Blacklisted 'woke' firms like BlackRock and State Street still have a lock on AUM in oil states like Oklahoma; anti-ESG politicians underestimated the fierce independence of state money managers and Republican lawmakers who back them

Oklahoma public pension fund revolts against state Treasurer and refuses to divest ESG funds in protest against mixing politics with fiduciary duties -- roughly a repeat of the ESG revolt in reverse.

Author **Oisin Breen** November 1, 2023 at 9:50 PM

Alyssa Stankiewicz: ESG funds are not the only ones employing different

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> ***Brooke's Note: Our heads spun when BlackRock was considered too squishy for Texas and other oil states. Now we are surprised again. The blacklists in some cases are simply failing to work. Part of the problem is that the anti-ESG movement fell into the same trap as ESG people who they accused of being too arbitrary. But the bigger problem apparently was something an RIA could appreciate. The money managers were simply – blacklists be damned – unwilling to manage billions of retirement assets based on a political edict. It's not necessarily a reprieve for ESG but it's safe to say, score one for BlackRock. Oisín delves in.***

Republican-led states that led a backlash against ESG investments last year that hit BlackRock and other fund firms are now facing a backlash of their own, largely led by… Republicans.

Texas, Arkansas, Kentucky, Iowa, Oklahoma and West Virginia, among others, enacted so-called "blacklist" mandates, prohibiting government entities – largely public pensions – from investing in funds managed by select proponents of environmental, social and governance (ESG) funds.

Supporters of the ban argue ESG investing puts policy and social objectives ahead of financial objectives and, in some cases, impacts local industries, like oil and gas companies.

Andrew Besheer: The real pushback will come from [money managers].

Professional money managers have begun rebelling against the restrictions because they remove as much – maybe more – investing freedom and actually cost more to follow.

Because anti-woke states are actively screening out investment firms for failing to meet particular political requirements – the basic ESG playbook – they are now getting hammered for precisely what they intended to avoid – putting politics above being a fiduciary.

"ESG funds are not the only ones employing different strategies to achieve change in line with their view of what's in the best interest of investors," says Alyssa Stankiewicz, Morningstar's associate director for sustainability research, via email.

Pushing back

The latest uproar is playing out in Oklahoma; Republican lawmakers and state pension board members are locking arms in revolt against a Republican-sponsored 'anti-woke' investment law enacted last year.

Beginning earlier this year, OPERS schooled the state's politicians at a series of hearings, explaining BlackRock and other 'woke' money managers check the most fiduciary boxes.

Then, after deeming the response to its request for proposals (RFP) of alternative investment options unsatisfactory, OPERS, which administers an $11.1 billion pension pot, took the nuclear option of applying a 'fiduciary exemption' to ignore the state's blacklist.

Kris Mayes: It is not the place of government to tell corporations ... they cannot invest.

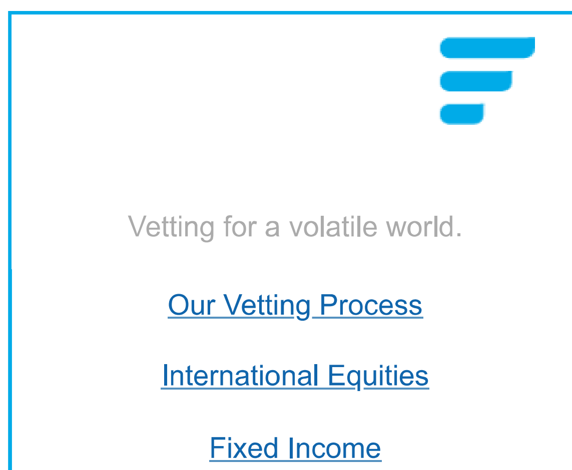
"Is there anything juicier than watching someone hoist by their own petard? I think not," says Andrew Besheer, director of wealth management at Boston consultancy Datos Insights, via email.

"Professional money managers should have the freedom to make the best decisions they can for fiduciary clients," he continues.

"There have been periods where ESG investments have outperformed, and others where they haven't. Let investment managers make the decisions. Don't handcuff them," he adds. See: Texas pronounces BlackRock guilty of pandering to sustainable investing interests.

The Oklahoma uproar is all the more surprising because Gov. Kevin Stitt is a Republican, and the party holds supermajorities in both chambers of the state legislature.

