

# SHAREHOLDER PROPOSAL RULE: CRACKER BARREL IN LIGHT OF *TEXACO*

## INTRODUCTION

In June 1994, six employees filed suit against Texaco, Inc., claiming that the company failed to hire and promote African-Americans.<sup>1</sup> Alleged incidents included the use of racial epithets by white senior executives to black employees.<sup>2</sup> The plaintiffs, who grew to a class of 1400 employees, sought \$520 million in damages.<sup>3</sup>

The lawsuit progressed slowly until November 4, 1996 when the New York Times published the transcript of an audiotaped August 1994 meeting of Texaco executives.<sup>4</sup> The tapes recorded the top officials making vulgar racist remarks and belittling black employee grievances.<sup>5</sup> The executives referred to African-American employees as "black jelly beans."<sup>6</sup> One executive was taped complaining about black workers' demand for recognition of the holiday Kwanzaa, stating, "I'm still having trouble with Hanukkah."<sup>7</sup> Within days of the release of the tapes, Texaco stock dropped three dollars a share, which equaled approximately one billion dollars in losses for shareholders.<sup>8</sup> Reverend Jesse Jackson and other civil rights leaders called for a national consumer boycott of the oil company.<sup>9</sup>

Within two weeks of the scandal, Texaco agreed to pay \$176.1 million to settle the case, the largest settlement ever in a United States discrimination lawsuit.<sup>10</sup> As part of the \$176.1 million settlement, Tex-

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<sup>1</sup> See Peter Fritsch, *Trustee of Big Fund With Texaco Stock Says Tape Shows 'Culture of Disrespect'*, WALL ST. J., Nov. 6, 1996, at A5; Jolie Solomon, *Texaco's Troubles: A Scandal Over Racial Slurs Forces the Oil Giant to Rethink—and Remake—Its Corporate Identity*, NEWSWEEK, Nov. 25, 1996, at 49.

<sup>2</sup> See Allanna Sullivan & Rochelle Sharpe, *Texaco to Pay \$176.1 Million in Bias Suit: Record Settlement Includes Task Force Possessing Oversight Power*, WALL ST. J., Nov. 18, 1996, at A3.

<sup>3</sup> See Fritsch, *supra* note 1, at A5.

<sup>4</sup> See Kurt Eichenwald, *Texaco Executives, On Tape, Discussed Impeding a Bias Suit*, N.Y. TIMES, Nov. 4, 1996, at A1; *Excerpts From Tapes In Discrimination Lawsuit*, N.Y. TIMES, Nov. 4, 1996, at D4; Solomon, *supra* note 1, at 48.

<sup>5</sup> See Eichenwald, *supra* note 4, at A1; *Excerpts From Tapes In Discrimination Lawsuit*, *supra* note 4, at D4.

<sup>6</sup> See *Excerpts From Tapes In Discrimination Lawsuit*, *supra* note 4, at D4.

<sup>7</sup> See Eichenwald, *supra* note 4, at A1.

<sup>8</sup> See Jack E. White, *Texaco's High-Octane Racism Problems: Piles of Cash and Substantial Reforms Fail to Reverse the Call for a Boycott*, TIME, Nov. 25, 1996, at 34.

<sup>9</sup> See *id.*

<sup>10</sup> See Sullivan & Sharpe, *supra* note 2, at A3.

aco would pay \$115 million in cash to the 1400 plaintiffs, \$26.1 million for pay raises over the next five years and \$35 million for diversity programs, including scholarship and internship programs.<sup>11</sup> The settlement included the establishment of an independent task force, consisting of three representatives of the plaintiffs, three representatives of management and a chairperson agreed upon by the other six, to oversee the company's employment policies.<sup>12</sup>

Texaco is not alone in suffering severe financial setbacks as a result of its employment policies.<sup>13</sup> Companies like Shoney's Inc., Mitsubishi Motor Manufacturing of America Inc., Publix Supermarkets Inc. and Home Depot Inc. recently have been embroiled in costly and publicly damaging racial and gender bias lawsuits.<sup>14</sup> The expense and negative publicity of these employment discrimination lawsuits have made apparent the adverse effects of employment policies on a company's bottom line.<sup>15</sup> The lawsuits, especially the case against Texaco, elucidate the necessity of management accountability to owners for employment decisions.<sup>16</sup>

This Note discusses the need for shareholder participation in employment policies through the shareholder proposal process. Under Section 14(a) of the Securities Exchange Act of 1934, Congress gave the Securities Exchange Commission ("SEC") the power to adopt rules allowing shareholders the right to submit proposals to management for inclusion in the corporation's proxy materials.<sup>17</sup> The SEC enacted Rules 14a-8 and 14a-9, which make it unlawful for a company to omit a shareholder proposal that complies with the conditions provided in the Rules.<sup>18</sup> Rule 14a-8(c)(7) allows companies to omit proposals that deal with ordinary business operations.<sup>19</sup> The SEC has struggled with whether proposals involving employment policies, like equal employment opportunity and affirmative action, are excludable as ordinary business matters.<sup>20</sup> The SEC stated in its 1976 Interpretive

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<sup>11</sup> See White, *supra* note 8, at 33.

<sup>12</sup> See *id.*

<sup>13</sup> See David A. Price, *Job-Bias Lawsuits Skyrocket*, INVESTOR'S BUS. DAILY, Oct. 13, 1997, at A1.

<sup>14</sup> See *id.*

<sup>15</sup> See George J. Church, *On the Job: Equality Pays: Corporate America Has Its Own Reason To Weed Out Discrimination—The Bottom Line*, TIME, June 23, 1997, at 39.

<sup>16</sup> See Joann S. Lublin, *Management: Texaco Case Causes a Stir in Boardrooms*, WALL ST. J., Nov. 22, 1996, at B1.

<sup>17</sup> See Securities Exchange Act of 1934, 15 U.S.C. § 78n(a) (1994).

<sup>18</sup> See 17 C.F.R. §§ 240.14a-8, 14a-9 (1997).

<sup>19</sup> See *id.* § 240.14a-8(c)(7).

<sup>20</sup> See Capital Cities/ABC, Inc., SEC No-Action Letter, [1990-1991 Transfer Binder] Fed. Sec. L. Rep. (CCIL) ¶ 79,690, at 78,116 (Apr. 4, 1991) [hereinafter Capital Cities/ABC No-Action Letter]; American Telephone & Telegraph Co., SEC No-Action Letter, 1988 WL 235275, at \*15 (Dec. 21, 1988) [hereinafter AT&T No-Action Letter].

Release that proposals dealing with matters that have significant policy implications must be included in the proxy statement. In a 1992 no-action letter to Cracker Barrel Old Country Store, Inc. ("Cracker Barrel"), however, the SEC declared that corporations no longer would be required to include shareholder proposals on social issues if they related to general employment issues.<sup>21</sup> The SEC is currently reassessing that position.

Section I of this Note describes other recent employment discrimination lawsuits that show the consequences of management control over employment policies.<sup>22</sup> Section II provides background on Section 14(a) and the shareholder proposal process.<sup>23</sup> Section III examines the ordinary business exception and the SEC interpretation of the exception in Cracker Barrel.<sup>24</sup> This section illustrates the SEC's difficulty in applying the exception to proposals involving employment policies. Section IV explores the reaction to Cracker Barrel and its proposed reversal.<sup>25</sup> Finally, this Note argues that in light of the costly employment litigation of recent years, the SEC position in Cracker Barrel should be reversed.<sup>26</sup>

## I. OTHER EMPLOYMENT DISCRIMINATION LAWSUITS NEGATIVELY AFFECTING SHAREHOLDERS

The Texaco case is not an anomaly.<sup>27</sup> There have been numerous high stakes employment discrimination lawsuits in recent years.<sup>28</sup> Like Texaco, Shoney's Inc. recently suffered negative publicity and financial strain from a racial bias lawsuit.<sup>29</sup> In 1989, eighteen black employees sued the restaurant chain for class-wide discrimination against black employees and job applicants, seeking a minimum of \$530 million in damages and a court-ordered affirmative action plan.<sup>30</sup> The plaintiffs claimed that executives, supervisors and managers disparaged, denied

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<sup>21</sup> See Adoption of Amendments Relating to Proposals by Security Holders, Exchange Act Release No. 12,999, 41 Fed. Reg. 52,994, 52,998 (1976) [hereinafter 1976 Interpretive Release]; Cracker Barrel Old Country Store, Inc., SEC No-Action Letter, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 76,418, at 77,284, 77,287 (Oct. 13, 1992).

<sup>22</sup> See *infra* notes 27-61 and accompanying text.

<sup>23</sup> See *infra* notes 62-81 and accompanying text.

<sup>24</sup> See *infra* notes 82-153 and accompanying text.

<sup>25</sup> See *infra* notes 154-86 and accompanying text.

<sup>26</sup> See *infra* notes 187-263 and accompanying text.

<sup>27</sup> See Price, *supra* note 13, at A1.

<sup>28</sup> See *id.*

<sup>29</sup> See Dorothy J. Gaiter, *Eating Crow: How Shoney's, Belled By a Lawsuit, Found the Path to Diversity*, WALL ST. J., Apr. 16, 1996, at B4.

