WHAT YOU DON'T KNOW CAN HURT YOU: HUMAN RIGHTS, SHAREHOLDER ACTIVISM AND

Eric A. Engle
Introduction

The post-Soviet world shows a continued interest in the nexus of human rights and corporate misconduct. However, contemporary human rights advocates do not frame the debate about the relationship between corporations and human rights in Marxist terms. Instead, contemporary human rights advocates take a reformist approach - they try to reconcile corporate profitability and human rights. They do so in one of two ways.

The first reformist approach looks to the state to remedy the problem. But contemporary statists do not take the interventionist approach of managed economies, such as state-owned factories, wage and price controls, and interventionist monetary policies. That approach has been universally rejected since 1990 in Europe and since 1980 in the United States. Instead, contemporary statists limit state intervention to sanctions on trade and investment to punish unfair and substandard practices such as "social dumping." n1 The logic is that limited regulatory intervention should make human rights compliance profitable with the minimum distortion to the market. The second contemporary approach to remedying corporate human rights abuse focuses on developing governance mechanisms within the company that favor the best human rights practices. n2
Both of these approaches take capitalism as their starting point. Each has its advantages: they are complementary ways to build a better world. However, most existing literature either takes the state-centered approach or examines only non-binding corporate governance mechanisms, such as codes of good conduct and social audits. There is very little, if any, literature on the use of binding governance mechanisms such as shareholders' derivative suits to remedy human rights abuses, with the exception of class actions as a remedy to torts which are violations of international human rights law. n3

This paper seeks to remedy the absence of literature on shareholder activism and derivative suits as a governance tool to improve human rights. In so doing, it also presents an overview of the mechanics of internal corporate governance in U.S. companies. Near the conclusion, this paper [*66] briefly looks at human rights class actions to round out a brief comprehensive survey of binding corporate governance mechanisms which can be used to safeguard human rights.

This article concludes that though in theory shareholders have several ways to influence their corporation's behavior, in practice they generally cannot. This may explain the absence of literature on binding governance mechanisms to protect human rights: remedies which theoretically exist are ineffective in practice. To remedy this problem, this article recommends that the few existing mechanisms should be used whenever possible, reformed to become better, and that the SEC should require companies to report on their human rights, environmental, and labor relations practices because that information is material to investment decisions. The risks can be shown in terms of cold cash: corporations which violate human rights face higher insurance costs, lawsuits in tort and the risk of paying settlements or damages payments. Human rights abuse creates a riskier political climate which can cause rioting, leading to destruction of corporate property and the possible nationalization of business assets. Such risks are not just intolerable to individual investors; they also poison the capital market generally and discourage efficient capital formation. Companies which violate human rights laws risk investors' assets for questionable gains. They seek to externalize costs resulting in diseconomies to the detriment of the market. Given these concrete economic costs, investors have a right to know about the labor, environmental, and human rights practices of their company.

I. Shareholder Resolutions and Proxy Contests as a Tool for Human Rights

Most current research on corporate social responsibility seems to focus on voluntary codes of good conduct (COGCs) as the best way to get corporations to internalize norms and costs such as pollution or substandard work environments, which corporations currently externalize on indigenous persons overseas. I am skeptical about COGCs because if exploitation is profitable (and it is), then any corporation would be foolish to renounce profit particularly since its competitors would then exploit that opportunity. Corporations renouncing exploitation profits not only renounce a benefit; they also incur a detriment due to competitors who take advantage of exploitation. Despite these obvious economic facts, corporate COGCs are often (at best naively and at worst, cynically) proposed as one way to compel a corporation to act in a socially responsible manner. "Better than nothing, but not by much" would be a quick and brutal summary of the utility of non-binding codes. As if the economic facts (greed) [*67] and governance issues (the non-binding nature of voluntary proposals) were not enough, important limitations on shareholder activism as a tool to compel corporate responsibility (the essentially passive role of investors) indicate that shareholders will have great difficult imposing COGCs on an unwilling board. Rather than focus on COGCs (which I have examined elsewhere), n4 I would like to examine the shareholders' resolution, as this has received less attention - and might be more effective, at least in certain states - as a tool to influence corporate governance.

A. Definition of Shareholders' Resolutions

A shareholder resolution is a non-binding n5 suggestion n6 to the board of directors as to how it ought to function. At the shareholders' meeting, the shareholders elect the next year's board of directors. SEA section 14a requires certain corporations (essentially large, publicly traded corporations) to send out proxy materials in preparation for the annual shareholders' meeting, including certain (not all) shareholder proposals. n7 Section 14a also applies to special elections, i.e., a proxy fight for control of the company. n8 If a shareholder proposal is placed before shareholders in a proxy
Shareholders have been able to use shareholder proposals as a way to compel companies to include their human rights proposals, such as COGCs, in proxy materials. However, even if presented and passed, the board of directors is under no legal obligation to comply with a shareholders' proposal. Shareholder resolutions have been attempted in the human rights context, but generally have not been adopted by corporations. Such resolutions have, however, influenced state governments' investment policies. Socially responsible investing has had its best successes with pension funds, especially state-run pension funds, probably because pension investors are very risk-averse and contributions are made by employees. As to the corporation though, shareholder proposals are ordinarily non-binding, and thus, usually ineffective at shaping corporate policy. For this reason, the author is skeptical about shareholders' proposals as tools of governance. In order to understand the limits of shareholder proposals, we must examine the rights and duties of shareholders and the board of directors.