"We've seen that in action in Oklahoma and Kentucky and other states where the [decision makers] have pushed back against mandating out asset managers and limiting their ability to make objective investment decisions," Besheer concludes.



Raising questions

The biggest targets of anti-ESG laws -- BlackRock and State Street Global Advisors (SSGA) – still have discretion over $7 billion of Oklahoma's defined benefit assets and both swing big sticks in the industry.

BlackRock manages around $9 trillion, or roughly 810 times the assets managed by Oklahoma's pension system, and SSGA manages around $3.5 trillion, or roughly 315 times that amount.

Dave Rader: 'There's confusion in this bill.'

The sheer size of both firms means they can blow most vendors away on pricing and still keep their own margins ticking along. See: Suddenly, 'Big Three' have the assets and the power of ESG mandates.

"It's really hard to ignore the largest [shops] out there when you're the fiduciary responsible for the pensions of thousands of citizens of a given state," says Besheer.

The Oklahoma Public Employees Retirement System (OPERS) can also still contract with the four other blacklisted firms, should it choose to do so, namely Wells Fargo & Co., JP Morgan Chase and Co., Bank of America and Climate First Bank.

"I don't find it particularly surprising Oklahoma is questioning how to implement or tweak its blacklist, and its treasurer is getting grilled," says Matt Cole, CEO of New York City 'anti-ESG' asset manager Strive Asset Management, via email.

"It's perfectly valid … to debate the cost of divesting from these asset managers, debate the benefits, and weigh them," he says.

A number of anti-ESG fund managers like Strive are also in the fight, bidding to replace companies like BlackRock that run ESG-funds. See: Vivek Ramaswamy sells anti-ESG to RIAs to nab quick $1 billion of AUM, but it's all 'Kabuki theater,' analyst says.

About face

Perhaps not surprisingly, pension fund managers are leading the backlash against the backlash.

"Harried chief investment officers feel like their freedom to operate in a way they deem as meeting

Besheer explains.

“The real pushback will come from [them] as they try and take back control of the decision making on who they’re going to place mandates with.

“That [doesn't] mean they will necessarily be placing more ESG mandates. This is simply about retaking the power,” he adds.

Todd Russ: There's a real hard conversation going on about what's reasonable.

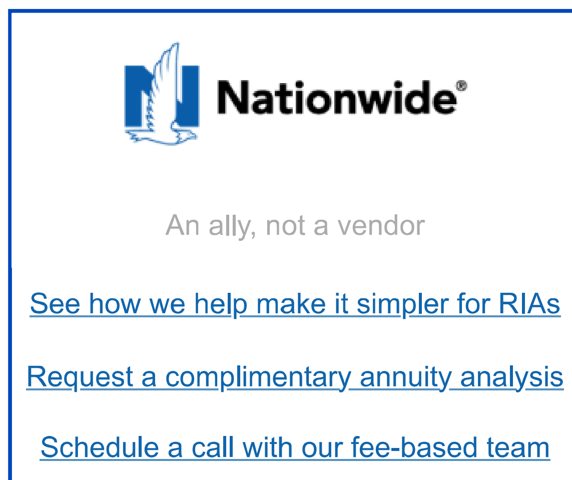
The same battle is playing out in other states as both attitudes and politics shift.

Arizona was one of 19 states whose attorneys general penned an open letter in 2022, blasting BlackRock CEO Larry Fink, for refusing to hold the company in its lane, and “circumvent[ing] the best possible return[s]."

Yet, following the election of Democrat Kris Mayes as Arizona's new attorney general in late 2022, the state did an about-face on ESG.

“It is not the place of government to tell corporations and their investors that they cannot invest in sustainable technologies and practices or improve their governance processes," Mayes said, in a statement, Feb. 13.

Blacklist battle



Anti-ESG lawmakers are far from conceding the issue. Significantly, they are waving red flags over the impact on home-grown businesses – even if they are giant corporations.

At issue in Oklahoma is the Oklahoma Energy Discrimination Elimination Act. The law, enacted in 2022, has caused confusion and driven a wedge between state Treasurer Todd Russ and some board members and staff for the state's pension system, according to Oklahoma Watch, a nonprofit publication that specializes in investigative journalism.