<sup>30</sup> See *Shoney's Inc.: Judge Approves Settlement of Racial Bias Lawsuit*, WALL ST. J., Jan. 26, 1993, at B4.

promotions, fired or declined to hire blacks.<sup>31</sup> Allegations arose that Shoney's then chairman and principal shareholder, Raymond Danner, espoused a company policy that "too many blacks" were not good for business.<sup>32</sup> Plaintiffs claimed that Danner referred to blacks as "niggers" and ordered managers to keep black employees out of public view.<sup>33</sup> Managers testified to a company strategy of weeding out minority job applicants by color-coding applications—a blackened-in "O" in the word Shoney's on the application meant the applicant was black and would not be called back for an interview.<sup>34</sup> When word of the lawsuit was made public, Shoney's stock tumbled from \$20 a share to as low as \$7.50 a share.<sup>35</sup>

Avoiding the negative publicity and expense of a trial, in 1992, Shoney's settled the suit for \$134.5 million, \$105 million of which would be available to over 20,000 employees.<sup>36</sup> Considering Shoney's relative size, the settlement was much more damaging than the Texaco settlement.<sup>37</sup> The Wall Street Journal reported that the settlement "walloped" the restaurant chain's earnings in 1992 and that the company posted a \$26.6 million loss for the year.<sup>38</sup>

The settlement also required Shoney's to integrate its work force completely, under the scrutiny of plaintiffs' lawyers, and required that managers provide detailed information about the company's affirmative action progress.<sup>39</sup> Soon after the suit was filed, Shoney's made an agreement with the Southern Christian Leadership Conference ("SCLC") that the company would pay \$30 million over three years to recruit more minorities, to purchase from black vendors and to assist blacks in acquiring franchises.<sup>40</sup> In 1996, the Wall Street Journal re-

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<sup>31</sup> See Gaiter, *supra* note 29, at B4.

<sup>32</sup> See STEVE WATKINS, *THE BLACK O: RACISM AND REDEMPTION IN AN AMERICAN CORPORATE EMPIRE* 4 (1997).

<sup>33</sup> See Brett Pulley, *Strained Family: Culture of Racial Bias at Shoney's Underlies Chairman's Departure*, WALL ST. J., Dec. 21, 1992 at A1.

<sup>34</sup> See WATKINS, *supra* note 32, at 5; Pulley, *supra* note 33, at A1.

<sup>35</sup> See Gaiter, *supra* note 29, at B4.

<sup>36</sup> See *id.*

<sup>37</sup> In January 1997, attorney Paul Neuhauser submitted a statement to the SEC on behalf of shareholders who presented a proposal to Shoney's Inc. requesting the company prepare an equal employment opportunity report. See Shoney's Inc., SEC No-Action Letter, 1997 WL 9826, at \*17 (Jan. 10, 1997) [hereinafter Shoney's No-Action Letter]. By analyzing the 1995 revenues of Texaco and Shoney's, he calculated that a comparable settlement for Texaco would have cost approximately \$4.5 billion as compared to the \$176 million it actually paid. See *id.*

<sup>38</sup> See Gaiter, *supra* note 29, at B4.

<sup>39</sup> See Michael J. McCarthy & Glenn Ruffenach, *Shoney's Chief Resigns, in Move Surprising Board*, WALL ST. J., Dec. 18, 1992, at B4.

<sup>40</sup> See Pulley, *supra* note 33, at A1.

ported that Shoney's had spent more than \$194 million on minority organizations and salaries to repair its image after the lawsuit.<sup>41</sup>

In recent years, there also have been many widely-publicized sexual discrimination lawsuits.<sup>42</sup> Mitsubishi Motor Manufacturing of America Inc. is currently embroiled in what could be the nation's largest sexual harassment lawsuit.<sup>43</sup> In April 1996, the Equal Employment Opportunity Commission ("EEOC") filed a class-action lawsuit against Mitsubishi that covers over five hundred women employed at the Normal, Illinois factory.<sup>44</sup> The EEOC alleged that the company tolerated a work environment in which female employees were fondled and routinely called bitches and whores, and obscene graffiti was placed on factory walls.<sup>45</sup> The more than five hundred potential plaintiffs each could be eligible for \$300,000 in compensatory and punitive damages, possibly costing Mitsubishi a total of \$150 million.<sup>46</sup> Reverend Jesse Jackson and the National Organization of Women organized a nationwide boycott and picketing of Mitsubishi dealerships in response to the sexual harassment charges.<sup>47</sup> Mitsubishi has continued to face intense financial and public relations setbacks because of the lawsuit.<sup>48</sup>

Two corporations recently settled expensive and widely-publicized sex-bias lawsuits.<sup>49</sup> In January 1997, Publix Supermarkets Inc. settled a class-action sex discrimination lawsuit that covered about 150,000 current and former female employees for \$81.5 million.<sup>50</sup> The plaintiffs claimed that the grocery store chain routinely had denied them "desirable job assignments, promotions and management opportunities."<sup>51</sup> One of the plaintiffs complained that she attempted to obtain a pro-

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<sup>41</sup> See Gaiter, *supra* note 29, at B4.

<sup>42</sup> See Price, *supra* note 13, at A1.

<sup>43</sup> See EEOC Official Says Mitsubishi Motor Suit Isn't Near Settlement, WALL ST. J., May 13, 1996, at B5.

<sup>44</sup> See Peter Annin & John McCormick, *More Than a Tune-up: Tough Going in a Fight Against Sexual Harassment*, NEWSWEEK, Nov. 24, 1997, at 50. In August 1997, Mitsubishi settled a similar lawsuit for \$9.5 million. See *id.* Twenty-nine female employees filed suit in December of 1994 claiming that Mitsubishi fostered a climate of sexual harassment. See *id.* at 52.

<sup>45</sup> See Rochelle Sharpc, *EEOC Sues Mitsubishi Unit For Harassment*, WALL ST. J., Apr. 10, 1996, at B1.

<sup>46</sup> See *id.*

<sup>47</sup> See Mitsubishi Motors Boycott Expanding To Some Partners, WALL ST. J., May 21, 1996, at A7.

<sup>48</sup> See Mitsubishi Picketing Concerning Lawsuits Is Readied by Groups, WALL ST. J., May 8, 1996, at B3.

<sup>49</sup> See Price, *supra* note 13, at A1.

<sup>50</sup> See Glenn Ruffenach, *Publix Supermarkets Will Pay \$81.5 Million to Settle Bias Suit*, WALL ST. J., Jan. 27, 1997 (available in 1997 WL 2407172).

<sup>51</sup> See *id.*

motion from a cashier's job but was told by management that women were incapable of working in supervisory positions.<sup>52</sup>

In November 1997, Home Depot, Inc. settled a class-action sex-bias suit, agreeing to pay \$87.5 million.<sup>53</sup> The case potentially covered more than 200,000 current and former employees and job applicants, who claimed that the home improvement retailer discriminated against women by limiting their advancement and promotional opportunities.<sup>54</sup> Home Depot projected that the settlement could result in a twenty-one percent decrease in the company's 1997 third quarter per share earnings.<sup>55</sup>

The costliness of these lawsuits is due in part to the passage of the Civil Rights Act of 1991, which allows discrimination plaintiffs the right to recover compensatory and punitive damages.<sup>56</sup> The Act also gives plaintiffs the option of a jury trial, which may help plaintiffs recover higher damages.<sup>57</sup> Furthermore, courts' willingness to allow plaintiffs to proceed as a class-action has increased the stakes of employment litigation.<sup>58</sup>

The costs of discriminatory employment policies have the potential to seriously harm the financial condition of a company and diminish shareholder value.<sup>59</sup> In response to these lawsuits,<sup>60</sup> shareholders have increased pressure to play a role in employment policy decision-

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<sup>52</sup> See *id.*

<sup>53</sup> See Jacqueline Bueno, *Home Depot's Agreement to Settle Suit Could Cut 3rd-Quarter Earnings by 21%*, WALL ST. J., Sept. 22, 1997, at B18.

<sup>54</sup> See *id.*

<sup>55</sup> See *id.*

<sup>56</sup> See Civil Rights Act of 1991, 42 U.S.C. § 1981a(a)(1) (1994); Price, *supra* note 13, at A1. The Act states in relevant part: "In an action brought by a complaining party under . . . the Civil Rights Act of 1964 against a respondent who engaged in unlawful intentional discrimination . . . , the complaining party may recover compensatory and punitive damages . . . ." See 42 U.S.C. § 1981a(a)(1).

<sup>57</sup> See 42 U.S.C. § 1981a(c); Price, *supra* note 13, at A1. The Act states that "[i]f a complaining party seeks compensatory or punitive damages under this section . . . any party may demand a trial by jury . . . ." See 42 U.S.C. § 1981a(c).

<sup>58</sup> See Price, *supra* note 13, at A1.

<sup>59</sup> See Church, *supra* note 15, at 38-39.

