of those firms that stood to benefit most from proxy access were actually more likely to resist proxy access proposals.[40] Thus, they concluded, shareholders might have avoided the firms that need proxy access the most, since in these firms, managers are more likely to resist shareholder proposals.[41]

Professors Choi, Fisch, Kahan, and Rock studied the implementation of majority voting ("MV") terms and reached a similar conclusion with respect to shareholder targeting.[42] As the authors found, characteristics of firms that adopted MV terms varied with time. The firms that were quick to implement MV terms ("early adopters") have better corporate governance and higher shareholder support for their directors in previous elections than firms that implemented MV terms only after significant numbers of other firms did ("late adopters").[43] The authors interpreted these results to suggest that shareholders may have first targeted firms that were more likely to implement MV proposals, rather than fighting them:

> Differences between early and late adopters can have important implications for understanding the spread of corporate governance reforms and evaluating their effects on firms. Rather than targeting the firms that, by their measures, are most in need of reform, reform advocates instead seem to have targeted the firms that were already the most responsive. These advocates may then have used the widespread adoption of majority voting to create pressures on the nonadopting firms to conform.[44]

To sum, in studying Project 1, Bhandari, Iliev, and Kalodimos found that market response to project 1 was positive, while firm targeting was pretty random. Firms that were more likely to benefit from proxy access were not more

[40] Bhandari, Iliev & Kalodimos, *supra* note 7, at 22 ("Interestingly, we find that firms that chose to challenge the proposal in this relatively extreme way are exactly the firms that were expected to benefit more from mandatory proxy access or more from being targeted with a shareholder proposal for proxy access.").

[41] *Id.* at 17 ("Further, we find some evidence suggesting that proponents may be less likely to target some firms at which proxy access would be particularly valuable because of expected strong managerial resistance or other frictions that would make implementation challenging.").

[42] *See* Choi et al., *supra* note 9, at 1124.

[43] *See id.* at 1146 ("For late adopters, by contrast, the variables that were significant for [early adopters] and that we took as indicators of shareholder responsiveness—the prior record of ISS 'withhold' recommendations and the presence of a poison pill—are now insignificant. By contrast, the variable that may reflect reduced outside pressure to adopt majority voting or the ability to resist such pressure—positive abnormal returns—is significant, which is consistent with lower pressure or a higher ability to resist pressure making the adoption of majority voting less likely.").

[44] *Id.* at 1120. *But see* Barzuza, *supra* note 9, at 253-54 (arguing that timing of MV implementation may have been affected by management resistance rather than by shareholder targeting).

likely to be targeted. And they also found some evidence that firms which were likely to have the highest gains from proxy access were less likely to be targeted. Combining this res;ult with their other finding that firms whose managers were more likely to resist proxy access proposals were exactly those firms that stood to benefit the most from them, the authors suggest, like Choi, Fisch, Kahan, and Rock before them, that shareholders may avoid targeting the difficult firms (at least at the initial wave).

B. *Project 2: Diversity*

On September 8, 2017, Stringer announced the launching of Project 2. Two days earlier, on September 6, 2017, the Office sent letters to 151 companies, requiring them to better disclose information about their individual directors' gender, ethnicity, and qualifications.[45] The letter provided a desirable matrix for appropriate disclosure.[46] In addition, the letter required firms to engage in a dialogue with the Office regarding the "composition and refreshment of their boards."[47] The ultimate goal, as reflected in the announcement, was to increase these firms' board diversity:

> The next phase of the campaign will ratchet up the pressure on some of the biggest companies in the world to make their boards more diverse, independent, and climate-competent, so that they are in a position to deliver better long-term returns for investors.
>
> . . . At present, directors' race and gender is rarely — if ever — released publicly. If disclosed, it would increase transparency and accountability across the market — and push more boards to be diverse and independent.[48]

Project 2 relies on the achievements of its predecessor—Project 1—that was launched in 2014 and was focused on implementing proxy access at the same 151 firms.[49] Since proxy access provides a non-costly way for an investor to nominate candidates to the board, it provides a credible threat for board nominations in case the firms are not responsive to the current appeal for diversity.

The push for more diversified boards started prior to the launching of Project 2, both from the Office and from other investors. As a result of this pressure, the percentage of women on Russell 3000 boards increased from 16.5% to 18% in

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[45] Letter from Scott M. Stringer, N.Y.C. Comptroller, to Chairs of Nominating/Governance Comms., Portfolio Companies (Sept. 6, 2017) https://comptroller.nyc.gov/wp-content/uploads/2017/09/BAP-2.0-Letter-A.pdf [https://perma.cc/ZAM4-SD9Q].