Ari Sonneberg: [Some funds] are blacklisting Oklahoma-based oil and gas industry companies from their funds as a result of ESG considerations.

The state pension board voted 9-1 in August to exempt BlackRock from the law so it wouldn't have to dump $6 billion in pension assets managed by the company.

Pension staff said divesting BlackRock's holdings – purely to sate political demand – could cost the state as much as $10 million, according to the muckraking website.

The Oklahoma Council of Public Affairs, a conservative private think-tank, countered in an Oct 30 blog post that the blacklist is "having a small but positive impact on Oklahoma's economy."

But Republican state Sen. Chuck Hall said the blacklist makes it harder to raise municipal funds.

"There's confusion in this bill ... [and] we have the treasurer not agreeing with the pension managers and the boards," said Dave Rader, another state Senate Republican, during an Oct. 11, state senate hearing.

Senators also stated the blacklist – one of six red state boycotts implemented to varying degrees of success – is effectively unworkable or in need of a serious rewrite. See: ESG firms may get Okie OK.

Hard conversation

Russ, a pension board member and the lone holdout in the board's 9-1 vote, fired off a 17-page letter, alleging the pension board's action was "in opposition to the letter and spirit" of EDEA.

"The state of Oklahoma should not be investing money with companies that boycott … our own industries," he wrote in the Aug. 15 missive.

He also wrote that five of the eight large funds presently managed by BlackRock and SSGA have "near-zero switching costs" and that some competitors were offering prices $200,000 below BlackRock's cost.

"There's a real hard conversation going on about what's reasonable and how do we carry out the

an October hearing, according to Pensions & Investments magazine.
In a recent client letter, Wagner Law Group recommended the fiduciary “best practice” for retirement plan managers is to avoid ESG funds with non-financial primary objectives. Wagner labels such funds “problematic” for potentially sacrificing returns to meet an “impact objective."

“The stated motive for ODEA was to prevent the state from entering into contracts or investing with asset managers that are blacklisting Oklahoma-based oil and gas industry companies from their funds as a result of ESG considerations," says Ari Sonneberg, partner at the Wagner Law Group in Boston, via email.

“Even if it were true, Oklahoma might lose money in the near-term from divesting … [it] most certainly has a pecuniary interest in avoiding contracting and investing with companies that specifically blacklist Oklahoma-based businesses crucial to the state’s economy," he explains.

Dublin-native and Edinburgh-based Oisín Breen has spent seven years writing about finance, including five whirlwind years diving into the advisor world for RIABiz. A widely published and well regarded poet with two full collections under his belt, Breen is also an academic in English Literature with a deep fondness for his Scottish rabbit, Hessell. @Breen

Brooke Southall and Keith Girard contributed to the editing of this article.

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August 8, 2022 at 9:57 PM

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Suddenly Vanguard, BlackRock, State Street not only

make them a growing threat to shareholder democracy, critics say

A handful of super-charged fund managers control $34 trillion of assets and most of the ESG inflows, giving them 'carte blanche' to shape corporate policies.

Author **Oisin Breen** July 28, 2021 at 6:35 PM

John Rekenthaler: I am concerned about the amount of power the [biggest fund managers] wield, even if they wield that power well.

The embrace of ESG by an ETF power bloc of BlackRock, Vanguard Group, Fidelity Investments, Capital Group and State Street may augur a dark future where they hold the power to sway shareholder votes, according to RIAs, fund trackers, hedge funds and ESG advocates alike.

The rising chorus of critics say the elite exchange-traded-fund producers from Boston, New York, Philly and Los Angeles pose a rising threat to "shareholder democracy" -- albeit because the power has been thrust upon them.

Vincent Deluard: Shareholder democracy will not work as intended.

Investors and advisors have not only funneled their assets to the

giving *carte blanche* to deploy Environmental, Social and Governance (ESG) filters that would freeze out scores of companies.
But now American investors need to be careful about what they asked for, says Vincent Deluard, global macro strategist at New York City brokerage, StoneX.

"It doesn't matter whether it's Vanguard, BlackRock, Fidelity or the California Public Employees Retirement System; if two or three investors control 20% to 40% of the vote of every US company, shareholder democracy will not work as intended," he says, via email.