B. Why Shareholders' Resolutions are of Limited Utility to Control the Board of Directors

1. Practical Factors

Numerous practical reasons explain why shareholders have such limited influence on corporate policy. Nominating directors is costly. Shareholder "proposals must be submitted months in advance of the [shareholders'] meeting and may become outdated." The board may simply ignore the calls for proxy voting. Even if the shareholders manage to pass a resolution or bylaw, the corporation might either ignore it or move to repeal it. Limitations on the form of the proxy also explain my skepticism about their utility. The shareholder proposal must be 500 words or less, and there is no possibility to meet any rebuttal the corporation presents in the proxy materials, except to take up rebuttal at the shareholders meeting. Shareholders can use proposals to "nominate individuals for board positions, but such nominees do not need to be included in corporate proxy materials." Though Delaware is the extreme, under Delaware law, all propositions by shareholders must be approved by management, with the exception of election of directors and amendment of bylaws. Even without considering the substance of the shareholder proposal, we can see there are important process constraints that severely constrict the use of shareholder proposals as a tool for shareholder activism.

2. Role of Shareholders

The limitations on shareholder activism are also a result of the asymmetric roles of the management and the board of directors. The exact contours of these asymmetries are detailed especially in the following two sections.

a. Shareholders Elect the Board of Directors (On Paper)

The general principle is that "shareholders are entrusted with all powers which have not been conferred either to the board of directors or to other intra-corporate bodies." Such a reservation of powers seems wide-ranging on first glance. However, an examination of reality shows that virtually all powers are expressly conferred to the board of directors, particularly those that concern the day-to-day operation of the company. Thus, in practice, "shareholder power is essentially limited to voting on major decisions and electing and removing directors." Shareholders can elect and sometimes remove board members. Shareholders cannot, however, control the board of the corporation. One of the few ways that shareholders can exercise their limited power is to vote out the board of directors. In practice, however, even the election of the new board is determined by the existing board.

b. Shareholders May Not Amend the Corporate Charter

Not only is shareholder power over the day-to-day operations of the corporation essentially impossible, so also is it impossible for shareholders to directly amend the corporate charter. Shareholders do have a veto power over charter
amendments and reincorporations proposed by management. Amendments made by management must be approved by the vote of the shareholders. However, only the board of directors can initiate a charter amendment. Thus, amending the corporate charter requires cooperation of the directors because management is granted the power to veto charter amendments. Exceptionally, direct charter amendment may be possible for shareholders under state law, but that is not the case generally, and so charter amendment is an unlikely tool for legal reform.

c. Bylaws: In Some States Shareholders May Amend the Corporate Bylaws; In Others, They May Not

Though direct amendment of the corporate charter by shareholders is almost impossible, some states permit shareholders to initiate amendments to the corporation's bylaws; others prohibit them from doing so. A 1980 SEC survey determined that:

1. No state requires both board and shareholder approval. Depending on the statute, either the board or shareholders can amend bylaws without action from the other.

2. Thirty-two states have provisions which, though they vary widely in form, give shareholders the ultimate power to amend bylaws.

3. Twenty-two jurisdictions provide that the procedure for amending bylaws may be set forth in the charter or bylaws. The most common format vests power to amend in the board unless the articles reserve the power to the shareholders.

4. California allows either the board or shareholders to amend the bylaws. Shareholders cannot directly amend the charter, and can directly amend the corporate bylaws only in some states. This represents an important limit on shareholder activism.

   i. Shareholders' Proposals to Make Binding Bylaw Amendments

Even if a bylaw amendment were proposed by the shareholders and adopted by the board of directors, the board of directors may then try to repeal or amend that bylaw. Can a bylaw be proposed which purports to be unamendable? That question is unresolved. In New York, shareholders are statutorily permitted to amend or repeal the boards' bylaws. The argument could be made that it would be impossible for the board of directors to amend the bylaw introduced by the shareholders. However, the opposite proposition appears to hold for Delaware. As to those states, such as New York, which permit direct amendment of the bylaws by the shareholder proposal, the question remains whether and how shareholders might make their efforts irrevocable.

   ii. Irrevocable Bylaw Amendments?

Shareholder proposals submitted pursuant to SEC Rule 14a-8 must ordinarily be phrased only as recommendations, and not as commands. However, the SEC permits shareholder proposals for bylaw amendments to be phrased as commands, on the logic that most states permit both the board and shareholders to make bylaw amendments. Binding shareholders proposals to make bylaw amendments can be linked to the qualifications of a director or the nomination of a given director. Sometimes even the threat of a binding bylaw amendment to nominate a
director or require a director to have certain qualifications has been sufficient to change the corporate behavior. No company has challenged the use of bylaw amendments on substantive grounds. Thus, in those states where shareholders themselves can initiate bylaw amendments, an amendment likely can be made binding and can also be used to target existing or proposed directors for inclusion or exclusion from the board.

3. Role of Directors

The role of the directors is to manage the business and operations of the corporation. Just as the shareholders are nearly powerless, the directors are nearly all-powerful. For example, Delaware’s statutory law and the Model Business Corporations Act require amendments of the corporate charter to be initiated only by the board of directors.

Under the Delaware Code and the MBCA, charter amendments must be initiated and brought to a shareholder vote of approval by the board. Regardless of how many shareholders want a given charter amendment and of how long they have supported the amendment, shareholders may not vote on it unless the board first elects to have such a vote. Likewise, only the board may initiate a vote on a merger proposal.