[46] *Id.*

[47] Press Release, Scott M. Stringer, *supra* note 10; *see* Letter from Scott M. Stringer, *supra* note 45.

[48] Press Release, Scott M. Stringer, *supra* note 10.

[49] Project 1 resulted in proxy access implementation in 141 firms, that is, 92% of the targeted firms. *See Focus Companies*, *supra* note 5 (listing 141 firms).

2018.[50] More importantly, among newly appointed board members, more than a third are female directors, suggesting that their proportion on boards will continue to increase.[51] Finally, the proportion of firms with no female directors has been on a constant decline, and in 2018, finally fell below 20%.[52] Supporters advocated for diversity with evidence that diversity is associated with better firm performance.[53] One frequently cited argument for board diversity relies on female contribution to board independence—since female directors are not part of the "old boys' club," they are likely to exercise independent thinking and effective monitoring.[54]

Since the NYC Comptroller, in fact, has focused on board diversity from the beginning, when Project 1 was initiated, it is possible that rather than being

[50] *Equilar Gender Diversity Index: Q1 2018*, EQUILAR (May 9, 2018), https://www.equilar.com/reports/55-gender-diversity-index-q1-2018.html [https://perma.cc/KGE3-HR35].

[51] *Equilar Q3 2018 Gender Diversity Index*, EQUILAR (Dec. 12, 2018), https://www.equilar.com/reports/61-equilar-q3-2018-gender-diversity-index.html [https://perma.cc/Q9XU-5SYZ].

[52] *Id.* (stating percentages of women on boards).

[53] *See* Ronald P. O'Hanley, President & CEO, State Street Global Advisors, Distinguished Speaker Address at the Weinberg Center 2017 Corporate Governance Symposium: Long-Term Value Begins at the Board (Mar. 7, 2017), https://www.ssga.com/investment-topics/environmental-social-governance/2018/03/long-term-value-begins-at-the-board.pdf [https://perma.cc/B9MM-JUDM] ("[W]e have been especially focused on gender diversity for a simple reason: Because of the compelling research connecting greater gender diversity with better performance."). However, while diversity is associated with better performance in cross-section studies, *see, e.g.*, CATALYST, THE BOTTOM LINE: CORPORATE PERFORMANCE AND WOMEN'S REPRESENTATION ON BOARDS (2004-2008), at 1 (2011), other evidence is more mixed. *Cf.* Kenneth R. Ahern & Amy K. Dittmar, *The Changing of the Boards: The Impact on Firm Valuation of Mandated Female Board Representation*, 127 Q.J. ECON. 137, 141 (2012) (finding negative market response to Norway's mandated quota); Amalia R. Miller, *Women and Leadership*, *in* THE OXFORD HANDBOOK OF WOMEN AND THE ECONOMY 539, 545-49 (Susan L. Averett, Laura M. Argys & Saul D. Hoffman eds., 2018) (discussing effects of board gender diversity).

[54] Renée B. Adams & Daniel Ferreira, *Women in the Boardroom and Their Impact on Governance and Performance*, 94 J. FIN. ECON. 291, 293 (2009) (finding that female board members are better monitors); *see also* Renée B. Adams & Patricia Funk, *Beyond the Glass Ceiling: Does Gender Matter?*, 58 MGMT. SCI. 219, 219 (2011); Renée B. Adams, Benjamin E. Hermalin & Michael S. Weisbach, *The Role of Boards of Directors in Corporate Governance: A Conceptual Framework and Survey*, 48 J. ECON. LITERATURE 58, 63 (2010) (introducing review of literature on corporate boards); Daniel Ferreira, Commentary, *Board Diversity: Should We Trust Research to Inform Policy?*, 23 CORP. GOVERNANCE: AN INT'L REV. 108, 108 (2015) ("In this short piece, I summarize what we have learned from the board diversity literature, and what is useful (and not useful) for policy debates and design."); Renée B. Adams, Stephen Gray & John Nowland, Does Gender Matter in the Boardroom? Evidence from the Market Reaction to Mandatory New Director Announcements 4 (Nov. 2, 2011) (unpublished manuscript), http://ssrn.com/abstract=1953152 ("We are interested not only in how the market perceives the appointment of female directors on average but how the market perceives their appointment relative to men.").

random, the targeting of firms was related to board diversity. The following Part will address this issue.

