

## ICGN Viewpoint

### The Biden Administration: A new start for US corporate governance

December 2020

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The transition from the Trump Administration to a Joe Biden presidency portends a new policy direction across a range of fronts in the United States, including corporate governance. While we have yet to see a detailed Biden agenda relating to corporate governance, it is possible to anticipate important shifts to the governance landscape in the US, many of which should be welcome to institutional investors and governance professionals. However, the final makeup of the US Congress, following the outcome of the two Senate races in Georgia in early January, will be critical in determining the extent to which the balance of power will shift in the Biden Administration and empower the new administration to enact new legislation – or reverse policy elements from the Trump era.

ICGN's mission does not extend to political analysis or advocacy, apart from commenting on policy issues of relevance to good corporate governance and investor stewardship. However, following the inauguration of Trump in 2017, ICGN did publish a Viewpoint on how the Trump agenda contrasted with ICGN's own policy positions on a variety of important issues, including systemic risk and financial markets, climate and environmental risk, trade and protectionism, tax policy, and, more broadly, business ethics and political influence.<sup>1</sup>

Without seeking to make a political statement, the 2017 Viewpoint concluded that the Trump presidency stood to contradict the spirit and letter of important investor concerns, particularly with regard to long-term investors, such as pension funds. In particular, the Viewpoint challenged the short-termism of Trump's policy dynamics: a looser approach to financial regulation, less urgency in addressing climate risk, protectionist support of uncompetitive sectors, along with mixed signals on private and public ethical standards. Most fundamentally, the ICGN Viewpoint questioned the long-term sustainability of the Trump agenda in both economic and ethical dimensions. It called on both companies and investors to assess which aspects of Trump's policies may be likely to stand the test of time-- and which may be of lesser durability.

Against this background investors can anticipate a fresh direction in the Biden Administration relating to corporate governance and stewardship on a range of issues:

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<sup>1</sup> ICGN Viewpoint: "Governance questions posed by the changing U.S. political landscape" (February 2017): <https://www.icgn.org/governance-questions-posed-changing-us-political-landscape>

## Ethics

In government as in business, the “tone at the top” is critical in setting an example of high ethical standards. In the case of Trump, he has been labelled as “the most corrupt president in American history” by the non-partisan independent US government ethics watchdog, the Center for Responsibility and Ethics (CREW).<sup>2</sup> This assessment documents a long list of transgressions, including his impeachment in 2019 on charges of abuse of power and obstruction of Congress by the US House of Representatives, as well as over 3000 conflicts of interest relating to Trump’s business activities—from which he refused to divest. Trump also set a precedent for his unwillingness to disclose his own tax returns, employing his own children in the White House, and eight of his associates have either been arrested or convicted of crimes. This is not an ethical track record nor an example of leadership that institutional investors want to see in either the public or private sector.

In the case of President-Elect Biden we cannot forget that he dropped out of the 1988 election for the presidency as a consequence of his committing an act of plagiarism. But that was long ago, and is an ethical offense of a lower order than the abuses chronicled by the CREW report regarding Trump. Moreover, Biden’s ethical track record since then, including during his time as Vice President in the Obama Administration, is encouraging, and stands in sharp contrast to the Trump years. The Biden-Harris Transition Team Ethics Plan has signalled the intent of the new administration to adopt the “highest ethical standards,” including a robust code of ethics that many officials in the current Trump Administration would fail, including Trump himself. For investors with holdings in the US, this is promising, and will hopefully set the stage for a new tone at the top that will have relevance for the US government as well as US companies.

But ethical scrutiny will always be important under any administration. There have been unsubstantiated claims raised by Trump with regard to Biden’s son Hunter and his involvement with the Ukrainian company Burisma Holdings Limited, and Hunter Biden recently has announced that he is under investigation by the US Justice Department relating to his taxes.<sup>3</sup> However, none of these allegations are linked to the President-Elect himself. Watchdogs will also assess how Biden responds to concerns that several of his highest level appointees have had past links to consulting and investment firms with significant political influence.<sup>4</sup>