Delaware law also makes clear that some changes in governance can only be made through the corporate charter and not by amending the corporation's bylaws. Shareholders have a right to veto or approve a proposed charter amendment initiated by the board of directors, but shareholders may not initiate a reincorporation in another state. Again, the levers of corporate control are clearly placed in the hands of the board of directors. In short, directors have wide ranging discretionary power:

As long as directors do not use their powers to line their own pockets, they enjoy legal discretion to run the firm pretty much as they please, including discretion to pursue corporate strategies that benefit nonshareholder groups at the shareholders' expense and over the shareholders' clear and unanimous objections. Thus directors legally can refuse to pay dividends; can reprice executives' options; can retroactively increase retirees' pensions; can shift to expensive but “socially responsible” production methods; and can even donate corporate funds to charity. If a firm’s shareholders pass a unanimous resolution requesting a board to stop doing such things, the board is free to ignore it. If the shareholders bring suit, the directors are protected by the business judgment rule.

The wide ranging discretion of the board of directors is also shown in that courts insulate most management decisions from accusations of ordinary negligence under the theory of the business judgment rule, which we now examine.

a. The Business Judgment Rule

The business judgment rule holds that a director will not be liable for their business decisions. The courts will not "second guess" ordinary managerial decisions as courts lack the necessary marketplace expertise and, in the final analysis, corporations are self-regulating. The business judgment rule shields the board of directors from the consequences of their own incompetence, on the logic that the board would otherwise be hamstrung and unable to act decisively to take advantage of corporate opportunities.

b. Exclusion of Shareholder Proposals Under Rule 14a-(8)(i)(7)

One of the powers of the board of directors is to exclude certain shareholder proposals from the corporation's proxy materials. The corporation can rightfully choose not to include a shareholder proposal with its proxy materials on the same logic as the business judgment rule. The role of the board is to set and direct corporate policy, whereas the role of shareholders is to provide capital, take profits, and select their agent, the board of directors.
requires inclusion of shareholder proposals in proxy statements. n53 However, there are numerous exceptions to the requirement of inclusion. The company can legally exclude shareholder proposals which are within the "ordinary business" of the corporation according to SEC Rule 14a-8(i)(7). n54 According to 14a- [74] 8(i), a company may exclude a shareholder proposal for any of the following reasons:

1. Improper under state law: If the proposal is not a proper subject for action by shareholders under the laws of the jurisdiction of the company's organization;

2. Violation of law: If the proposal would, if implemented, cause the company to violate any state, federal, or foreign law to which it is subject;

3. Violation of proxy rules: If the proposal or supporting statement is contrary to any of the Commission's proxy rules, including Rule 14a-9, which prohibits materially false or misleading statements in proxy soliciting materials;

4. Personal grievance: special interest: If the proposal relates to the redress of a personal claim or grievance against the company or any other person, or if it is designed to result in a benefit to you, or to further a personal interest, which is not shared by the other shareholders at large;

5. Relevance: If the proposal relates to operations which account for less than 5 percent of the company's total assets at the end of its most recent fiscal year, and for less than 5 percent of its net earnings and gross sales for its most recent fiscal year, and is not otherwise significantly related to the company's business;

6. Absence of power/authority: If the company would lack the power or authority to implement the proposal;

7. Management functions: If the proposal deals with a matter relating to the company's ordinary business operations;

8. Relates to election: If the proposal relates to an election for membership on the company's board of directors or analogous governing body;

9. Conflicts with company's proposal: If the proposal directly conflicts with one of the company's own proposals to be submitted to shareholders at the same meeting. n55

[75] Not only can management exclude a shareholder proposal, management can also insulate itself from a wrongful exclusion of a shareholder proposal by asking the SEC in a request for a "no-action" letter whether the exclusion of the
shareholder proposal from the proxy statement would be permissible. The SEC then tells the company whether or not it will take "no action" were the company not to include the statement in its proxy. Once again, it is clear that enormous power is placed in the hands of the board of directors as compared with the few and limited powers of the shareholders.

4. Proxy Costs

As noted, proxy contests (see infra, C1) are expensive, complicated, uncertain, and biased in favor of the board of directors. Under Delaware law and elsewhere, successful shareholder insurgents may be reimbursed for the costs of their proxy expenses. However in reimbursement of the costs of a proxy fight, the management, as always, has the advantage. Insurgents are only reimbursed if successful, unlike management, and insurgents are rarely successful. As a result, "corporate presidents usually control the selection of members of the board of directors." The corporate governance deck is largely stacked against shareholders. However, the Internet may provide some relief.

5. The Internet as Tool for Shareholder Activism: SEC Rules 13d and 14a-2

As shown, one of the limits on shareholder activism is the cost and timeliness of making a proxy contest or shareholder proposal. A way to reduce this cost and make the issue timelier is to use the Internet, where communication is instant, global, and virtually costless. A variety of shareholder activism-related websites exist. They are, however, subject to SEC regulation.

Ordinarily, shareholders can communicate freely with each other. However, the SEC closely regulates communications regarding proxy contests. SEC Rule 13d-1 is triggered when a shareholder or group of shareholders acquires more than 5 percent of a company's stock. Rule 13d imposes a filing obligation on the shareholders. The triggering group must submit a Schedule 13D to the SEC disclosing ownership information about the security. Rule 13d-1 is only triggered when the shares are purchased or held for a control-related purpose. Generally, the SEC requires submission of a proxy filing and disclosure document prior to solicitation of proxies. However, Rule 14a-12 permits solicitation prior to the final filing of the proxy statement provided that (1) the filing is finalized prior to first use, (2) disclosure of the participants or at least information where information about the participants can be found, as well as a statement that shareholders should read the final proxy statement when it appears and that the proxy statement and other relevant documents will be able to be viewed on the SEC's website, and (3) actual delivery of the proxy card and necessary supporting documents to the shareholder for their decision must occur only after the delivery of definitive proxy statements. Shareholder activists should note that they can reduce their costs and the difficulties of communicating with other shareholders using the Internet, but must be careful to observe the formalities of Rule 14a-12. That rule eases some of the practical burdens of proxy solicitation, but in no way removes the formal legal requirements nor addresses all asymmetries of the shareholders versus the board of directors.