II. BOARD ACCOUNTABILITY PROJECT 1: WHICH FIRMS WERE TARGETED

This Part inquires further into the targeting strategy of the NYC Comptroller's Board Accountability Project 1. While previous studies concluded this targeting to be random, this Part looks at another overlooked characteristic—board diversity—as a potential targeting criterion. In particular, I look into different measures for board diversity to determine whether the Comptroller was more likely to target firms with poor diversity.

A. *Targeted Firms: Financials and Governance*

Table 1 presents summary statistics of the financial characteristics of the sample of firms that were targeted by the Comptroller in the launching of Project 1. As shown in Table 1, firms that were targeted are significantly larger and have higher market value and revenues. Targeted firms also generally invest more in capital expenditures, research and development investments in particular, and are relatively low in cash.

Table 1. Summary Statistics—Financials.[55]

Features	Target Firms		Other Firms		All Firms		
	N	Mean	N	Mean	N	Mean	Difference
Size	68	9.5	4824	6.87	4,892	6.9	-2.63***
Cash	68	.11	4741	.206	4,824	.205	.091***
Market Value	68	9.48	5308	6.52	5376	6.56	-2.95***
Revenues	68	10819.98	4817	4347.77	4885	4437.7	-6472.2***
Leverage	67	.60	4819	.59	4886	.59	-.01
Payout	63	.051	4499	.049	4562	.049	-.002
ROA	68	.002	4817	-.103	4885	-.102	-.105
Investment	68	.053	4787	.034	4855	.034	-.019***
R&D Invest	27	.054	2526	.135	2553	.134	.081***

Table 2 presents governance characteristics as collected from Institutional Shareholder Services ("ISS").[56] As the table shows, targeted firms tend to have

[55] Table 1 presents financial factors of firms targeted by the Comptroller and firms that were not. Data is taken from Compustats. Firm size is measured by log(AT); market value by log(PRCC_F*CSHO); cash by CHE/AT; leverage by LT/AT; Payout by (DVP + DVC + PRSTKC)/IB; ROA by NI/AT; Investment by CAPX/AT; and R&D Investment by XRD/AT.

[56] ISS governance covers S&P 1500 companies. *See The Global Leader in Corporate Governance & Responsible Investment*, ISS, https://www.issgovernance.com/about/about-iss/ [https://perma.cc/VH7B-JV38] (last visited Apr. 17, 2019). There are 151 targeted companies are included in the S&P 1500 index.

good governance on several measures. To begin, firms that were not targeted by the Comptroller were significantly more likely to have a staggered board, which is an entrenching structure associated with lower firm value.[57] Second, firms that were targeted by the Comptroller were less likely to have a poison pill installed.[58] Third, targeted firms were significantly more likely to have a MV requirement for the election of directors at the annual meeting. Finally, almost none of the targeted firms had a dual class structure.

[57] *See* Lucian A. Bebchuk & Alma Cohen, *The Costs of Entrenched Boards*, 78 J. FIN. ECON. 409, 411 (2005) (finding that staggered boards are associated with lower firm value).

[58] The existence of a poison pill is less indicative, however, since unlike a staggered board, which requires a shareholder vote to be implemented, a poison pill can be implemented unilaterally by the board in less than twenty-four hours. *Id.* Accordingly, the difference is not statistically significant.

Table 2. Summary Statistics—Governance.[59]

	Target		No Target		All		Difference
	N	Mean	N	Mean	N	Mean	
Blank Check	75	.83	1435	.93	1510	.93	.1***
Staggered Board	75	.21	1435	.36	1510	.36	.15***
Poison Pill	75	.09	1435	.09	1510	.09	.004
Dual Class	75	.01	1435	.06	1510	.06	.05**
Cumulative Voting	75	0	1435	.05	1510	.05	.05***
Golden Parachute	75	.76	1435	.82	1510	.82	.06
Majority Voting	75	.72	1435	.53	1510	.54	-.19***
Limited Ability to Amend Charter	75	.85	1435	.97	1510	.97	.12***
Votes Required to Amend Charter	63	61.66	1390	63.03	1453	62.97	1.37
Limited Ability to Amend Bylaws	75	.83	1435	.88	1508	.88	.05
Votes Required to Amend Bylaws	51	61.98	988	61.69	1039	61.7	-.288
Votes Required to Call a Special Meeting	30	29.5	788	31.13	818	31.07	1.63
Votes Required to Act by Written Consent	41	76.41	854	77.08	895	77.05	.67

B. *Targeted Firms: Diversity*

Project 1's press release included a link to a list of the firms that were targeted. As explained above, in studying which firms were targeted, Bhandari, Iliev, and Kalodimos showed that firms who, in the eyes of the market, were most likely to benefit from proxy access, were neither more nor less likely to be targeted by the Comptroller.[60] Thus, previous literature focused on the proxy access side.