<sup>60</sup> Increased shareholder activism through the shareholder proposal process after recent discrimination lawsuits is evidenced by the number of statements submitted to the SEC with company requests for no-action letters that refer to the Texaco and Shoney's cases to support the inclusion of employment-related proposals in the proxy statement. See, e.g., Rite Aid Corp., SEC No-Action Letter, 1998 WL 40240, at \*4 (Jan. 26, 1998) (referring to Shoney's and Texaco settlements as support for resolution to report on company's equal employment opportunity data); Shoney's No-Action Letter, 1997 WL 9826, at \*15-17 (arguing that equal employment opportunity issues affect the bottom line and therefore are of enormous concern to shareholders).

making. They see the shareholder proposal process as a way to change company policies and thereby protect their investment.<sup>61</sup>

## II. THE SHAREHOLDER PROPOSAL PROCESS

### A. Section 14(a)

Proxy solicitation has become an important means for socially responsible investors to voice ownership concerns to management and demand changes in company policies.<sup>62</sup> The use of shareholder proposals in proxy materials for social purposes emerged in the early 1970s, when shareholders submitted proposals seeking corporate withdrawal from South Africa.<sup>63</sup> Shareholders also began to submit proposals on employment-related issues in the 1970s, requesting that companies disclose their equal employment opportunity data.<sup>64</sup>

The right of shareholders to submit proposals for proxy solicitation developed out of Section 14(a) of the Securities Exchange Act of 1934.<sup>65</sup> Congress delegated to the SEC the power to regulate proxy materials as it deemed "necessary or appropriate in the public interest or for the protection of investors."<sup>66</sup> It declared that proxy solicitation in violation of the SEC rules would be unlawful.<sup>67</sup> The purpose of Section 14(a) was to prevent management from obtaining authorization by shareholders through deceptive or inadequate disclosure through proxy solicitation.<sup>68</sup> Congress also sought to encourage corporate democracy, stating that "[f]air corporate suffrage is an important right that should attach to every equity security bought on a public exchange."<sup>69</sup> The United States Court of Appeals for the District of Columbia Circuit has stated that the purpose of Section 14(a) is "to

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<sup>61</sup> See Church, *supra* note 15, at 38-39.

<sup>62</sup> See Paul Beckett, *SEC to Vote on Proxy Rule Covering Holders' Proposals on Workplace Issues*, WALL ST. J., Aug. 27, 1997, at C16; Steven M. H. Wallman, *Equality Is More Than 'Ordinary Business'*, N.Y. TIMES, Mar. 30, 1997, at § 3, 12.

<sup>63</sup> See Shoney's No-Action Letter, 1997 WL 9826, at \*14.

<sup>64</sup> See *id.*

<sup>65</sup> See Securities Exchange Act, 15 U.S.C. § 78n(a) (1997). The Act provides in relevant part: It shall be unlawful for any person . . . in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors, to solicit . . . any proxy or consent or authorization in respect of any security (other than an exempted security) registered pursuant to section 78l of this title.

See *id.*

<sup>66</sup> *Id.*

<sup>67</sup> See *id.*

<sup>68</sup> See *J.I. Case Co. v. Borak*, 377 U.S. 426, 431 (1964).

<sup>69</sup> See *id.* (citation omitted).

assure to corporate shareholders the ability to exercise their right—some say their duty—to control the important decisions which affect them in their capacity as stockholders.<sup>70</sup> Through the voting procedures of proxy solicitation, Congress intended to give stockholders a role in the management of the corporation.<sup>71</sup>

### B. Rule 14a-8

In 1942, the SEC, pursuant to the authority granted it under Section 14(a), adopted Rule 14a-8, which gives shareholders the right to submit proposals to be included in the corporation's proxy statement.<sup>72</sup> Rule 14a-8(a) states that if any shareholder notifies the registered company of his or her intention to present a proposal at an upcoming meeting, the company must set forth the proposal in its proxy statement.<sup>73</sup> If a company omits a shareholder proposal in violation of Rule 14a-8, the proxy materials are deemed misleading and the company may be subject to an SEC enforcement action.<sup>74</sup> Rule 14a-8, therefore, advances the remedial purposes of Section 14(a) by assuring shareholder access to the company's proxy materials.<sup>75</sup> It further facilitates communication among shareholders and between shareholders and management.<sup>76</sup>

Although Rule 14a-8 provides shareholders access to the proxy materials, it contains eligibility requirements and exceptions that limit the number of proposals that a corporation will have to include in its proxy statement.<sup>77</sup> The SEC recognized the potential for companies to

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<sup>70</sup> Medical Comm. for Human Rights v. SEC, 432 F.2d 659, 680-81 (D.C. Cir. 1970). In *Medical Comm.*, a shareholder brought suit against the SEC after it permitted Dow Chemical to omit a proposal requesting that the company include in its proxy statement a resolution to discontinue the manufacturing of napalm. Ultimately remanding the case to the SEC, the court considered the merits of the shareholder proposal under 14a-8(c)(7). See *id.*

<sup>71</sup> See *id.*

<sup>72</sup> See 15 U.S.C. § 78n(a); 17 C.F.R. § 240.14a-8.

<sup>73</sup> See 17 C.F.R. § 240.14a-8(a). Rule 14a-8(a) states in relevant part:

If any security holder of a registrant notifies the registrant of his intention to present a proposal for action at a forthcoming meeting of the registrant's security holders, the registrant shall set forth the proposal in its proxy statement . . . . Notwithstanding the foregoing, the registrant shall not be required to include the proposal in its proxy statement or form of proxy unless the security holder has complied with the requirements of this paragraph and paragraphs (b) and (c) of this section.

*Id.*

<sup>74</sup> See *id.* § 240.14a-8, 14a-9.

<sup>75</sup> See 15 U.S.C. § 78n(a); 17 C.F.R. § 240.14a-8; *Borak*, 377 U.S. at 431-32.

<sup>76</sup> See *Medical Comm.*, 432 F.2d. at 680-81.

<sup>77</sup> In order for a shareholder to submit a proposal, he or she must own at least one percent or \$1,000 worth of stock, intend to present the proposal at the company's annual meeting and must have owned the stock for at least one year and continue to own the stock until the annual meeting. See *id.* § 240.14a-8(a)(1). The company must receive the proposal four months before

become inundated with proposals.<sup>78</sup> It also recognized the amount of time and money that companies must spend to comply with Rule 14a-8.<sup>79</sup> As the United States Court of Appeals for the District of Columbia Circuit explained, the SEC did not intend to make proxy solicitations "an all-purpose forum for malcontented shareholders to vent their spleen about irrelevant matters."<sup>80</sup> Therefore, the SEC imposed restrictions that limit congestion and reduce the number of proposals that a company must include in its proxy statement.<sup>81</sup>

### III. THE ORDINARY BUSINESS EXCEPTION

The exception companies wishing to omit employment-related shareholder proposals commonly use is Rule 14a-8(c)(7), the ordinary business operations exception.<sup>82</sup> Adopted in 1953, Rule 14a-8(c)(7) states that a registrant may omit a proposal if it "deals with a matter relating to the conduct of the ordinary business operations of the registrant."<sup>83</sup> Recognizing the impracticability of investor involvement in daily business matters, the SEC crafted the exception to relieve companies of the burden of including in the proxy materials proposals dealing with routine business decisions that are normally within the discretion of management.<sup>84</sup> The exception allows management to use its expertise to handle the complexities of the daily operation of a company without shareholder interference.<sup>85</sup> Although the purpose of the exception of proposals on matters best left to the specialized skills of management is clear, the SEC has struggled to establish a workable

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the annual meeting. *See id.* § 240.14a-8(a)(3)(i). A company can exclude a proposal that failed to garner a certain percentage of the votes at a previous annual meeting. *See id.* § 240.14a-8(c)(12). There are also exceptions to Rule 14(a)(8). *See, e.g.,* § 240.14a-8(c)(5) (proposal not significantly related to the company's business operations); 14a-8(c)(7) (proposal related to ordinary business operations); 14a-8(c)(10) (proposal rendered moot).

<sup>78</sup> *See* Alan R. Palmiter, *The Shareholder Proposal Rule: A Failed Experiment in Merit Regulation*, 45 ALA. L. REV. 879, 886-87 (1994). The SEC recently estimated that between 300 and 400 companies receive a total of about 900 shareholder proposals per year. *See* Amendments to Rules on Shareholder Proposals, Exchange Act Release No. 39,093 [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,961, at 89,851 (proposed Sept. 18, 1997) [hereinafter Proposed Rules].

<sup>79</sup> According to the results of an SEC questionnaire in which 67 companies responded, companies spend an average of around \$50,000 in printing costs to include shareholder proposals. *See* Proposed Rules, Exchange Act Release No. 39,093 [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 89,876. The cost to companies to consider and prepare a submission under Rule 14a-8 to the SEC, including internal and external legal fees, averaged around \$37,000, based on the responses of 80 companies. *See id.*

<sup>80</sup> *Medical Comm.*, 432 F.2d at 678.

<sup>81</sup> *See* Palmiter, *supra* note 78, at 885.

<sup>82</sup> *See* 17 C.F.R. § 240.14a-8(c)(7).

<sup>83</sup> *Id.*

<sup>84</sup> *See Medical Comm.*, 432 F.2d at 678.

<sup>85</sup> *See id.* at 679.

definition of "ordinary business operations."<sup>86</sup> In particular, the SEC has had difficulty applying the exception to proposals that relate to an operational decision but also concern a significant social issue.<sup>87</sup> Such proposals fall under the "business operations" language but not under the "ordinary" language of Rule 14a-8(c)(7).<sup>88</sup> The application of the exception to employment-related proposals has been especially problematic.<sup>89</sup> Companies attempt to omit proposals involving employment practices because hiring and firing seems to fall within ordinary business decisions.<sup>90</sup> The SEC has had difficulty condoning such omissions when the hiring and firing decisions also involve social policies, like discrimination.<sup>91</sup>

### A. *The 1976 Interpretive Release*

The SEC attempted to clarify the meaning of "ordinary business operations" and to adopt a more workable standard for application of the exception in its 1976 Interpretive Release.<sup>92</sup> The SEC adopted the Release after a formal notice and comment rule-making period, thereby rendering the legislative rule legally binding.<sup>93</sup> The SEC recommended a flexible interpretation of the 14a-8(c)(7) exception in the Release.<sup>94</sup> It stated:

the term "ordinary business operations" has been deemed on occasion to include certain matters which have significant policy, economic or other implications inherent in them. For instance, a proposal that a utility company not construct a proposed nuclear power plant has in the past been considered excludable . . . . In retrospect, however, it seems apparent that the economic and safety considerations attendant to nuclear power plants are of such magnitude that a determi-

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<sup>86</sup> See 17 C.F.R. § 240.14a-8(c)(7); *Medical Comm.*, 432 F.2d at 678-79.