Between them, the big five manage $27.7 trillion in client assets globally, and administer over $34 trillion. In US equities alone, the grouping manages $15.07 trillion, or 61.89% of all assets held in US equity funds, according to Morningstar Direct.

Kingmakers

Indeed, one veteran Morningstar voice is troubled by the potential implications of placing so much power in the hands of so few, warning that their growing stranglehold on US equity funds will hand them a de-facto veto on all major corporate decisions by 2040.

"I'm concerned about the amount of power they wield, even if they wield that power well. If the sales trend over the past decade continues, then the 35% [cumulative voting] position will occur circa 2040," says Morningstar vice president for research, John Rekenthaler. via email.

"[Then they] truly would be kingmakers. Unless a proposal is so wildly unpopular as not to attract even a 15% vote from remaining shareholders, [they] could ensure the initiative passes."

"Conversely ... they could effectively shut down almost any activist activities," he adds, in a June 7 Op-ed.

Peter Krull: 'I simply don't trust them, or their motives.'

BlackRock and SSGA signaled a willingness to comment on these raised concerns but ultimately declined. Vanguard did not respond to a request for comment.

Rekenthaler says what triggered the alarm was Vanguard, BlackRock and SSGA's early June decision to combine forces to topple a quarter of the Exxon Mobil board.

The trio acted in support of a bid by tiny activist ETF vendor Engine No. 1 to stack the oil giant's board with pro-ESG candidates.

Much of the ESG movement opposes fossil fuel companies that seek to maximize profits based on selling polluting products to customers who pump tons of carbon dioxide-- a greenhouse gas-- into the atmosphere.

"This topic wasn't on my radar when the biggest fund managers ... endorsed the status quo. I paid greater attention after the ExxonMobil vote," says Rekenthaler.

"The issue for me isn't how [this] big three voted, but my belated realization of what power they now possess," he explains.

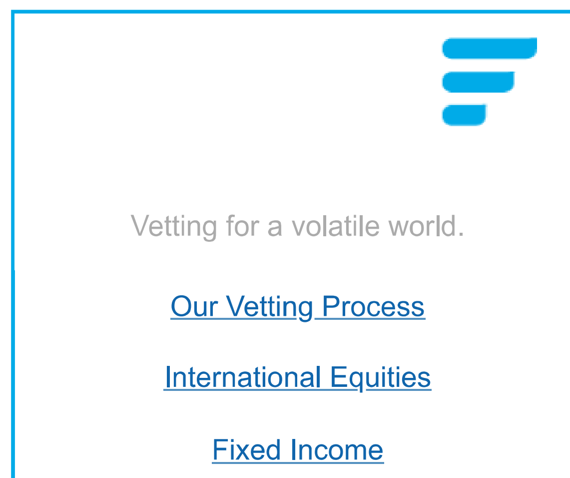
That's no outlier, reports The Telegraph.

"BlackRock voted against 255 board directors at companies including Warren Buffett’s Berkshire Hathaway and oil and gas firm Exxon Mobil in the year to June 30, because they failed to act on climate issues," it wrote. "This is more than four times the 55 executives it rejected the year before."

Double edged sword

ESG advocates are also wary of that the power of big asset managers. They see it as a double-edged sword that, indeed, cuts both ways.

"I personally don't want Blackrock, Vanguard and SSGA to be the ultimate arbiters of proxy proposals, because I simply don't trust them or their motives," says Peter Krull, CEO of Asheville, N.C., RIA, Earth Equity Advisors, with $145 million of AUM.



"Worst case scenario is that the big three suddenly turn their backs on any sort of positive ESG voting," he adds, via email.

Indeed, even today the record of major fund managers in proxy votes shows that more often than not they effectively block pro-ESG initiatives, according to a Morningstar report.

In 2020, BlackRock funds, for instance, voted in favor of just 16% of ESG proposals put forward, and

Overall, Vanguard manages $7.9 trillion globally, BlackRock $9.5 trillion, SSGA $3.9 trillion and Capital Group $2.3 trillion. Fidelity administers $10.4 trillion and manages $4.1 trillion.

In US equity funds alone, Vanguard manages $6.8 trillion, BlackRock $2.65 trillion, Fidelity $2.4 trillion, American Funds $2.2 trillion and SSGA $970 billion, according to Morningstar Direct.