C. Proxy Contests

1. Definition of Proxy Fight

A proxy fight is a contest for corporate control. Each contestant tries to persuade shareholders to designate proxies to vote at the shareholder's meeting who will favor their position. As noted earlier, proxy fights are closely regulated by the SEC under the 1934 Act and Rule 14a, which seek to prevent false or misleading proxy statements. Also noted earlier, shareholders can use a proxy contest to promote a (likely ineffectual) shareholder proposal or, they can go for the jugular and seek to change the composition of the board of directors. We now explore the second possibility.

2. Description of the Proxy Fight
As mentioned earlier, management mails the proxy form (the proxy card) along with a proxy statement (where the shareholder's 500-word proposal would appear, and any company-issued rebuttal) along with the company's annual report prior to the annual shareholders meeting. A proxy card consists of a checkbox which the shareholder can tick to approve the corporate nominees or another checkbox to withhold their vote. The proxy form authorizes the designated proxy to vote the shares of the shareholder in a certain manner.

Because proxy contests are expensive and uncertain, they are also rare. "Activists have launched an average of twenty-five proxy contests a year since 1996, and most such contests have involved relatively small companies." Yet again, the few theoretical remedies for shareholders are in practice ineffective.

**D. Corporate Democracy?**

1. **The Critique of Corporate Democracy**

As we have seen, corporate power is decisively placed in the hands of the board of directors, leaving shareholders little or no say in how their investments are used. The one-sided nature of corporate structure naturally leads to criticism. One author writes, "despite the formal trappings of corporate "democracy,' directors have far more power over election outcomes than shareholders do. At election time, the incumbent board typically nominates a slate of candidates without input from shareholders... corporate law discourages shareholders from mounting opposition campaigns." There is much truth to such critiques of corporate democracy. However, the wide-ranging discretionary power of management is nonetheless subject to the scrutiny of the court of equity, as always the last refuge of the powerless. Accordingly, we consider what remedies equity may provide shareholders who are practically disenfranchised, whether through operation of law or illegally.

2. **Equity as a Response to the Critique of Corporate Democracy**

Courts can and do constrain the corporation to act fairly using their powers as courts of equity: "Inequitable action does not become permissible simply because it is legally possible." Although the burden is on the plaintiff to show an act of the directors was inequitable and amounted to, for example, waste, fraud or abuse, that burden can be met, at least in theory, provided the other procedural restrictions on equity are met (e.g., the legal remedy must be inadequate, the plaintiff herself must have acted equitably, and the plaintiff must act in a timely fashion).

3. **Praxis: Shareholder Proposal Cases**

Despite the possibility of equitable remedies, the deck seems stacked against shareholder activism at least in theory. How does this work out in practice? There are few litigated cases on shareholder activism for human rights. However, those few cases seem to verify the impression that the law here favors the incumbent board of directors.

An early example of a corporation successfully refusing to include a shareholder proposal was Peck v. Greyhound Corp. The Greyhound company had a problem with black and white persons - namely, it segregated according to race. Though Greyhound has since changed its policy, it did successfully refuse to include a shareholder proposal condemning segregation on its busses. Apparently "leave the driving to us" once meant "get in the back of the bus." In the rather famous case of State ex rel. Pillsbury v. Honeywell, Inc., a shareholder whose purpose was political, not pecuniary, was denied the right of inspection of the company records (see infra, II A). In contrast, in 1970, the Medical Committee for Human Rights, an antiwar organization, forced Dow Chemical to include in its proxy statement the committee's proposal that Dow no longer manufacture napalm. The proposal received less than 3 percent of the votes cast. The few litigated cases on the use of shareholders' proposals as a tool for human rights favor corporations and incumbent boards of directors.

**II. Company Disclosure**
A. The Shareholder's Right of Inspection: A Discovery Tool

One of the few tools which shareholders can effectively use to discover and expose human rights abuse by corporations is the shareholder's right to inspect corporate records. The shareholders of a corporation have a near absolute right to inspect just about any corporate record relevant to their investment decision. Indeed, "in a majority of jurisdictions, statutes require that the person seeking the examination be a shareholder, make their demand in writing, at a reasonable time, and for a proper purpose." A political purpose generally is not proper, but an economic one is. The way around the problem is to point out the fact that a corporation which aids and abets human rights abuse exposes the company to higher insurance costs and the risk of lawsuits, thus negatively affecting present and future dividends. A positive correlation between human rights compliance and stock market performance has been shown to exist. Thus records regarding human rights are material to investment decisions. Once inspection is permitted, it may turn up false or misleading statements. If any of the inspected documents are false or misleading, and if the material might support a 10b or 10b-5 action, (especially if causation was also shown, which will be presumed in a 10b-5 class action under certain conditions), then those corporate records are relevant. They would thus be subject to disclosure, which would influence the company's profitability.