<sup>87</sup> See Cracker Barrel No-Action Letter, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCIH) ¶ 76,418, at 77,287 (expressing difficulty of SEC in line-drawing under ordinary business exception).

<sup>88</sup> See 17 C.F.R. § 240.14a-8(c)(7).

<sup>89</sup> See Cracker Barrel No-Action Letter, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCIH) at 77,287 ("the line between includable and excludable employment-related proposals based on social policy considerations has become increasingly difficult to draw").

<sup>90</sup> See, e.g., AT&T No-Action Letter, 1988 WL 235275 (Dec. 21, 1988).

<sup>91</sup> See *id.*

<sup>92</sup> See 1976 Interpretive Release, 41 Fed. Reg. 52,994, 52,998 (1976).

<sup>93</sup> See *Amalgamated Clothing and Textile Workers Union ("ACTWU") v. Wal-Mart Stores Inc.*, 821 F. Supp. 877, 883-84 (S.D.N.Y. 1993) [hereinafter "ACTWU I"].

<sup>94</sup> See 1976 Interpretive Release, 41 Fed. Reg. at 52,998.

nation whether to construct one is not an "ordinary" business matter. Accordingly, proposals of that nature, as well as others that have major implications, will in the future be considered beyond the realm of an issuer's ordinary business operations, and future interpretive letters of the Commission's staff will reflect that view.<sup>95</sup>

The SEC drew the line between business matters that are "mundane in nature" and matters involving "substantial policy or other considerations."<sup>96</sup>

### B. SEC Review of Ordinary Business Exception

Although the SEC attempted to provide a clear standard for the ordinary business exception in its 1976 Interpretive Release, the SEC has struggled in applying the ordinary business operations exception through no-action letters.<sup>97</sup> If a company wishes to exclude a proposal from the proxy materials based on the eligibility requirements and exceptions, it may submit the proposal to the SEC with a written explanation of its reasons for the omission.<sup>98</sup> The SEC will respond in a letter stating whether it will recommend action against the company for the exclusion.<sup>99</sup> The purpose of this no-action letter is to aid companies in determining whether to include proposals.<sup>100</sup>

The no-action letters are not binding on the SEC, the courts or the parties.<sup>101</sup> The SEC's determinations in these letters are confined to the particular facts and circumstances of a certain company's request for approval for omission.<sup>102</sup> When the SEC responds, it only gives its opinion of whether the omission is appropriate.<sup>103</sup> Because of the great number of proposals submitted and the SEC's limited staff, the SEC reviews proposals quickly and informally and rarely gives detailed explanations for its decisions.<sup>104</sup> The SEC is not bound by positions

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<sup>95</sup> *Id.*

<sup>96</sup> *Id.*

<sup>97</sup> *See id.*

<sup>98</sup> *See* 17 C.F.R. § 240.14a-8(d).

<sup>99</sup> *See, e.g.,* Shoney's No-Action Letter, 1997 WL 9826, at \*33 (Jan. 10, 1997).

<sup>100</sup> *See id.* (as part of no-action letter, SEC writes that it "believes that its responsibility with respect to matters arising under Rule 14a-8 . . . is to aid those who must comply with the rule by offering informal advice and suggestions").

<sup>101</sup> *See* New York City Employees' Retirement System ("NYCERS") v. SEC, 45 F.3d 7, 12 (2d Cir. 1995).

<sup>102</sup> *See id.*

<sup>103</sup> *See id.*

<sup>104</sup> The SEC has enclosed a statement with its no-action letters emphasizing the informal nature of the shareholder proposal procedure. *See* Shoney's No-Action Letter, 1997 WL 9826, at

taken in no-action letters and is free to reverse its previous decisions.<sup>105</sup> Although no-action letters offer guidance to companies when assessing whether the SEC will take action against them for excluding a proposal, relying on a no-action letter can be dangerous.<sup>106</sup> Even though the SEC may state in such a letter that it will not recommend enforcement action against a company, it may still take action.<sup>107</sup>

Furthermore, no-action letters are not binding on the courts.<sup>108</sup> Because no-action letters are not adopted according to formal rule-making, they do not have a precedential value to which courts must defer.<sup>109</sup> Reliance on an SEC no-action letter may be risky for a company if a lawsuit is brought against it.<sup>110</sup> That a company omitted a proposal in reliance on a no-action letter is not a defense to a securities violation claim.<sup>111</sup>

In its review of employment-related proposals in no-action letters before 1992, the SEC decided on a case-by-case basis whether a proposal related to everyday operational decisions or involved a significant policy issue elevating it from the realm of the ordinary business exception.<sup>112</sup> The SEC consistently deemed proposals regarding such matters as employee health benefits, general compensation issues, management of the workplace, employee supervision, labor-management relations, employee hiring and firing, conditions of employment and employee training and motivation as falling within the ordinary business operations exception.<sup>113</sup> These proposals fit easily into the definition of ordinary business because they involved routine personnel matters and did not touch on significant social issues.<sup>114</sup>

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\*34. It states, "[i]t is important to note that the staff's and Commission's no-action responses to rule 14a-8(d) submissions reflect only informal views." *Id.*

<sup>105</sup> See *NYCERS*, 45 F.3d at 12.

<sup>106</sup> See *id.*

<sup>107</sup> See *id.*

<sup>108</sup> See *id.* at 13; *ACTWU I*, 821 F. Supp. at 885.

<sup>109</sup> See *ACTWU I*, 821 F. Supp. at 884-85. According to the SEC's Informal Procedures Statement, "[t]he determinations reached in these no-action letters do not and cannot adjudicate the merits of a company's position with respect to the proposal. Only a court such as a U.S. District Court can decide whether a company is obligated to include shareholder proposals in its proxy material." See Shoney's No-Action Letter, 1997 WL 9826, at \*34.

<sup>110</sup> See *ACTWU v. Wal-Mart Stores, Inc.*, 54 F.3d 69, 72 (2d Cir. 1995) (hereinafter "*ACTWU II*") (Wal-Mart's good faith reliance on SEC no-action letter did not bar plaintiff's award of attorneys' fees).

<sup>111</sup> See *id.*

<sup>112</sup> See Cracker Barrel No-Action Letter [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 77,287 (abandoning case-by-case approach and adopting a bright line standard).

<sup>113</sup> See United Technologies Co., SEC No-Action Letter [1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 76,635, at 77,701 (Feb. 19, 1993) (staff listing of excludable issues).

<sup>114</sup> See *id.*

The SEC, however, was not consistent in deciding whether issues of affirmative action and equal employment opportunity could be excluded as ordinary business.<sup>115</sup> In 1988, in a letter to American Telephone and Telegraph Co. ("AT&T"), the full commission affirmed a staff letter concluding that AT&T could not omit a proposal requesting the company to phase out its affirmative action program.<sup>116</sup> The SEC reasoned that because the proposal involved policy issues—an affirmative action program designed to give equal employment opportunities to minority groups and women—the proposal could not be excluded under 14a-8(c)(7).<sup>117</sup> Until April 1991, the SEC consistently determined that companies could not exclude proposals dealing with affirmative action and equal employment because those proposals involved policy concerns.<sup>118</sup>

In an April 1991 no-action letter to Capital Cities/ABC Inc., the SEC narrowed its position on affirmative action and equal employment opportunity proposals.<sup>119</sup> In an earlier letter to Capital Cities/ABC, the SEC decided that the company could not exclude a proposal requesting the company to disclose equal employment opportunity data and describe its affirmative action programs, stating that "questions with respect to affirmative action involve policy decisions beyond those personnel matters that constitute the Company's ordinary business operations."<sup>120</sup> Upon review of the letter by the full Commission, however, the SEC reversed the staff position.<sup>121</sup> It determined that because the proposal involved detailed information about the company's work force and employment practices, the proposal related to the company's ordinary business operations.<sup>122</sup> The SEC narrowed the applicability of its earlier stance and adopted a new position—that when a proposal

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<sup>115</sup> See Capital Cities/ABC SEC No-Action Letter [1990-91 Transfer Binder] Fed. Sec. L. Rep. (CCH) at ¶ 79,690, 78,120 (Apr. 4, 1991) (excluded); AT&T No-Action Letter, 1988 WL 235275, at \*15 (not excluded).

<sup>116</sup> See AT&T No-Action Letter, 1988 WL 235275, at \*14. Upon request, the SEC will reconsider a prior position taken in a no-action letter when the request for reconsideration is accompanied by material information that has not been furnished previously. See SEC Procedures for Staff Advice on Shareholder Proposals, Exchange Act Release No. 12,599, [1976 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 80,635, at 86,605-06 (July 7, 1976).

<sup>117</sup> See AT&T No-Action Letter, 1988 WL 235275, at \*15.