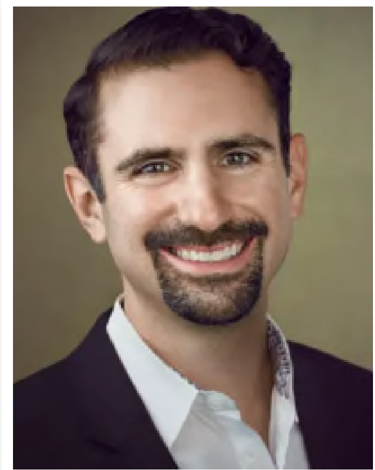
Inevitable outcome

The rise of a corporate control of millions of proxy votes on behalf of investors in pursuit of their own agendas was inevitable, according to Joshua Levin, co-founder and chief strategy officer of the now JP Morgan-owned direct indexer OpenInvest.

"The problem is not passive managers, active managers, or consumers. The problem is a paper-based legacy system that favored corporatism.

"This system was already heavily consolidated in favor of corporate managers [and] it is largely paid for by corporations ... [who] have enjoyed nearly impenetrable board voting power as a result," he says, via email.

"What's happening now is that indexing consolidation is shifting some of that power from corporations to asset managers, and people are concerned. But I expect that index manager proxy power is a temporary way point," he adds. See: As part of sale to J.P. Morgan, OpenInvest is orphaning RIA clients.



Joshua Levin: There are significant concerns around principal engagement, conflicts of interest, and monumental voting blocs

Waypoint, or not, a raft of industry figures now assert that growing pressure to back 'ethical' shareholder resolutions in proxy votes has handed fund giants a license to use their increasingly decisive voting powers as they see fit, albeit wrapped in an ESG mandate.

Significant concerns

In recent years, activist groups including the Sierra Club have lobbied hard to compel asset managers to support shareholder resolutions favoring the aims of the surging "ethical" ESG movement. See: Sierra Club slams Larry Fink's 'lip-service' to green future.

Fund vendors, as a result, have begun to highlight their ESG credentials. Indeed, BlackRock CEO Larry Fink recently described what he saw as a "tectonic shift"

ESG lobbyists also have surging ESG asset growth to boost their ambitions.

In the last year, the value of domestic ESG fund investments more than doubled, up 123% year-over-year, to $266 billion, as of March, 2021, according to Morningstar Direct.

Indeed, since March, US ESG fund assets jumped another 14%, to $304 billion, including $17.5 billion of net inflows, according to the latest July Morningstar report.

An estimated 33% of the roughly $51.4 trillion in domestic managed assets are also held in sustainable investments, CNBC reports.

RIAs have also come under pressure from ESG lobbyists to take a more active role in convincing their clients to invest in ESG funds. See: RIAs are just not that into ESG investing -- at their peril, a new study says.

For years, however, the shoe was on the other foot.

"There are significant concerns around principal engagement, conflicts of interest and monumental voting blocs that historically defaulted to management positions," he explains.

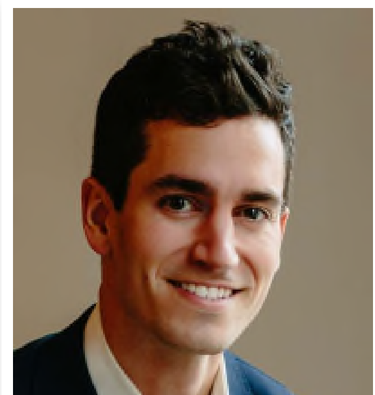
Yet the more asset managers get proactive about pushing an agenda during corporate proxy votes, the more corporate decision-making becomes contingent on the caprice of a small group, according to Levin.

"Rekenthaler [was] right to call out potentially concerning levels of control over shareholder voting from the big index managers," he says.

Threat to free enterprise

All of the big five fund companies have backed pro-ESG shareholder resolutions in recent years.

In June 2020, Vanguard backed resolutions to cut carbon emissions at United Parcel Service, J.B. Hunt Transport Services and oil driller Ovintiv. Later in the year, BlackRock pledged to back an increasing number of ESG resolutions in corporate voting, and



Backing ESG resolutions is increasingly good for business, too, as ESG funds grow in popularity. It also contributes to a company's corporate social responsibility agenda.