Where a corporation refuses to permit inspection of its records, the proper remedy is to seek the writ of mandamus in a proceeding before the court of equity (in New York, mandamus is statutorily replaced by a CPLR Art. 78 proceeding which closely resembles mandamus). The shareholder need not indicate with specificity the particular books or records to be inspected. Corporate records covered include not merely ledgers of accounting but also contracts, expense accounts, insurance documents, tax records, and even correspondence. Trade secrets, however, are not ordinarily subject to the right of inspection, though confidential communications or trade secrets which affect the financial status or value of shareholder stock may be subjected to the shareholder's right of inspection. Shareholders are also entitled to lists of other shareholders. A corporation holding shares in another company enjoys the right to inspect the records of the other company, as may shareholders of the parent; they may inspect the records of the wholly-owned subsidiary.

The source of the shareholder's right of inspection is in the agency relationship of shareholder to director as well as in a property interest of the shareholder. The right of inspection cannot be abolished or restricted by the corporation's charter or bylaws. Yet the proper purpose must be economic, not political. That is, of course, the greatest challenge in human rights activism. However, by pointing out that human rights non-compliance places the company at risk for expensive litigation and attendant settlements or payouts, by demonstrating the positive correlation between human rights compliance and stock market performance, showing that some investors use human rights as one factor in screening stocks as well as showing the higher insurance premiums and risks of rioting or nationalization that accompany corporate noncompliance with foreign and international human rights laws, the nexus between profitability and human rights compliance can be proven theoretically and empirically.

The right of inspection is not the only disclosure obligation of the corporation. The SEC also imposes affirmative duties on certain corporations to disclose financial and non-financial information about corporate operations.

B. SEC Disclosure Rules

Section 14a of the Securities Exchange Act of 1934 ("Exchange Act") allows the SEC to require disclosure "as necessary or appropriate in the public interest or for the protection of investors.

There are several arguments in favor of broad-reaching corporate disclosure requirements. One is that disclosure permits corporate self-regulation. Another is that it allows for efficient capital allocation. Yet another is that disclosure attracts foreign capital - full disclosure makes U.S. capital markets more honest and thus more attractive than
foreign capital markets which are at times less than transparent. n115

1. Who Must Disclose?

Companies whose securities are traded on any exchange must disclose their information. n116 Over-the-counter stocks (NASDAQ stocks) with more than 500 shareholders and 10 million dollars worth of assets must also disclose. n117 Debt instruments subject to registration requirements under the "33 Act must disclose unless there are fewer than 300 bondholders of record. n118

2. When Must Disclosure Occur?

The SEC requires disclosure of issues that the SEC regards as material to investors n119 "upon issuance of stock, quarterly and annually after issue, upon the happening of extraordinary events, and in conjunction with the annual shareholders' meeting." n120

3. What Must Be Disclosed?

The SEC can require disclosure to promote the public interest, to [*83*] protect investors or to achieve the goals of SEC statutes. n121 Some distinguish between financial information - data that reflects the extent to which a company is profitable - and social information which bears on how the company generates profits. n122 In all events, the SEC clearly requires disclosure of both financial and nonfinancial information.

a. Mandatory Disclosure of Financial Data

A rough and quick synopsis of the financial data disclosure requirements would look at the Generally Accepted Principles of Accounting ("GAAP"). Financial data that companies must disclose include those basic statistics found in any regular corporate accounting. n123 This obviously includes, but is not necessarily limited to, information on sales, income and losses from continuing operations, assets, debt, leases, stock and dividends per share. n124 "When in doubt, disclose" is a prudent adage of securities law.

b. Mandatory Disclosure of Nonfinancial Data

Nonfinancial data that must be disclosed include information on the business challenges and market conditions facing a company, n125 composition and compensation of management and the board, n126 litigation facing the company, n127 and trends and events likely to affect the company's financial results. n128 Human rights disclosure falls under Regulation S-K items 101 and 103. n129 The SEC already requires disclosure about a company's environmental liabilities as well as its relationships with employees. n130 This is "because corporate environmental and equal [*84*] employment opportunity practices may have economic impacts, [and therefore] disclosure of this information is within the public interest and protects investors." n131 Thus, it is no great leap to see that the SEC will likely recognize the materiality of human rights compliance or lack thereof to investor decisions. A company that abuses workers overseas is likely to abuse shareholders at home.

4. Human Rights Disclosure

Currently, the SEC does not generally require disclosure of compliance with foreign or international human rights or labor laws, n132 though that may change as an increasing number of investors find such information relevant to their investment decisions due to the risks of tort liability, insurance costs or nationalization of foreign held corporate assets. n133 However, "although the SEC does not require disclosure of information related to human rights, overseas labor, and related social issues, [transnational corporations] have already been voluntarily releasing such information, primarily in an effort to improve public relations and attract consumers and investors." n134 Just as one can distinguish between financial or non-financial information, one can also distinguish between mandatory and voluntary disclosure,
which we now examine.

a. Mandatory Disclosure of Human Rights Information

The SEC does require company disclosure in at least one human rights context. Companies with investments in foreign countries on a State Department "blacklist" must disclose that they do business with countries regarded as unfriendly by the United States. n135 One could argue that the membership in this blacklist is determined not by human rights concerns but rather by realpolitik concerns (most blacklisted countries are in the Islamic world) - but Burma is also on the list. Burma has oil. If realpolitik were the only concern of the State Department, Burma would not be blacklisted. Even if realpolitik were the only concern, disclosure of human rights information in one field will likely have a ripple effect elsewhere. n136