<sup>118</sup> See, e.g., Dayton Hudson Corp., SEC No-Action Letter, 1991 WL 178560, at \*9 (Mar. 8, 1991).

<sup>119</sup> See Capital Cities/ABC No-Action Letter, [1990-91 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 78,120.

<sup>120</sup> *Id.* at 78,119.

<sup>121</sup> See *id.* at 78,120.

<sup>122</sup> See *id.*

requests detailed information, the proposal relates more to everyday hiring and firing decisions than to policy matters.<sup>123</sup>

In another April 1991 letter to Wal-Mart Stores, Inc., the SEC further supported its position in Capital Cities/ABC.<sup>124</sup> Wal-Mart sought to exclude a shareholder proposal requesting information on the company's equal employment opportunities and affirmative action policies.<sup>125</sup> In its no-action letter, the SEC used similar language as in the Capital Cities/ABC no-action letter to approve the omission, stating that the proposal "involves a request for detailed information on the composition of the Company's work force, employment practices and policies."<sup>126</sup>

### C. *The Cracker Barrel Bright Line Standard*

The SEC resolved its difficulty in reaching consistent decisions when applying the ordinary business exception to certain employment-related proposals in no-action letters in 1992.<sup>127</sup> In a no-action letter to Cracker Barrel Old Country Stores, Inc., the Commission established a bright line standard for proposals involving employment matters.<sup>128</sup> That a company's employment policy is tied to a social issue no longer would remove the proposal from the realm of the ordinary business exception.<sup>129</sup>

In January of 1991, Cracker Barrel issued a press release stating its policy to deny employment to individuals "whose sexual preferences fail to demonstrate normal heterosexual values."<sup>130</sup> Following the announcement, the company fired a number of gay employees.<sup>131</sup> After public protests, pickets and boycotts, Cracker Barrel rescinded its anti-gay policy.<sup>132</sup> The company, however, did not include homosexuals in its anti-discrimination policy.<sup>133</sup>

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<sup>123</sup> See *id.*

<sup>124</sup> See Wal-Mart Stores, Inc., SEC No-Action Letter, 1991 WL 178759 (Apr. 10, 1991) [hereinafter Wal-Mart No-Action Letter]; Capital Cities/ABC No-Action Letter [1990-1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 78,120.

<sup>125</sup> See Wal-Mart No-Action Letter, 1991 WL 178759, at \*3.

<sup>126</sup> *Id.*; see Capital Cities/ABC No-Action Letter, [1990-1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 78,120.

<sup>127</sup> See Cracker Barrel No-Action Letter [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 77,287.

<sup>128</sup> See *id.*

<sup>129</sup> See *id.*

<sup>130</sup> *NYCERS*, 45 F.3d at 9.

<sup>131</sup> See *id.*

<sup>132</sup> See *id.*

<sup>133</sup> See *id.*

Cracker Barrel's actions prompted the New York City Employees' Retirement System ("NYCERS"), a pension system of city employees and a Cracker Barrel shareholder, to submit a proposed resolution requesting that management implement a nondiscriminatory employment policy based on sexual orientation and add prohibitions against such discrimination in the company employment statement.<sup>134</sup> The corporation submitted the proposal to the SEC, requesting the Commission's opinion as to whether the proposal could be excluded under the ordinary business operations exception.<sup>135</sup> On October 13, 1992, the SEC staff responded that the proposal could be omitted from the proxy material as ordinary business.<sup>136</sup>

The letter went further to establish the Commission's position on socially-related employment proposals in future no-action letters.<sup>137</sup> The staff decided that the line between social policy concerns and matters of everyday business had become too difficult to draw.<sup>138</sup> The Commission conceded that it lacked the resources and expertise to make such subjective determinations on important policy issues.<sup>139</sup> The letter stated, "the distinctions recognized by the staff are characterized by many as tenuous, without substance and effectively nullifying the application of the ordinary business exclusion . . . ."<sup>140</sup> Therefore, the Commission chose a bright line test for 14a-8(c)(7)—if a proposal is employment-based in nature, it falls within the ordinary business operations exception.<sup>141</sup> The SEC stated, "that a shareholder proposal concerning a company's employment policies and practices for the general workplace is tied to a social issue will no longer be viewed as removing the proposal from the realm of ordinary business operations of the registrant."<sup>142</sup> Thus, after Cracker Barrel, the SEC would allow companies to omit shareholder proposals even though they involved substantial policy concerns.<sup>143</sup>

In 1994, in *New York City Employees' Retirement System ("NYCERS") v. SEC*, the United States Court of Appeals for the Second Circuit

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<sup>134</sup> See Cracker Barrel No-Action Letter [1992-93 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 77,284-85.

<sup>135</sup> See *id.* at 77,285.

<sup>136</sup> See *id.* at 77,287.

<sup>137</sup> See *id.*

<sup>138</sup> See *id.*

<sup>139</sup> See Cracker Barrel No-Action Letter [1992-93 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 77,287.

<sup>140</sup> *Id.*

<sup>141</sup> See *id.*

<sup>142</sup> *Id.*

<sup>143</sup> See *id.*

upheld the position adopted by the SEC in Cracker Barrel.<sup>144</sup> After unsuccessfully petitioning the SEC to reverse the Cracker Barrel no-action letter, NYCERS, joined by the United States Trust Company and the Women's Division of the Board of Global Ministries of the United Methodist Church, sued the SEC, seeking to enjoin the Commission from following the policy announced in the no-action letter.<sup>145</sup> The plaintiffs challenged the new interpretation of 14a-8(c)(7), claiming that the Commission had established a legislative rule without subjecting the interpretation to notice and comment procedures and that the new interpretation was arbitrary and capricious.<sup>146</sup>

The court upheld the new SEC interpretation of 14a-8(c)(7), determining that the Cracker Barrel no-action letter was an interpretive rule, rather than a legislative rule, and therefore was not subject to notice and comment procedures.<sup>147</sup> According to the court, however, the Cracker Barrel no-action letter did not amend the legislative rule adopted in the 1976 Interpretive Release because it is an informal statement and has no binding authority.<sup>148</sup> Thus, courts will defer to the 1976 Interpretive Release, which stated that proposals involving substantial policy consideration were outside the realm of ordinary business matters.<sup>149</sup> The court further held that the no-action letter was not reviewable as an arbitrary or capricious action because the plaintiffs had an effective alternative to suing the SEC—they could institute a private action against Cracker Barrel under Rule 14a-8 enjoining the company from omitting their proposal in its proxy materials.<sup>150</sup>

Without interference from the courts, the SEC has consistently followed the standard adopted in Cracker Barrel in later no-action letters.<sup>151</sup> In a 1997 no-action letter to Shoney's, Inc., the SEC approved the company's omission of a proposal requesting that the company reveal equal employment opportunity data, any affirmative action programs, any litigation against the company involving race, gender and disabilities and any policy of purchasing goods and services from minority or female-owned businesses.<sup>152</sup> In another 1997 no-action letter

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<sup>144</sup> See 45 F.3d at 14.

<sup>145</sup> See *id.* at 7.

<sup>146</sup> See *id.* at 9.

<sup>147</sup> See *id.* at 12-13.

<sup>148</sup> See *NYCERS*, 45 F.3d at 14; 1976 Interpretive Release, 41 Fed. Reg. at 52,998.

<sup>149</sup> See *NYCERS*, 45 F.3d at 14; 1976 Interpretive Release, 41 Fed. Reg. at 52,998.

<sup>150</sup> See *NYCERS*, 45 F.3d at 14.

<sup>151</sup> See Cracker Barrel No-Action Letter [1992-1993 Transfer Binder] Fed. Sec. L. Rep. at 77,287. See, e.g., Rite Aid Corp., SEC No-Action Letter, 1998 WL 40240, at \*8 (Jan. 26, 1998); Texaco Inc., SEC No-Action Letter, 1997 WL 58881, at \*5 (Feb. 10, 1997); Shoney's No-Action Letter, 1997 WL 9826, at \*33.

<sup>152</sup> See Shoney's No-Action Letter, 1997 WL 9826, at \*31, 33.

to Texaco, Inc., the SEC concluded that a shareholder proposal requiring the company to adopt a policy to prevent discrimination and preferential treatment on the basis of race, sex or national origin could be omitted because it related to the conduct of the company's ordinary business.<sup>153</sup>

#### IV. CRITICISM AND PROPOSED REPEAL OF CRACKER BARREL

##### A. *Judicial, Congressional and Executive Criticism of Cracker Barrel*

Although the SEC continues to follow the rule established in Cracker Barrel, shareholders can force a company to include their employment-related proposal in the proxy materials by suing the company in federal court.<sup>154</sup> Although the language of Section 14(a) does not explicitly authorize a private right of action, the Supreme Court has held that private parties have a right to bring suit for violations of Section 14(a).<sup>155</sup> Despite the effort and expense of bringing a private action, shareholders have been successful in enjoining companies from omitting their proposals.<sup>156</sup>

In 1993, in *Amalgamated Clothing and Textile Workers Union ("ACTWU") v. Wal-Mart Stores, Inc.*, the United States District Court for the Southern District of New York held that, based on the 1976 Interpretive Release, a shareholder proposal regarding equal employment opportunity and affirmative action programs involved significant policy considerations and therefore did not fall within the ordinary business operations exception.<sup>157</sup> The plaintiffs, Wal-Mart shareholders, submitted a proposal to be included in the company's 1993 proxy materials, requesting the board of directors to report on the company's equal employment opportunity and affirmative action policies.<sup>158</sup> After receiving a no-action letter agreeing with the company's proposed omission, Wal-Mart excluded the proposal from its proxy material.<sup>159</sup> Plaintiffs sued Wal-Mart, alleging that the omission violated Rule 14a-8.<sup>160</sup> Wal-

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<sup>153</sup> See Texaco Inc., SEC No-Action Letter, 1997 WL 58881, at \*5.