Yet Engine No. 1's plucky campaign to put four of its own candidates on Exxon Mobil's board has focused several industry

wearing ETF makers could pose a threat to the free enterprise system.

Michael O'Leary: [Investors] can't be expected to cast ten thousand ballots themselves

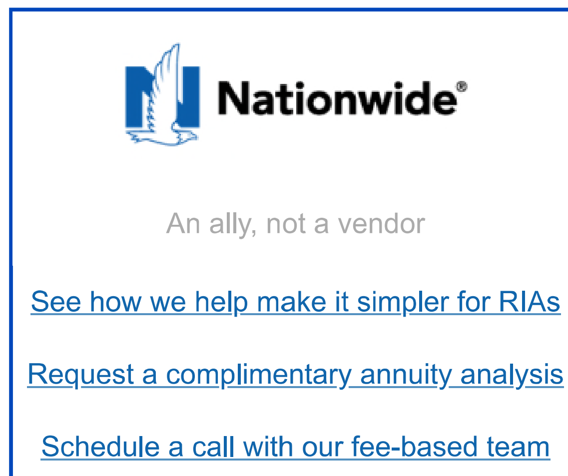
The mouse that roared

Founded last year by a consortium of private equity investors--Goldman Sachs, BlackRock, and Bain Capital alumni--Engine No. 1, began targeting Exxon in Dec. 2020.

Three of its four candidates now sit on the Exxon board, despite the fact that Exxon outspent its campaign by a factor of ten. Indeed, Engine No. 1 only achieved its goal as a result of Vanguard, BlackRock and SSGA's decision to back the company's bid as a bloc.

In doing so, the three firms demonstrated that they hold the balance of power, even at a company as individually powerful as Exxon, which has a market capitalization of $243.75 billion.

Today, Vanguard, BlackRock and SSGA, alone, control a minimum 43.47% of the domestic fund industry’s holdings in US-listed companies, and they have posted the highest net new US equity ETF and mutual fund sales, according to Morningstar Direct.



Engine No.1 launched its first ETF (VOTE), Jun. 22. VOTE tracks the Morningstar US Large Cap index, and the company has pledged to push ESG resolutions across the companies it invests in.

New York City robo-advisor Betterment also just rebalanced its ESG portfolios to include VOTE.

Fifty years out of date

The concentration of corporate voting power among fund vendors hinges specifically on the fact that ETFs and mutual funds disintermediate investors from the stock they hold, leaving the job of buying and selling to expert traders.

Now, as a result of the massive surge in popularity of "set-and-forget" index ETFs in the wake of the last financial crisis, the largest asset managers are responsible for the proxy votes of millions of

It's a problem that needs to be solved, says Michael O'Leary, managing director at Engine No. 1, via email.

"Disintermediated voting is a great solution for the way people invested fifty years ago before the advent of index investing. Today, many investors hold hundreds or thousands of stocks through index funds. They can't be expected to cast ten thousand ballots," he explains.

The system worked, when no one paid attention, adds Levin.

"Proxy voting has traditionally been a perfunctory backwater, where large asset managers are mainly concerned with fiduciary compliance and operational ease. The common logic has been to default to management positions for those reasons, and no one looked askance," he explains.

System flaw

The systems built to manage proxy voting also weren't designed to handle the scale of today's fund industry, or the complexity of ESG, says Deluard

This leaves asset managers and the outsourcers they depend on underfunded and understaffed, he explains.

"Practically, BlackRock and Vanguard do not have the staff or the expertise to cover all the votes they are a part of, [so they also] rely on equally understaffed and unaccountable proxy voting firms," he continues.

"[Proxy advisors] focus on 'low-cost/low-value voting', which doesn't require much research.

"They typically vote for independent directors, splitting the roles of CEO and board chairman, and against poison pills and multiple-class share structure[s] ... [which] may reduce governance risk but is unlikely to move the [ESG] needle," he says.

At one major proxy outsourcer, Institutional Shareholder Service, a team of some 270 global research analysts covers 40,000 shareholder meetings and an estimated 250,000 votes.

BlackRock, which boasts of having the "largest global stewardship team in the industry," employs roughly 50 staff over 85 voting markets.