b. Voluntary Disclosure of Human Rights, Labor, and Environmental Information

Though the SEC does not generally require disclosure of compliance with foreign and international human rights laws, as a result of a combination of shareholder proposals, market conditions and state pressure, companies sometimes do adopt sustainable environmental and human rights policies. At the state level, the Organisation of Economic Cooperation and Development ("OECD") and the International Labor Organization ("ILO") also propose non-binding guidelines to states for socially responsible corporate governance. n137 The non-binding UN Global Compact also aims to "encourage businesses to "embrace and enact" human rights provisions. n138 At the corporate level, the U.N. Global Compact, AccountAbility 1000, n139 Social Accountability 8000, n140 and Sustainable Reporting Guidelines developed by the Global Reporting Initiative n141 create frameworks for sustainability accounting. n142 Corporate disclosure has thereby expanded from accounting and antitrust into human rights, labor and environmental issues. n143 Some sustainability reporting requirements in a few countries are in fact mandatory, n144 but most "triple [*86] bottom line" accounting is voluntary. n145 Yet, though generally voluntary, "almost half of the 100 largest companies in the world have adopted some form of a sustainability report" in their annual reports within these frameworks. n146 Today companies like Procter & Gamble, General Motors and Nokia issue sustainability reports because they know being seen as a polluter or exploiter is bad for business. n147 Disclosure of environmental factors has been driven forward by environmental law, the potential application of SEC disclosure rules and the profit motive (public relations). n148 Those enterprises that will not lose profits by adopting codes likely will. Of course, those enterprises that require regulation are the ones that will not adopt codes. This explains why, despite the interest of some [*87] enterprises to adopt COGCs, I am skeptical about their utility as a regulatory tool.

Sustainability or "green" reports issued by companies describe the company's environmental, labor, and human rights practices. Sustainability reports typically contain: (1) a general mission statement defining the company's goals and ethics, (2) specific issues that are of particular relevance to the company, and (3) a statement regarding enforcement and compliance mechanisms. n149 Green reports are typically unaudited and highlight the corporation's good deeds. n150

C. The Use of SEC Rule 10b-5 to Vindicate Human Rights Claims

Though sustainability reports generally are made pursuant to non-binding law and are usually unaudited, they are nonetheless statements made by the corporation and thus subject to SEC Rule 10b-5: "Rule 10b-5 requires veracity in corporate statements, even when there is no affirmative duty to disclose such information, the rule reaches a broader cross-section of corporate statements than those required in the periodic and annual statements." n151 A false or misleading material statement in a sustainability report could thus constitute a violation of SEC Rule 10b-5 and give rise to an attendant private cause of action. n152 What, then, are the elements of a private claim under 10b-5?

1. Elements of a Private Claim Under Rule 10b-5

The Exchange Act, section 10, provides a general anti-fraud provision concerning stock transactions. n153 Rule 10b-5,
enacted pursuant thereto, permits victims of false or misleading statements which result in damages [*88] to recover against the perpetrator of stock fraud. n154 The plaintiff must show that the defendant was subject to Rule 10b-5, that there was a false or misleading statement as to a material fact made recklessly or with intent to deceive, and that the plaintiff relied on this misstatement in connection with either the purchase or sale of a security. n155 The private plaintiff must also show that they purchased or sold the security at the time and "in connection with" the false or misleading fraudulent statement. n156 As a misrepresentation must be material to be actionable, a brief examination of the materiality requirement is in order.

2. Materiality

False or misleading statements of the corporation must be material to be actionable. n157 Materiality is generally defined as that which would affect profitability, that is, the decision of a reasonably prudent investor. n158 Compliance with international human rights and labor standards is [*89] generally deemed immaterial. n159 However, as companies internalize risk factors, whether by the increasing application of human rights laws to their activities, by insurance, by tort payouts or by outright nationalizations of their foreign assets, investors will recognize that human rights non-compliance represents a significant and largely preventable financial risk, and thus alter their investment patterns accordingly. It is already admitted that environmental risks can be material. n160 Further, some investors prefer to make a lower return on an investment they regard as ethical - including large, risk averse pension funds! Imagine an investor in a sustainable environment fund who discovered that the companies in which the funds invested in fact systematically lied about polluting activities. That would be clearly fraudulent: a misrepresentation of a material fact made with knowledge of falsehood, intended to induce reliance, in fact inducing reliance and resulting in injury. n161 After all, some injuries are non-pecuniary.

D. False Advertising

False advertising can of course be a tort - the tort of deceit. The elements of the tort of deceit are black letter law: (1) A misrepresentation (statement or omission!) of (2) a material fact (3) made with recklessness or knowledge of falsehood (4) intended to induce reliance which (5) actually induces reliance (causation). n162

The most famous human rights case involving false advertising was Kasky v. Nike, Inc.. n163 In that case, Nike was accused of making false and misleading statements about the conditions of labor in its offshore factories and was sued for false advertising. n164 The case nearly went before the Supreme Court but ultimately Nike settled. n165 The settlement alone cost the company, and thus the shareholders, over one million dollars. n166 [*90] Including the costs of attorneys, the action likely cost Nike at least two million dollars. n167 Would this affect your investment decision?

In the 10b-5 context however, advertising not only must be false, it also must be material to the investment decision. n168 Thus, though state consumer anti-fraud statutes may be available, a 10b-5 action will not necessarily also be available. As always, plaintiffs must plead facts to show the desired remedy with sufficient specificity to avoid directed verdict and summary judgement! In my limited survey of U.S. human rights cases, winnable cases are often lost not due to some capitalist cabal, but because of bad pleading!