<sup>154</sup> See *J.I. Case Co. v. Borak*, 377 U.S. 426, 430 (1964).

<sup>155</sup> See 15 U.S.C. § 78n(a); *Borak*, 377 U.S. at 430.

<sup>156</sup> See *ACTWU I*, 821 F. Supp. at 892; *NYCERS v. Dole Food Co.*, 795 F. Supp. 95, 101 (S.D.N.Y. 1992); *NYCERS v. American Brands, Inc.*, 634 F. Supp. 1382, 1392-93 (S.D.N.Y. 1986); *Lovenheim v. Iroquois Brands, Ltd.*, 618 F. Supp. 554, 562 (D.D.C. 1985).

<sup>157</sup> See *Amalgamated Clothing and Textile Workers Union v. Wal-Mart Stores Inc.*, 821 F. Supp. 877, 891 (S.D.N.Y. 1993); 1976 Interpretive Release, 41 Fed. Reg. 52,994, 52,998 (1976).

<sup>158</sup> See *ACTWU I*, 821 F. Supp. at 879.

<sup>159</sup> See *id.*

<sup>160</sup> See *id.*

Mart asserted that the proposal could be excluded because it related to ordinary business operations.<sup>161</sup>

In an opinion written by Judge Kimba Wood, the court refused to defer to the SEC no-action letter sent to Wal-Mart and the standard adopted in *Cracker-Barrel* and held that the proposal could not be excluded because it dealt with matters of social import.<sup>162</sup> In reaching this conclusion, the court relied on the 1976 Interpretive Release's definition of the ordinary business operations exception, rather than the interpretation adopted by the SEC in *Cracker Barrel*.<sup>163</sup> Because the Interpretive Release was subjected to formal notice and comment rule-making procedures, the court refused to defer to an inconsistent position taken in a later no-action letter.<sup>164</sup> According to the court, the SEC was free to abandon its interpretation taken in the 1976 Release, but it had to do so by following the appropriate procedures.<sup>165</sup> The court stated that until the SEC amended its rules through notice and comment procedures, courts should defer to the standard adopted in the 1976 Interpretive Release.<sup>166</sup> Therefore, the SEC position in *Cracker Barrel* did not completely eliminate shareholder access to proxy materials for employment-related proposals.<sup>167</sup>

The courts are not alone in their disagreement with the SEC interpretation of "ordinary business operations" in its no-action letters.<sup>168</sup> Congress recently mandated that the SEC conduct a study of the shareholder proposal process.<sup>169</sup> The National Securities Markets Improvement Act of 1996 required the Commission to conduct a study of (1) the impairment of shareholder access to proxy statements by

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<sup>161</sup> *See id.*

<sup>162</sup> *See ACTWU I*, 821 F. Supp. at 892.

<sup>163</sup> *See id.* at 890; 1976 Interpretive Release, 41 Fed. Reg. at 52,998.

<sup>164</sup> *See ACTWU I*, 821 F. Supp. at 890, n.13; 1976 Interpretive Release, 41 Fed. Reg. at 52,998.

<sup>165</sup> *See ACTWU I*, 821 F. Supp. at 890, n.13; 1976 Interpretive Release, 41 Fed. Reg. at 52,998.

<sup>166</sup> *See ACTWU I*, 821 F. Supp. at 892; 1976 Interpretive Release, 41 Fed. Reg. at 52,998.

<sup>167</sup> *See ACTWU I*, 821 F. Supp. at 892. On appeal in 1995, the United States Court of Appeals for the Second Circuit held that shareholders were entitled to an award of attorneys fees, even though their proposal was defeated at a previous annual meeting. *See ACTWU II v. Wal-Mart, Inc.*, 54 F.3d 69, 71-72 (2d Cir. 1995). The district court granted summary judgment for the shareholders and awarded them attorneys fees. *See id.* at 70. After the ruling, Wal-Mart included the proposal in its 1993 proxy materials and the proposal was defeated by approximately 90% of the voting shares. *See id.* at 70, 71. Wal-Mart appealed the award of attorneys fees, claiming that because the proposal was defeated, the litigation had not conferred a substantial benefit on the class members. *See id.* at 71. The Court of Appeals held that the promotion of corporate suffrage on a significant policy issue was a sufficiently substantial benefit to warrant an award of attorneys fees. *See id.* at 72.

<sup>168</sup> *See ACTWU I*, 821 F. Supp. at 892.

<sup>169</sup> *See* National Securities Markets Improvement Act of 1996, 15 U.S.C.A. § 78n (1997) (Study and Report on Shareholder Access to Proxy Statements).

recent statutory, judicial, or regulatory changes and (2) the ability of shareholders to have proposals relating to corporate practices and social issues included as part of the proxy statement.<sup>170</sup> The Commission must report back to Congress within a year with any recommendations for regulatory or legislative changes that it believes necessary to improve shareholder access to proxy materials.<sup>171</sup>

The executive department has also spoken out against the SEC's position in Cracker Barrel.<sup>172</sup> Former Secretary of Labor, Robert Reich, urged the Commission to reassess its interpretation of excludable shareholder proposals to include proposals relating to sweatshops and working conditions.<sup>173</sup> Reich stated, "there's a legitimate argument to be made that if a company is substantially involved in an important issue facing the country that transcends that individual company, shareholders ought to be permitted to vote on that company's role."<sup>174</sup> The former Secretary's statements were in response to a proposal relating to alleged sweatshop conditions at factories that produce Disney products.<sup>175</sup>

Even members of the SEC staff have pressured the Commission to repeal Cracker Barrel.<sup>176</sup> Former SEC Commissioner, Steven M.H. Wallman, openly criticized the SEC's stance on employment policies.<sup>177</sup> Wallman referred to continuation of Cracker Barrel as a "terrible mistake."<sup>178</sup> He stated, "Cracker Barrel is bad public policy because the wrong message is sent as to what the Commission believes is important."<sup>179</sup> Wallman considers discriminatory hiring policies to be an important public policy matter that should not be excluded from proposals because of the ordinary business exception.<sup>180</sup>

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<sup>170</sup> See *id.*

<sup>171</sup> See *id.*

<sup>172</sup> See Stuart Silverstein, *Votes on Employment Practices Urged Labor: Reich's Call to Involve Shareholders Could Heat Up Sweatshop Fight Between Disney, Brokerage*, L.A. TIMES, Nov. 5, 1996, at D2.

<sup>173</sup> See *id.*

<sup>174</sup> *Id.*

<sup>175</sup> See *id.*

<sup>176</sup> See Proposed Rules, Exchange Act Release No. 39,093, [1997 Transfer Binder] Fed. Sec. L. Rep. (CCF) at 89,882 (Wallman concurrence).

<sup>177</sup> See Rachel Witmer, *SEC Proposes Reversal of 'Cracker Barrel' In Revamped Shareholder Proposal System*, 29 Sec. Reg. & L. Rep. (BNA) No. 37, at 1285 (Sept. 19, 1997).

<sup>178</sup> Proposed Rules, Exchange Act Release No. 39,093 [1997 Transfer Binder] Fed. Sec. L. Rep. (CCF) at 89,883-84 (Wallman concurrence).

<sup>179</sup> *Id.* at 89,884.

<sup>180</sup> See *id.*

### B. *The Proposed Amendments*

In response to the criticism, in September of 1997, the SEC proposed new rules on shareholder access to proxy materials that would reverse its position in *Cracker Barrel*.<sup>181</sup> The SEC would no longer automatically exclude shareholder proposals involving employment practices under the ordinary business exception.<sup>182</sup> Instead, the SEC would return to its earlier practice of determining whether employment-related proposals could be excluded on a case-by-case basis.<sup>183</sup> The repeal of *Cracker Barrel* was proposed in a package of other proposed amendments to 14a-8.<sup>184</sup> Attempting to balance the interests of shareholders and companies, the SEC tied the repeal to other proposed reforms that would allow companies to exclude more proposals from the proxy materials.<sup>185</sup> The SEC is presently taking comment on the proposed repeal of *Cracker Barrel* and other 14a-8 reforms.<sup>186</sup>

## V. ANALYSIS

In light of the enormous costs of employment discrimination today, the SEC must reverse its position in *Cracker Barrel*.<sup>187</sup> *Cracker Barrel* rests on the assumption that all employment policies are ordinary business matters.<sup>188</sup> A policy that can potentially devastate the

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<sup>181</sup> See Proposed Rules, Exchange Act Release No. 39,093 [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 89,848.

<sup>182</sup> See *id.* at 89,858.

<sup>183</sup> See *id.*

<sup>184</sup> See *id.* at 89,849.