***January 2021 Update:*** since this Viewpoint was first published in December 2020, the Trump ethical legacy was further scarred by Trump’s refusal to accept the results of the November election and his attempts to use his influence to illegally overturn the election. This culminated in his provocation of a mob of Trump supporters to invade the US Capitol on 6 January 2021 during the formal Congressional confirmation of the Biden victory, and

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<sup>2</sup> CREW, “President Trump’s worst offenses”, 19 October 2020:

<https://www.citizensforethics.org/news/analysis/president-trumps-worst-offenses/>

<sup>3</sup> Adam Goldman, Katie Benner, and Kenneth R. Vogel, “Hunter Biden Discloses that He Is Focus of Federal Tax Inquiry”, New York Times, 9 December 2020: <https://www.nytimes.com/2020/12/09/us/politics/hunter-biden-tax-investigation.html?action=click&module=Top%20Stories&pgtype=Homepage>

<sup>4</sup> Eric Lipton and Kenneth P. Vogel, “Biden Aides’ Ties to Consulting and Investment Firms Pose Ethics Test”, New York Times, 29 November 2020: <https://www.nytimes.com/2020/11/28/us/politics/biden-westexec.html>

*resulted in Trump being the first US President ever to have been impeached twice. This event will stand as an attack on democracy and a long-lasting stain on American history; it is a testament to the risks that come with weak ethical leadership.*

## **Climate Change**

A fundamental concern of institutional investors relates to the systemic risk of climate change and its long-term threat to companies, markets, and society more broadly.<sup>5</sup> In Trump's first year in office he withdrew the US from the 2015 Paris Climate Agreement to reduce greenhouse gases, putting the world's largest economy dangerously out of lockstep with its peers --and almost all other countries in the world. At best the Trump Administration gave occasional lip service to addressing climate change, though Trump was more frequently on record expressing doubts about climate science, and his administration will be more remembered for reversing or watering down climate and environmental regulations.<sup>6</sup>

Here again, the Biden Administration offers greater promise to investors for the priority it has already placed on addressing climate change. This featured in the Biden-Harris campaign platform, and Biden has pledged to recommitting the US to the Paris Accord. It is also promising that he has created a "Climate Tsar" role for former US Secretary of State John Kerry, who initially signed the Paris Accord in 2016 on behalf of the US to lead the Obama Administration's climate agenda. On the disclosure front, we can expect greater consideration of corporate disclosure requirements relating to climate change, which could extend to the application of the TCFD (Task Force on Climate-related Disclosures) framework, as will soon be required in the UK, for example, for companies with a Premium Listing on the London Stock Exchange. Most institutional investors should welcome this new policy direction, though some of its scope could be limited if the Republican Party controls the US Senate.

## **ESG and stakeholder capitalism**

A related development is the surge of interest in environmental, social and governance (ESG) issues among investors, both from an ethical and economic perspective. While not a bi-product of the Trump agenda, the social role of business has come under renewed scrutiny in recent years, particularly with regard to companies having a purpose that extends beyond simple profit maximisation. "Stakeholder capitalism" has become a popular term of art, and has a broad intuitive appeal in many quarters, particularly in the Democratic Party – and even with the conservative Business Roundtable. As a presidential candidate, Biden challenged the strict interpretation of shareholder primacy, and, together with Vice President-Elect Kamala Harris, we can expect greater consideration of ESG issues, including social justice and stakeholders' rights and welfare relating to employees, customers, communities and broader social impacts.

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<sup>5</sup> ICGN Viewpoint, The Board of Directors and Climate Change, July 2020: <https://www.icgn.org/board-directors-climate-change>

<sup>6</sup> Nadja Popvovich, Livia Albeck-Ripka and Kendra Pierre-Louis, "The Trump Administration is reversing more than 100 environmental rules. Here's the full list", New York Times, 10 November 2020: <https://www.nytimes.com/interactive/2020/climate/trump-environment-rollback-list.html>

Policy specifics remain to be seen, but this could manifest itself in greater disclosure requirements relating to climate change, board diversity by gender and ethnicity, a greater emphasis on reducing the gender pay gap for women and a higher minimum wage. While some shareholders might interpret this direction as shareholder-unfriendly, long-term investors, particularly those with a focus on ESG and sustainable investment, will recognise the strategic importance of strong stakeholder relations-- as well as the need to address income inequality and to strengthen the social fabric in a very socially divided country. In a medium to long-term horizon this should reap benefits not only to stakeholders themselves but should also contribute towards stronger markets and economies, from which investors will benefit.