[59] Table 2 presents governance factors of the seventy-five firms that were targeted by the NYC Comptroller and the firms that were not. The data is taken from ISS Governance. *See The Global Leader in Corporate Governance & Responsible Investment*, *supra* note 56.

[60] Bhandari, Iliev & Kalodimos, *supra* note 7, at 17.

However, as revealed from Project 2, a main motivation for Project 1 was improving board diversity. Thus, it is possible that the Comptroller targeted firms in need of improved board diversity. In fact, the Comptroller's press release stated that proxy access proposals were submitted to firms with problematic practices with respect to the environment, board diversity, and executive pay.[61] The following Sections will inquire into different measures of board diversity of the targeted firms.

1. All-Male Boards

The first category reviewed is firms with all-male boards. In the recent shareholder activism to improve diversity, there is a consensus that this is the most problematic group of firms. To begin with, while there is no optimal number or proportion of female directors, it is hard to justify why having none of them would be optimal. Thus, an all-male board could be indicative of a related problem, such as a lack of independence. Accordingly, as previously noted, ISS, the largest proxy advisor announced that starting in 2020, they will recommend voting against boards with no female directors.[62] In October 2018, California passed a law that bans all-male boards.[63] On March 7, 2017, State Street Global Advisors announced that they would vote against boards of portfolio firms with all-male boards.[64] Figure 1 shows the proportion of firms among targeted and non-targeted firms with all-male boards. As Figure 1 shows, in the ISS population, the proportion of firms with all-male boards is less than 20%. However, this proportion among targeted firms is higher than 30%—more than one and a half times larger than the non-targeted firms. As shown in the regression in Table 3 below, the results are larger in magnitude after controling for market value.

[61] *See* Press Release, Scott M. Stringer, *supra* note 10. Ultimatley however, project 2 focused on board diversity which is the focus of this study. While this study focuses on the 75 firms that were targeted in 2014, initial results, as well as statements from the Office, suggest that board diversity remained a main tareting consideration in following years.

[62] *See* Keoun & Keitz, *supra* note 11.

[63] *See* CAL. CORP. CODE § 3.01.3 (West 2019).

[64] *See* Lublin & Krouse, *supra* note 11.

Figure 1. Proportion of Firms with "All-Male Boards."