<sup>185</sup> See *id.* To accommodate corporate interests, the SEC suggested imposing stricter eligibility standards for submitting proposals, proposing that a shareholder must own \$2,000 in market value of the company stock, rather than \$1,000. See *id.* at 89,866. The proposed rules would change the requirements for resubmission of proposals that received an insignificant percentage of the vote in the previous year. See *id.* at 89,859. Under the new rules, a company could exclude a proposal if it failed to receive at least 6% of the vote on the first submission, 15% on the second and 30% on the third. See *id.* The current requirements are 3%, 6% and 10%. See 17 C.F.R. § 240.14a-8(c)(12). The SEC accommodated shareholder interests in addition to the repeal of *Cracker Barrel* by introducing an override mechanism. See Proposed Rules, Exchange Act Release No. 39,093, [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 89,860-61. The rule would allow shareholders to override a company's decision to exclude a proposal by mustering 3% of the company's share ownership. See *id.*

<sup>186</sup> See Proposed Rules, Exchange Act Release No. 39,093, [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 89,848.

<sup>187</sup> See *Cracker Barrel* No-Action Letter, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 77,287.

<sup>188</sup> See *id.*

financial condition of a company is hardly ordinary.<sup>189</sup> Although the proposed amendments call for the reversal of Cracker Barrel, the SEC does not go far enough to address the need for shareholder access to employment decisions.<sup>190</sup> Instead of adopting a bright line test to replace Cracker Barrel, the SEC currently proposes to return to the uncertainty of subjective determinations of social import by SEC staff members.<sup>191</sup> The SEC should adopt a standard that would include in the proxy materials shareholder proposals involving employment matters that can result in high stakes litigation and thereby harm the company's financial condition.

The numerous and expensive employment discrimination lawsuits against major corporations in recent years make apparent the need for reversal of the SEC position on employment-related proposals in Cracker Barrel.<sup>192</sup> It is difficult to reconcile the high stakes involved in employment litigation with the SEC belief that employment policies are ordinary day-to-day business matters.<sup>193</sup> As the Texaco and Shoney's cases indicate, employment discrimination lawsuits have the potential to seriously harm the financial condition of a company and diminish shareholder value.<sup>194</sup>

Because of the Civil Rights Act of 1991 and the ease with which plaintiffs can achieve class-action status, companies face the prospect of enormous damages in employment discrimination lawsuits.<sup>195</sup> For companies wishing to avoid the risk of unlimited damages and the negative publicity and costs of a trial, settlement payments can be staggering.<sup>196</sup> Although the payment of \$176.1 million to settle discrimination claims did not devastate Texaco, considering its size and revenues, the \$134.5 million settlement charge against Shoney's seriously affected the company's financial position.<sup>197</sup> Home Depot also reported financial setbacks after its settlement of a class action gender bias case.<sup>198</sup> Furthermore, employment practices may have adverse effects

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<sup>189</sup> See *id.*

<sup>190</sup> See Proposed Rules, Exchange Act Release No. 39,093, [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 89,857-58.

<sup>191</sup> See *id.*

<sup>192</sup> See Cracker Barrel No-Action Letter, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 77,287; Price, *supra* note 13, at A1.

<sup>193</sup> See Cracker Barrel No-Action Letter, [1992-93 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 77,287.

<sup>194</sup> See Church, *supra* note 15, at 38-39; Gaiter, *supra* note 29, at B4.

<sup>195</sup> See 42 U.S.C. § 1981a; Price, *supra* note 13, at A1.

<sup>196</sup> See Church, *supra* note 15, at 38-39; Gaiter, *supra* note 29, at B4.

<sup>197</sup> See Gaiter, *supra* note 29, at B4.

<sup>198</sup> See Bueno, *supra* note 53, at B18.

on stock values as evidenced by the performance of Texaco and Shoney's stock while the companies were immersed in lawsuits.<sup>199</sup> Employee morale may suffer because of a company's insensitive personnel policies, which can lead to decreased productivity.<sup>200</sup> The negative publicity emanating from employment lawsuits may also translate into losses in revenue.<sup>201</sup> The publishing of the audio tape transcripts of Texaco executives resulted in a national boycott.<sup>202</sup> When allegations were made public in the sexual harassment lawsuit against Mitsubishi, the picketing of dealerships and a nation-wide boycott soon followed.<sup>203</sup>

Because of losses in revenues stemming from consumer avoidance and negative publicity, companies may have to spend significant sums to repair their image after embarrassing lawsuits.<sup>204</sup> By 1996, Shoney's had spent almost two hundred million dollars since its 1992 settlement, pumping money into minority organizations, recruitment of minorities and minority salaries, in an attempt to erase the perception of Shoney's as a racist enterprise.<sup>205</sup> Furthermore, management must spend its time developing programs to improve public relations rather than running the company.<sup>206</sup>

Another possible result of an employment lawsuit is the loss of management control over employment decisions, which also can affect a company's condition.<sup>207</sup> For example, as part of the Texaco settlement, management gave up control over the company's personnel policies to an independent task force.<sup>208</sup> The financial consequences of recent employment litigation show that management's control of employment policies can affect the bottom line.<sup>209</sup>

Because employment policies have the potential to impact shareholder value adversely, the SEC must repeal its position in Cracker Barrel which currently denies shareholder access to the proxy materials on employment matters.<sup>210</sup> In Cracker Barrel, the SEC stated that it would consider proposals regarding employment practices within the realm of ordinary business.<sup>211</sup> In light of the recent employment litiga-

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<sup>199</sup> See Gaiter, *supra* note 29, at B4; White, *supra* note 8, at 34.

<sup>200</sup> See Wallman, *supra* note 62, at § 3, 12.

<sup>201</sup> See Gaiter, *supra* note 29, at B4; White, *supra* note 8, at 34.

<sup>202</sup> See White, *supra* note 8, at 33.

<sup>203</sup> See *Mitsubishi Picketing Concerning Lawsuits is Readied By Groups*, *supra* note 48, at B3.

<sup>204</sup> See Gaiter, *supra* note 29, at B4; Sullivan & Sharpe, *supra* note 2, at A3.

<sup>205</sup> See Gaiter, *supra* note 29, at B4.

<sup>206</sup> See Pulley, *supra* note 33, at A1; Solomon, *supra* note 1, at 49-50.

<sup>207</sup> See White, *supra* note 8, at 33.

<sup>208</sup> See *id.*

<sup>209</sup> See Church, *supra* note 15, at 38-39.

<sup>210</sup> See Cracker Barrel No-Action Letter, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 77,287.

<sup>211</sup> See *id.*

tion, this position cannot be sustained.<sup>212</sup> When the SEC adopted the ordinary business exception, it intended to relieve companies from shareholder interference in minor, day-to-day matters.<sup>213</sup> Decisions that can expose a company to a half-billion dollars in damages and intense public criticism are hardly minor or routine.

The ordinary business exception also is rooted in the belief that management has specialized talents and is more qualified than shareholders to make certain business decisions.<sup>214</sup> When a company faces decisions involving important policy issues, it is difficult to argue that management has more expertise than the owners of the company, especially in light of the allegations against top executives in the Texaco and Shoney's lawsuits.<sup>215</sup> Indeed, shareholders are just as qualified as management to make decisions on social policies like affirmative action and equal employment opportunity.<sup>216</sup> Management expertise and competence do not justify a categorical denial of shareholders' ability to take part in the company's employment policies.<sup>217</sup>

The costly discrimination lawsuits of recent years and their negative effects on shareholder value reveal the need for management accountability to ownership on employment policies.<sup>218</sup> The shareholder proposal process achieves accountability by forcing management to address employment issues.<sup>219</sup> It further provides shareholders with greater insurance that the company will not tolerate illegal practices and the resulting liability.<sup>220</sup> Proposals are a means for shareholders to communicate to management issues that they deem important for the company to address.<sup>221</sup> The reversal of Cracker Barrel may protect investors from a loss in shareholder value as a result of costly employment litigation by making management more accountable to owners regarding their workplace policies.<sup>222</sup>

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<sup>212</sup> See Price, *supra* note 13, at A1.

<sup>213</sup> See Medical Comm. for Human Rights v. SEC, 432 F.2d 659, 678-79 (D.C. Cir. 1970).

<sup>214</sup> See *id.*

<sup>215</sup> See *id.* at 681.

<sup>216</sup> See *id.*

<sup>217</sup> See *id.*

<sup>218</sup> See Gaiter, *supra* note 29, at B4; Price, *supra* note 13, at A1.

<sup>219</sup> Although shareholder proposals often fail to garner a majority of the ownership vote when placed in the proxy materials, the proposals communicate to management important issues that shareholders deem important. See Proposed Rules, Exchange Act Release No. 39,093 [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 89,877 (reporting a study finding that between January 1, 1997 and Sept. 18, 1997, only 19 out of 234 proposals gained shareholder approval).

<sup>220</sup> See Wallman, *supra* note 62, at § 3, 12.

<sup>221</sup> See Medical Comm., 432 F.2d at 680-81.

<sup>222</sup> See Cracker Barrel No-Action Letter, [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 77,287.