## Regulation

The final balance of the US Congress will have a critical influence in shaping the status of future legislation regarding corporate governance and responsible investment, even though changing existing regulations may be more challenging, again depending on the political makeup of the Senate. In particular, new leadership of the US Securities and Exchange Commission (SEC) in the Biden Administration has the potential to address current investor concerns with the Trump agenda. Among other things, the future Chairman will face investor pressures to address harshly restrictive measures on proxy agencies, which are important service providers for investors in exercising shareholder voting rights. ICGN has challenged the SEC's proxy advisor interpretation and guidance, including treating proxy voting agencies as a form of proxy solicitation.<sup>7</sup> The US Department of Labor (DoL) has also proven problematic with its proposals to challenge investors' rights to vote at shareholder meetings if there is not a demonstrable economic impact to the investor-- suggesting that this is more of a cost to investors than a benefit. This is a fundamental confusion and distortion of investor fiduciary duty.<sup>8</sup>

ICGN has also challenged the SEC's recent regulatory initiative to place greater restrictions on shareholder proposals.<sup>9</sup> Shareholder proposals are a fundamental ownership right, and are important to both institutional and retail investors, particularly with regard to encouraging greater sensitivity by companies to important ESG issues. In our view this recent SEC initiative was retrograde in nature, and counter to the spirit of supporting stewardship and corporate accountability to its shareholders. Yet even under the Biden Administration it may prove tough for the next SEC chair to revamp the proxy advice and shareholder proposal rules the SEC has recently passed. Ultimately, any changes would have to be formally proposed and put out for comment and justified with economic analysis. The US business community is likely to challenge proposed changes and could litigate to overturn any revisions that the new SEC proposes.

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<sup>7</sup> ICGN comment letter to SEC on Proxy Advisor Interpretation and Guidance, 21 November 2019: <https://www.icgn.org/sites/default/files/19.%20SEC%20Proxy%20Advisor%20Interpretation%20and%20Guidance.pdf>

<sup>8</sup> ICGN comment letter to DoL regarding fiduciary duties and shareholder rights: [https://www.icgn.org/sites/default/files/15.%20ICGN%20DoL%20Proxy%20Voting%20Letter\\_0.pdf](https://www.icgn.org/sites/default/files/15.%20ICGN%20DoL%20Proxy%20Voting%20Letter_0.pdf)

<sup>9</sup> ICGN comment letter to SEC on proposed amendments to Exchange Act Rule 14a-8, 4 December 2019: [https://www.icgn.org/sites/default/files/20.%20SEC%20shareholder%20resolution%20\\_0.pdf](https://www.icgn.org/sites/default/files/20.%20SEC%20shareholder%20resolution%20_0.pdf)

Human capital is an area of increasing focus for investors, in recognition of the critical role of employees in long-term corporate sustainability and success.<sup>10</sup> Here again, ICGN has engaged with the SEC to encourage stronger reporting requirements and metrics relating to workforce compensation, turnover and diversity.<sup>11</sup> We are hopeful that the priority that the Biden-Harris ticket has placed on social justice, stakeholders and the workforce more specifically will lead to improved company disclosures and to more meaningful company engagement with employees and stronger employee relations.

We have already highlighted the growing importance of ESG factors as a matter of consideration both for company boards and investors. It is a complex area, and the subject of much discussion globally with regard to the consolidation of ESG data standards and reporting frameworks. Many US companies and investors are constructively engaged with ESG reporting issues. However, at a public sector level the US has not shown the leadership we might have hoped for from the world's largest economy and capital market. In a global context we believe the US is lagging the European Union and other jurisdictions where ESG and sustainability are high priority issues.

This is particularly relevant with regard to ESG reporting, where there is a general need globally to raise the quality, consistency and comparability of ESG information. If anything, the Trump Administration has presented itself as suspicious, if not antagonistic, regarding ESG reporting, wrongly and unnecessarily politicising this as an issue. For example, the DoL sought to inhibit the consideration of ESG factors in the investment process under the premise that use of ESG information by investors is some ways “non-pecuniary,” subordinating investment returns for broader social benefits.