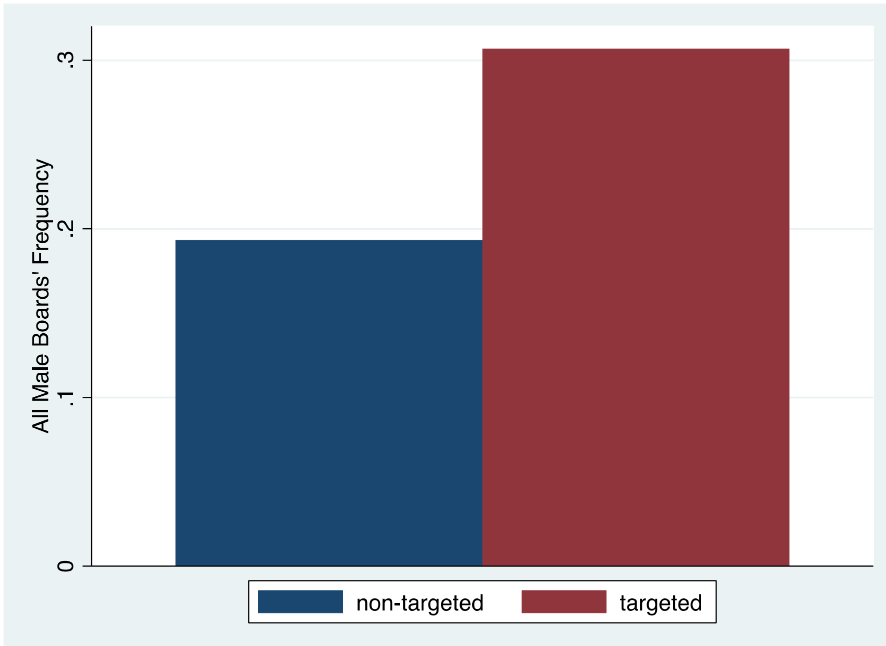


Table 3. All-Male Boards.
Dependent Variable: All-Male Boards

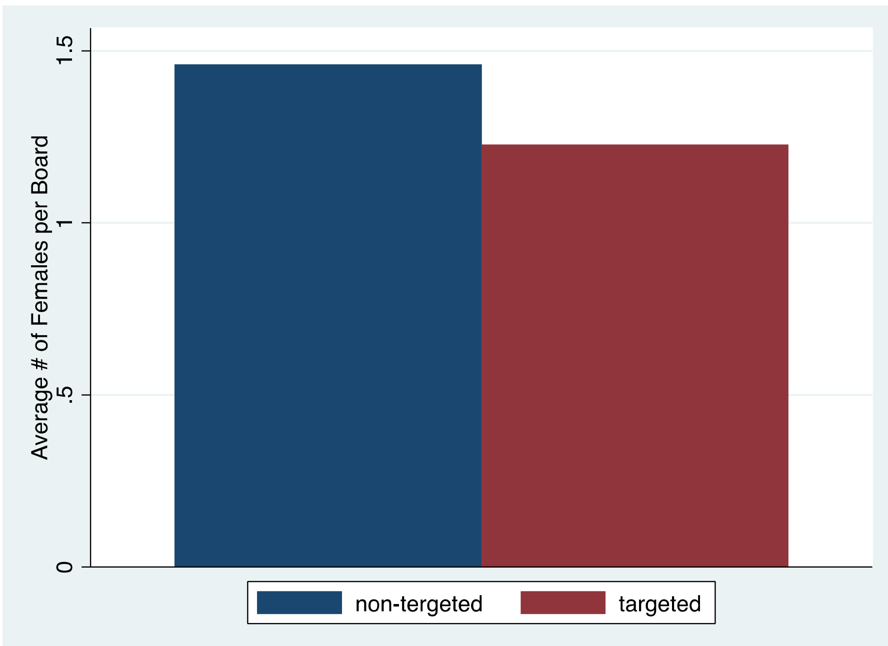
	(1)	(2)
VARIABLES	Model 1	Model 2
targetfirm	0.110**	0.208***
	(0.0516)	(0.0536)
marv		-0.0876***
		(0.00601)
Constant	0.186***	0.913***
	(0.00946)	(0.0561)
Observations	1,775	1,393
R-squared	0.003	0.109

Robust standard errors in parentheses
*** p<0.01, ** p<0.05, * p<0.1

2. Average Number of Female Directors on Board

While all-male boards represent an extreme case, the total number of female directors is also important. For example, recent research finds that in boards with a minimum of three female directors, the female directors are significantly more influential and effective.[65] The number of female directors is sufficiently important that California mandated a certain minimum number that different boards must meet. Senate Bill 826, which the California Governor signed into law in October 2018, requires all firms headquartered in the state to have female directors on their boards by the end of 2019.[66] By the end of 2021, the minimum mandate increases to two female directors for firms with five board members, and three female directors for firms with six directors or more.[67] And, in February 2018, BlackRock announced that it would vote against boards of portfolio firms with less than two female board members.[68] Also on this measure, targeted firms fair worse than average. As Figure 2 demonstrates, while the average number of female directors among all firms is almost 1.5, among targeted firms it is close to 1. As shown in the regression in Table 4 below, the results remain significant, and grow in magnitude, after controlling for market value .

Figure 2. Average Number of Female Directors per Board.



[65] *See* Schwartz-Ziv, *supra* note 13, at 753.

[66] S.B. 826, 2018 Leg., 2017-2018 Sess. (Cal. 2018); *see also* CAL. CORP. CODE § 3.01.3; Fuhrmans, *supra* note 15.

[67] *See* CAL. CORP. CODE § 3.01.3.

[68] *See* Krouse, *supra* note 14.

Table 4. Average Number of Females Per Board.
Dependent Variable: Number of Female Directors

VARIABLES	(1) Model 1	(2) Model 2
targetfirm	-0.257**	-0.605***
	(0.128)	(0.146)
marv		0.315***
		(0.0178)
Constant	1.479***	-1.132***
	(0.0263)	(0.147)
Observations	1,775	1,393
R-squared	0.002	0.186

Robust standard errors in parentheses
*** p<0.01, ** p<0.05, * p<0.1

3. Proportion of Female Directors

Finally, I also look at the proportion of female directors. In large boards there are more reasons to have a larger number of directors. Accordingly, California's mandated quota demands different minimums for different-size boards. On this measure also, targeted firms fair worse—with an average that is slightly higher than 10% relative to 15% in non-targeted firms. As shown in the regression in Table 5 below, also with respect to this measure the results are larger in magnitude after controlling for market value.