The SEC must reverse Cracker Barrel because its position is contrary to the Congressional intent behind Section 14(a).<sup>223</sup> The chief purposes of Section 14(a) are to encourage corporate suffrage and to protect investors.<sup>224</sup> Congress delegated to the SEC the power to adopt rules "as necessary or appropriate . . . for the protection of investors."<sup>225</sup> By prohibiting shareholders from having a say in employment policies, the SEC is not protecting investors.<sup>226</sup> Instead, the SEC leaves investors at the mercy of management to make decisions on employment policies that can seriously harm their investment.<sup>227</sup>

The SEC has recognized the need to reevaluate its position in Cracker Barrel.<sup>228</sup> Perhaps spurred by Congress's mandate in the National Markets Improvement Act of 1996 and the widespread criticism of Cracker Barrel, the SEC has proposed the repeal of its position which allows companies to automatically exclude employment-related proposals.<sup>229</sup> The proposed amendments that reverse Cracker Barrel, however, do not go far enough to ensure shareholder involvement in employment policies.<sup>230</sup> Although it appears that the proposed repeal of Cracker Barrel would expand shareholder access to proxy statements by allowing a broader range of includable proposals, there is no guarantee that employment-related proposals will be included.<sup>231</sup> Instead of adopting a bright line test to include employment-related proposals in proxy materials, the SEC proposed to return to a case-by-case determination of whether proposals are excludable.<sup>232</sup> The social significance of a proposal again would be decided based on an SEC staff member's subjective evaluation of the proposal.<sup>233</sup> Therefore, proposals involving important social issues could still be excluded under 14a-8(c)(7).<sup>234</sup>

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<sup>223</sup> See 15 U.S.C. § 78n(a); *J.I. Case Co. v. Borak*, 377 U.S. 426, 431-32 (1964); *Medical Comm.*, 432 F.2d at 680-81.

<sup>224</sup> See 15 U.S.C. § 78n(a); *Borak*, 377 U.S. at 431.

<sup>225</sup> 15 U.S.C. § 78n(a).

<sup>226</sup> See *Borak*, 377 U.S. at 431.

<sup>227</sup> See Church, *supra* note 15, at 38-39; Gaiter, *supra* note 29, at B4.

<sup>228</sup> See Proposed Rules, Exchange Act Release No. 39,093, [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,961, at 89,857-59 (Sept. 18, 1997); Cracker Barrel No-Action Letter, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 77,287.

<sup>229</sup> See 15 U.S.C.A. § 78n; Proposed Rules, Exchange Act Release No. 39,093, [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 89,849.

<sup>230</sup> See Proposed Rules, Exchange Act Release No. 39,093 [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 89,857-59.

<sup>231</sup> See *id.* at 89,859.

<sup>232</sup> See *id.* at 89,858.

<sup>233</sup> See *id.* at 89,883 (Wallman concurrence).

<sup>234</sup> See *id.* (Wallman concurrence).

For example, proposals requesting equal employment opportunity data and information on affirmative action programs could be excluded as they were in the Capital Cities/ABC, Inc. no-action letter before Cracker Barrel.<sup>235</sup> The SEC once again could reason that although the proposal involved a significant policy issue, the proposal was within the ordinary business operations exception because the information it requested was too detailed.<sup>236</sup> The proposed return to subjective decisionmaking by the SEC staff provides no assurances that proposals dealing with employment policies that could potentially harm shareholder value will be included on the proxy materials.<sup>237</sup> The proposed case-by-case approach to employment-related proposals will return the shareholder proposal process to the uncertainty of the pre-Cracker Barrel days.<sup>238</sup> Although questionable on policy grounds, the Cracker Barrel standard provided certainty for shareholders and companies as to the excludability of proposals.<sup>239</sup> Before Cracker Barrel, the SEC often reached inconsistent decisions in its no-action letters.<sup>240</sup> The SEC wavered on whether proposals involving affirmative action and equal employment opportunity data could be omitted under 14a-8(c)(7).<sup>241</sup> Instead of returning to a case-by-case approach, the SEC should amend 14a-8(c)(7) to provide certainty to the shareholder proposal process.<sup>242</sup>

Furthermore, the SEC should not return to case-by-case determinations of excludability because it is not the appropriate body to evaluate the merits of proposals that involve social issues.<sup>243</sup> The purpose of the SEC is to regulate the transfer of securities, not to evaluate the importance of social policy decisions.<sup>244</sup> In the Cracker Barrel no-action letter, the SEC admitted that it felt uncomfortable in its role

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<sup>235</sup> See Capital Cities/ABC No-Action Letter, [1990-1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 78,120.

<sup>236</sup> See *id.*

<sup>237</sup> See Proposed Rules, Exchange Act Release No. 39,093, [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 89,883 (Wallman concurrence).

<sup>238</sup> See e.g., Capital Cities/ABC No-Action Letter [1990-91 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 78,120 (proposal requesting information about company's affirmative action policy relates to ordinary business operations); AT&T No-Action Letter, 1988 WL 235275, at \*14 (proposal dealing with affirmative action did not relate to ordinary business operations because involved social policy issues).

<sup>239</sup> See Cracker Barrel No-Action Letter, [1992-93 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 77,287.

<sup>240</sup> See *supra* notes 115-26 and accompanying text.

<sup>241</sup> See 17 C.F.R. § 240.14a-8(c)(7); *supra* notes 115-26 and accompanying text.

<sup>242</sup> See 17 C.F.R. § 240.14a-8(c)(7).

<sup>243</sup> See Palmiter, *supra* note 78, at 905.

<sup>244</sup> See *id.*

of line drawing on proposals with social policy considerations.<sup>245</sup> The proposed amendments do not improve shareholder access to the proxy materials because they place proposals at the mercy of an agency that is not equipped and does not want to draw lines on social policy issues.<sup>246</sup>

Instead, the SEC must adopt a clear standard on employment shareholder proposals whereby if a proposal deals with employment decisions that can adversely impact shareholder value, the proposal does not relate to ordinary business and cannot be excluded under 14a-8(c)(7).<sup>247</sup> Employment decisions that have the potential to seriously harm the financial condition of a company no longer would be excluded under the false assumption that such decisions are ordinary.<sup>248</sup> Furthermore, this standard would not rely on subjective policy determinations by an SEC staff member.<sup>249</sup>

Such a standard would provide management accountability.<sup>250</sup> The ownership of a company would have an active role in major employment decisions that could seriously impact the company's financial condition.<sup>251</sup> Shareholders no longer would be excluded from employment decisions based on the false assumption that they lack the competence that management possesses to make such decisions.<sup>252</sup> If an employment policy decision could result in a financially damaging lawsuit, shareholders are just as qualified as management to be involved in those decisions.<sup>253</sup>

The standard I suggest would bring Rule 14a-8 back in line with the Congressional purposes of Section 14(a)—to protect investors and encourage corporate suffrage.<sup>254</sup> By presenting proposals on major employment policies, shareholders would have a voice in matters that can seriously harm their investment.<sup>255</sup> Furthermore, such a rule protects investors from the potential of costly lawsuits because of biased management decisionmaking on employment issues.<sup>256</sup> The standard I

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<sup>245</sup> See Cracker Barrel No-Action Letter, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 77,287.

<sup>246</sup> See Proposed Rules, Exchange Act Release No. 39,093, [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 89,857-59; Cracker Barrel No-Action Letter [1992-93 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 78,287; Palmiter, *supra* note 78, at 905.

<sup>247</sup> See 17 C.F.R. § 240.14a-8(c)(7).

<sup>248</sup> See *supra* notes 192-209 and accompanying text.

<sup>249</sup> See Palmiter, *supra* note 78, at 905.

<sup>250</sup> See *supra* notes 218-22 and accompanying text.

<sup>251</sup> See Church, *supra* note 15, at 38-39; Gaiter, *supra* note 29, at B4.

<sup>252</sup> See *Medical Comm.*, 432 F.2d at 248.

<sup>253</sup> See *id.*

<sup>254</sup> See 15 U.S.C. § 78n(a); 17 C.F.R. § 240.14a-8; *Borak*, 377 U.S. at 431.

<sup>255</sup> See *Borak*, 377 U.S. at 431.

<sup>256</sup> See Church, *supra* note 15, at 38-39; Gaiter, *supra* note 29, at B4.

propose would return the SEC to its proper role in adopting rules as "necessary and appropriate in the public interest and for the protection of investors."<sup>257</sup>

In addition, this standard would eliminate the uncertainty remaining after the Capital Cities/ABC no-action letter.<sup>258</sup> Proposals requesting information about a company's equal employment opportunity and affirmative action programs would not be excludable under this standard.<sup>259</sup> Because decisions on affirmative action and equal opportunity employment can result in financial and public relations setbacks, the proposals would not fall under the ordinary business exception.<sup>260</sup>

Although this standard would involve some line-drawing by the SEC on what employment policies could be harmful to a company, it would provide much more certainty than the subjective decisionmaking proposed in the amendments.<sup>261</sup> A case-by-case determination of the potential for costly lawsuits resulting from an employment policy involves more objective criteria than the determination of the importance of a social issue.<sup>262</sup> Furthermore, the SEC is more qualified and would be more comfortable in making determinations about the financial consequences of employment decisions than about social policy issues.<sup>263</sup>

## CONCLUSION

The need for the repeal of Cracker Barrel is apparent with the increased threat to shareholder value in recent years from costly employment lawsuits. The proposed reversal of Cracker Barrel and return to case-by-case determinations by the SEC staff is not the answer. Instead, the SEC should adopt a standard that would make shareholder proposals beyond the realm of the ordinary business exception when they deal with employment decisions that could result in loss in shareholder value.

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<sup>257</sup> 15 U.S.C. § 78n(a).

<sup>258</sup> See *supra* notes 115-26 and accompanying text.

<sup>259</sup> See *id.*

<sup>260</sup> See 17 C.F.R. § 240.14a-8(c)(7).

<sup>261</sup> See Proposed Rules, Exchange Act Release No. 39,093, [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 89,857-59.

<sup>262</sup> See *id.*

<sup>263</sup> See Cracker Barrel No-Action Letter, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 77,287; Palmiter, *supra* note 78, at 905.