E. An Activist Strategy

Given the limitations of shareholder activism and the possibilities of the Exchange Act, section 10 and Rule 10b-5 as a basis for action, a very sensible activist strategy would be to introduce a shareholder resolution to require "triple bottom line" sustainability reports. The board might not want to adopt such a resolution, but why wouldn't they? What board of directors could successfully oppose increased standards of accountability or fairness? Once adopted, if the resolution were ignored, the shareholders would have at least a derivative claim for enforcement of the accounting provision. Further, if false or misleading material statements were made in the accounting provision, a 10b-5 the shareholder might have a direct action under SEC Rule 10b-5. Such claims would be enforced either using a direct or derivative lawsuit against the corporation by the shareholders or against the board of directors by the shareholders on behalf of the
company. We now examine shareholders' direct and derivative lawsuits.

III. Lawsuits By or On Behalf of the Company

Lawsuits may also be used to compel corporate action. There are two types of lawsuits that may be instigated by shareholders, direct and derivative. A direct action is one brought by the shareholder herself on her own behalf. A derivative action is an action brought by a shareholder on behalf of the company. Whether an action is direct or derivative depends on who was injured (the corporation itself or the individual shareholder?). A derivative action is only appropriate where the corporation itself is the injured party. A direct action is only appropriate where an individual shareholder alleges a specific personal injury. The fact that the right vindicated lies with a different person in each case conditions the substantive remedies and procedural process which must be taken in each. Thus, they are separately considered.

A. Derivative Claims

1. The Shareholder's Derivative Suit is an Action in Equity

The shareholder's derivative suit is an action in equity for the shareholder compels a specific act using the writ of mandamus (or, in New York, Art. 78, CPLR). "A shareholders' derivative suit is an equitable device through which shareholders can enforce the corporation's rights if the directors are unwilling or unable to do so, and thereby indirectly protect their interests in the corporation." A derivative suit is "particularly useful when corporate insiders, such as directors and officers, are the potential defendants" - shareholder derivative actions are often a good remedy to a breach of fiduciary duty by the board. Though the remedy is in equity, there is nonetheless a right to a jury trial where the corporation would, had it sued in its own right, have had recourse to a jury.

2. Exhaustion/Demand Requirement

Because the derivative action is brought on behalf of the corporation, the shareholder must exhaust all remedies within the corporation before proceeding to the courts. Thus, in a derivative action, the plaintiff must first make a demand on the board of directors to remedy the injury; that is, they must exhaust the remedies within the corporate structure before going to the courts for redress. Of course, if such remedies would be futile the court may excuse the shareholder from exhausting all remedies which though theoretically available are not practically available, as for example might be the case of a dissident minority shareholder. Since the derivative action is that of the corporation itself, opposition to the derivative action by a majority of shareholders will ordinarily block the derivative remedy's availability. Of course, fraudulent or abusive majority shareholder conduct will not escape the equity court's attention.

3. Security Expenses

One limit on suing the corporation, is "security for expenses" statutes. "Security for expenses" statutes oblige shareholders to post bond prior to litigating the derivative suit. The plaintiff must have owned the shares at the time of the injury. This is one more limit on possible shareholder activism.

B. Direct Claims

The direct claim is brought by the shareholder herself for some injury suffered by the shareholder personally. Denial by the corporation of the shareholder's right to vote their shares, corporate failure to enforce voting rights, corporate denial of preemptive rights, corporate denial of the right of the shareholder to inspect corporate records as corporate denial of rightful dividends all raise the right to make a direct claim against the corporation. Of course, a derivative claim may be litigated as a class action. Note also that the same cause of action may be brought as a direct or a derivative action. Plaintiff will not be precluded from bringing a direct action where they
could have brought a derivative action. n192 For example, a claim that the company, by violating human rights laws exposed the company to risk resulting in increased insurance premiums, potential lawsuits and a diminished stream of future dividends would be a possible direct claim, though so speculative as to be unlikely accepted by the court. As elsewhere in law, claimants must plead and prove facts with specificity to win and can plead in the alternative.

Though limited by "security for expenses" statutes, shareholders direct or derivative lawsuits may be one way to compel the corporation to act responsibly. Note also that a lawsuit against the company may be brought as a class action which we now examine briefly discuss in order to round out this survey.

IV. Class Actions

Class actions occur in both human rights litigation (mass torts) and in shareholder's derivative actions. The class action, its advantages, disadvantages and suitability to litigation of human rights actions has been treated at length by many others. I only describe the black letter law briefly to round out this survey and refer the reader to other authors who treat the subject of the human rights class action or the class action in shareholder' derivative actions in greater depth.

To bring a class action the class must be so numerous as to make joinder impractical. n193 There must be common questions of law or fact throughout the class. n194 The defendants' claims or defenses must be typical as to all class members. n195 Finally, the litigants must fairly and adequately [*94] protect the interests of the class. n196 All these conditions can hold both for injury to a group of shareholders and to victims of mass torts overseas.

Though there is extensive literature on class actions in both the context of shareholder's derivative suits (typically, a 10b-5 action) and in the context of the mass tort which is also a violation of human rights law (typically, the Alien Torts Statute ("ATS") and/or the Torture Victims' Protection Act ("TVPA")), few have treated the subject of the interaction of the shareholders' derivative class action and the human rights' class action. This is because practical reasons indicate that it is unlikely that both the mass tort victims overseas and the tortiously injured shareholders will litigate their actions in one proceeding. Alien tort victims are unlikely to be shareholders of record at the time of the injury. Even if shareholders of record at the time of injury were friendly to the tort victims overseas there would not be enough commonality of facts, law, and class interests to justify proceeding in one action. True, the injured shareholders and victims might have common issues as to causation of their injury - but the nature and extent of their injury, one pecuniary, the other physical - explains why a class action would be improper.