This is a fundamental misunderstanding of how investors regard ESG data, and we believe highly inappropriate for a US government agency to determine what does or does not have pecuniary merit in the investment decision making process. Indeed, we believe it is a core fiduciary duty of investors to use ESG information to better understand company management quality, risks and opportunities – and that it boils down to wilful ignorance for the DoL to dismiss the importance of ESG information.<sup>12</sup> We hope and believe the Biden Administration will take a more progressive and supportive stance regarding ESG reporting.

Finally, we would like to highlight audit quality and the work of the Public Company Accounting Oversight Board (PCAOB). Audit quality is of fundamental importance to companies, investors and financial markets more broadly. The formation of the PCAOB to promote high standards of audit quality was an encouraging development, with its mission to “protect investors and the public interest.” ICGN has engaged the PCAOB constructively on

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<sup>10</sup> ICGN Viewpoint on Human Capital Management, October 2018: <https://www.icgn.org/human-capital-management-why-investors-should-care-and-what-they-should-look-corporate-disclosure>

<sup>11</sup> ICGN comment letter to SEC on Modernization of Regulation S-K Items 101, 103, and 105, 26 August 2020: <https://www.icgn.org/sites/default/files/12.%20ICGN%20Letter%20Reg%20S-K%20to%20SEC.pdf>

<sup>12</sup> ICGN comment letter to DoL proposal on Financial Factors in Selecting Plan Investment Proposed Regulation: RIN 1210-AB95, 29 July 2020: [https://www.icgn.org/sites/default/files/11.%20ICGN%20Response%20to%20the%20Department%20of%20Labor%20proposal%20on%20Financial%20Factors%20in%20Selecting%20Plan%20Investment%20Proposed%20Regulation\\_0.pdf](https://www.icgn.org/sites/default/files/11.%20ICGN%20Response%20to%20the%20Department%20of%20Labor%20proposal%20on%20Financial%20Factors%20in%20Selecting%20Plan%20Investment%20Proposed%20Regulation_0.pdf)

its quality control standards.<sup>13</sup> However, we are concerned that the voice of investors, as key beneficiaries of a quality audit process, is not a high priority. For example, the PCAOB has not had a meeting of either its investor advisory committee nor its standing advisory committee (which has investors on it) for two years. The PCAOB has also recently moved to weaken auditor independence rules.<sup>14</sup> This raises questions about PCAOB's own governance and transparency, and we are hopeful that a Biden Administration will revitalise the PCAOB and enhance its investor focus and engagement. However, this could take a while, given that the current chair, William Duhnke is not required to step down when Biden takes office.

## **Conclusion**

The US market is hugely important to institutional investors, and has an enviable track record of growth and value creation. But the dynamics of building sustainable economies to meet the needs of the 21<sup>st</sup> Century have been evolving, and in our view the Trump Administration has fallen short on a wide range of issues. While we are aware that the makeup of Congress may inhibit making progress in many of these areas, we are hopeful that the Biden presidency will lead to a change of direction in a way that with both create sustainable value for investors and promote the interests and rights of the broad stakeholder base that is essential for ongoing economic growth and social welfare.

## **ICGN Viewpoints**

ICGN Viewpoints are produced by Secretariat and by our member-led Policy Committees. While not defining a formal ICGN position on the subject, they provide opinion on emerging corporate governance issues and are intended to inform and generate debate. This ICGN Viewpoint was written by George Dallas, ICGN Policy Director.

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<sup>13</sup> ICGN comment letter to PCAOB Concept Release for Potential Approach to Revisions to PCAOB Quality Control Standards, 16 March 2020: <https://www.icgn.org/sites/default/files/3.%20ICGN%20Response%20to%20PCAOB%20on%20Audit%20Quality.pdf>

<sup>14</sup> J. Robert Brown Jr., "Reducing PCAOB Authority over Auditor Independence", 19 November 2020: <https://pcaobus.org/news-events/speeches/speech-detail/reducing-pcaob-authority-over-auditor-independence>