Figure 3. Proportion of Female Directors.

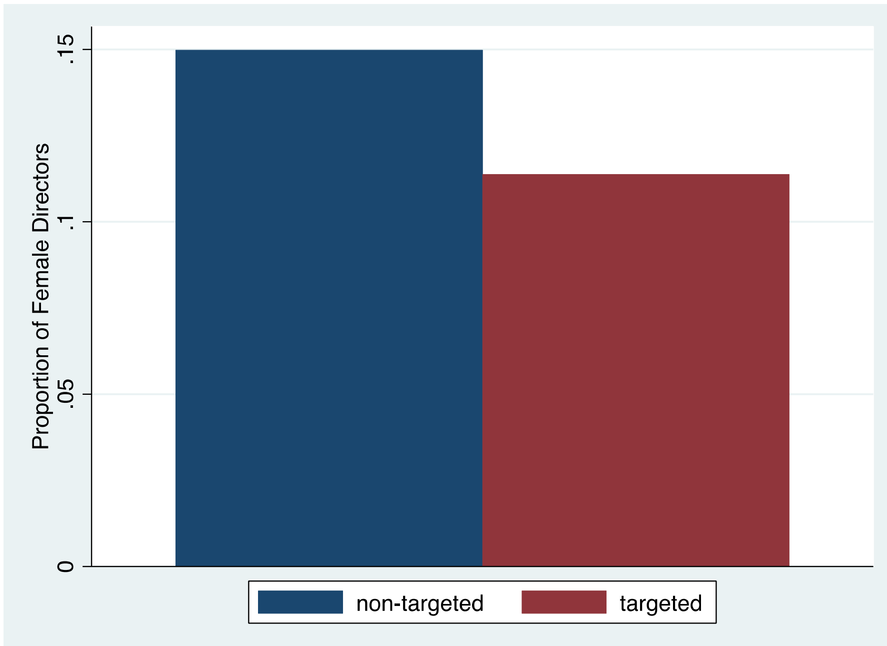


Table 5. Proportion of Female Directors.
Dependent Variable: Proportion of Female Directors

VARIABLES	(1) Model 1	(2) Model 2
targetfirm	-0.0347***	-0.0588***
	(0.0117)	(0.0133)
marv		0.0210***
		(0.00167)
Constant	0.150***	-0.0232
	(0.00250)	(0.0145)
Observations	1,775	1,393
R-squared	0.005	0.093

Robust standard errors in parentheses
*** p<0.01, ** p<0.05, * p<0.1

4. The Likelihood of Being Targeted

Finally, the regression in Table 6 shows the effect of the three measures on the likelihood of being targeted. As the regression demonstrates, both the number and proportion of female board members are negative and statistically significant. Also consistent with these conclusions, having an all-male board signficantly increases the likelihood of being targeted.

Table 6. The Likelihood of Being Targeted.
Dependent Variable: Being Targeted

VARIABLES	(1) Model 1	(2) Model 2	(3) Model 3
All Male Boards	0.0658*** (0.0178)		
Market Value	0.0346*** (0.00473)	0.0375*** (0.00527)	0.0343*** (0.00471)
#Female Directors		-0.0277*** (0.00741)	
Female Proportion			-0.264*** (0.0669)
Constant	-0.250*** (0.0368)	-0.221*** (0.0330)	-0.196*** (0.0302)
Observations	1,393	1,393	1,393
R-squared	0.055	0.058	0.057

Robust standard errors in parentheses
*** p<0.01, ** p<0.05, * p<0.1

CONCLUSION

This Article documents the first systematic use of proxy access. It finds that while proxy access has not been used to nominate directors directly, it functions as a bargaining tool to improve board diversity. As this Article finds, the NYC Comptroller targeted firms that were poor on diversity. Targeted firms had a higher proportion of boards with no female directors, a low average number of females per board, and a low proportion of female directors. The office then followed up with project 2, that was focused on improving boards' diversity.

The pressure to increase diversity is likely to increase boards' turnover rate, independence level, and monitoring functions. Thus, while promoting diversity might seem to be an unrelated goal, this use of proxy access is not remote from the initial goals it was created for. These results have implications for empirical research and for corporate law policy.