It's good to be king

One solution floated by Levin, among others, is to use technology to strip voting power from fund

"Exposing voting rights to individual investors is right around the corner. Rekenthaler points out the sheer volume of ballot measures. Yet to use a metaphor, while there is an overwhelming volume of songs I could choose from, this doesn't stop me from streaming music," Levin explains.

"Once there's sufficient consumer awareness, then there's a market to deploy the curation technologies that can make proxy voting a thrilling experience. I also expect financial advisors, influencers, and other intermediaries will play a big part of that on-platform curation," he adds.

Yet fund companies are unlikely to just hand over the power they've become used to holding, says Deluard.

"Why not develop tools which would allow motivated Gen-Z-ers and Millennials to vote via their Vanguard account or Robinhood app? My guess would be that Larry Fink would resist the idea."

"It's good to be king," he adds.

Dublin-native and Edinburgh-based Oisín Breen has spent seven years writing about finance, including five whirlwind years diving into the advisor world for RIABiz. A widely published and well regarded poet with two full collections under his belt, Breen is also an academic in English Literature with a deep fondness for his Scottish rabbit, Hessell. @Breen

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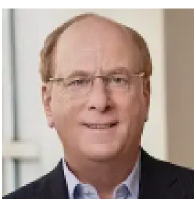

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August 8, 2022 at 9:57 PM

Vanguard Group shows up as 'alpha' disciple with two new fixed-income fund launches as it surpasses PIMCO's $2 trillion with ex-Goldman Sachs partner now calling the shots

The $8 trillion Malvern, Pa. manager owns beta investing, but RIAs are demanding higher income -- hence market timing and cherry picking -- from their fixed-income allocation.

August 10, 2021 at 7:46 PM

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Perry E Gibbs

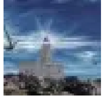
July 29, 2021 — 4:30 PM

Those who make the rules win the game, and the people are pawns of the game, the corporate way. Nothing personal, it's business!

Theguy

July 29, 2021 — 5:50 PM

Seems like every article assumes that ESG only looks at left wing issues... abortion, family values, gambling, porn, etc... never come up. Half of the investors would vote that way.



Karl McGaugh

August 16, 2021 — 10:09 AM

Great article! Yes, something needs to be done to limit this power but what? In my opinion, this began with the changes in the legal definition of a corporation. The limits were removed and now we have corporations owning other corporations. If this was outlawed then flesh & blood individuals would own as much as they want but corporations would be limited to their own stock. Competition would return to the market and individual investors would vote their conscience. This single change would solve every problem in this article and create vast new opportunities for investors. If Buffet wants to invest in a corporation he cannot be a corporation himself. And if he wants to be and private index fund he can not sell shares because he is not a corporation. He could sell his index picks as a research product but the selling of corporate bonds and shares are prohibited unless he is a corporation and if he becomes a corporation he is prohibited from buying shares in the companies in his index. This simple idea of prohibiting corporations from owning other corporations is the best way to limit and prevent multinational corporations (monopoly).

DDearborn

January 22, 2022 — 8:03 PM

Hmmm History is replete with an almost endless cast of some of the vilest, evil, maniacal lunatics that bear a striking resemblance to the latest cast of would-be Kings and Queens. History also teaches us that that simply trying to change our rules imposed by their game never gets you out of the pot because they don't follow any rules. In spite of the fact that History remains a startingly accurate and consistent guide offering considerable certainty that the latest crop of wannabe totalitarians and/or their seed will inevitably meet a similar fate, we must strengthen our resolve to resist complacency and indifference by whatever means necessary. Keep firmly in mind that if the outcome was as heavily weighted in their favor as we are being led to believe the seemingly endless machinations, manipulations and lies spewing out of every orifice of their regimes targeting the common man would not be necessary. In short, not only is it abundantly clear that the outcome is still very much in doubt, despite their every effort to convince us otherwise, that fact of the matter is that we still hold most of the hole cards

Mellisa Rose

February 27, 2022 — 1:15 AM

Those that makes the rules wins the game. I'm curious, wonder what did those that made the rules have to do exactly to get where they are at? They have done the unthinkable, unimaginable, and many dishonest manipulations have they put forth, to be in the position they are at. Just think about a bunch of country folks take control of the world... TN. Way to go, what a disgrace you are, & greed doesn't look good on you !

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