Class actions have the disadvantage that different members of the class may have competing interests n197 which can result not only in practical tactical problems but also limitations on the applicability of the class action: Litigants may well be of diverse citizenship implicating the interpretation of numerous potentially conflicted laws. n198 Partial certification in such cases is of course only a partial solution. n199 Further, like the Alien Torts Claims Act ("ATCA"), the class action was not designed with the intent of being used as a tool for litigation of human rights claims of injured groups limiting the possibility of combining human rights provisions such as the ATCA with Rule 23 class actions. n200

Despite the limitations of both the ATCA and FRCP 23 as tools to remedy human rights violations, these are the principal tools for litigating human rights claims because few, if any, other laws are available. Courts have, in fact, used their equity powers to adapt these instruments to avoid [*95] procedural injustice, for example by allowing equitable tolling of statutes of limitations in cases of human rights violations. n201 Thus, despite their limitations, human rights advocates have been able to use class action techniques to human rights claims. n202 Thus human rights class actions under FRCP 23 will not go away and will likely increase, n203 all the more so because of globalisation. However human rights litigation - trying to cure a damage incurred - could be avoided entirely by increasing corporate disclosure requirements to signal both the board of directors and the shareholders as when the corporate board makes risky ill-advised investments that also are violations of human rights laws whether domestic, foreign, or international.

Conclusion and Recommendations
This article has attempted to present an inventory of possible remedies for shareholder activists. The shareholder's right of inspection is the easiest and perhaps most effective tool since it can be used to ferret out the extent of a company's human rights abuse. Shareholder resolutions are a theoretical possibility, but in practice are very limited. Proxy contests are even less likely to succeed in effectuating corporate change. On the other hand, the shareholders likely could compel their company to undertake social responsibility accounting ("triple bottom line"). Any material misstatements there could result in liability under SEC Rule 10b-5. Further, advertising law may provide remedies for human rights fraud. Finally the shareholders can bring their grievances either as direct or derivative suits and use joinder and class action to pool their claims.

There are only a few effective remedies for shareholder activists but there are some. Three remedies not considered here are (a) suing in tort using the ATS and the TVPA, and (b) suing using Racketeering Influenced Corrupt Organizations Act ("RICO"), and (c) remedies under criminal law such as the writ of quo warranto - whether foreign, national, or international. The reason is that the author has considered the ATS, the TVPA n204 and RICO n205 elsewhere. Those remedies, though not considered [*96] here, must nevertheless be considered by lawyers.

To conclude, the normative recommendation of this article is for the SEC to require reporting as to corporate compliance with foreign and international human rights laws as such information is more than tangentially relevant to the risks and profitability of a firm. The reason is that an ounce of prevention is worth a pound of cure. Rather than letting boards keep investors in the dark and subject their investments to unnecessary risks (insurance costs, riots, nationalizations, paying out on tort settlements and judgements) the SEC could simply require social disclosure and thereby prevent expensive and interminable human rights class actions.

Legal Topics:
For related research and practice materials, see the following legal topics:
Business & Corporate Law
Corporations
Directors & Officers
Management Duties & Liabilities
General Overview
Business & Corporate Law
Corporations
Directors & Officers
Scope of Authority
Limitations
Business & Corporate Law
Corporations
Shareholders
Meetings & Voting
General Overview

FOOTNOTES:

n1. "A general definition of "social dumping' is suggested by Grossmann and Koopmann: "Unlike conventional dumping which means selling abroad below cost or at lower prices than charged in the home market, 'social dumping' refers to costs that are for their part depressed below a "natural' level by means of 'social oppression' facilitating unfair pricing strategies against foreign competitors. Remedial action would either consist of the offending firms consenting to raise their prices accordingly or failing that, imposing equivalent import restrictions." Bob Hepple, A Race to the Top? International Investment Guidelines and Corporate Codes of Conduct, 20 Comp. Lab. L. & Pol'y J. 347, 347 (1999) (citing Harald Grossmann & Georg Koopmann, Social Standards in International Trade, A New Protectionist Wave?, in World Trade After the Uruguay Round 115, 116 (Harald Sander & Andras Inotai eds., 1996)).

n2. Id.


n6. "Shareholder democracy does not permit the majority to set company policy directly. Shareholder resolutions are merely suggestions to the board of directors, and attempts to control the directors by majority vote will be rebuffed[.]" Anupam Chander, Minorities, Shareholder and Otherwise, 113 Yale L.J. 119, 127 (2003).


n12. "Shareholder resolutions are the main vehicle for these principles' implementation, and all shareholder resolutions failed. Nevertheless, five states - Connecticut, Massachusetts, New Jersey, New York, and Rhode Island - adopted the MacBride Principles to guide their investment policies regarding TNCs in Northern Ireland, causing many companies to take notice." Barbara A. Frey, The Legal and Ethical Responsibilities of Transnational Corporations in the Protection of International Human Rights, 6 Minn. J. Global Trade 153, 176 (1997).

n13. Id.

n14. Van Ho, supra note 10, at 1213.

n15. Id. at 1214.


n17. Van Ho, supra note 10, at 1213.


n20. Olson, supra note 16.

n21. Van Ho, supra note 10, at 1214.


n25. Blair & Stout, supra note 11, at 291.

n26. "Shareholders have no right to direct or control the corporation, its board or its managers ... shareholders have no right to bind a public corporation, its directors, or its managers." Daniel J.H. Greenwood, Democracy and Delaware: The Mysterious Race to the Bottom/Top, 23 Yale L. & Pol'y Rev. 381, 435 (2005).


n34. Id. (internal citations omitted).

n35. Brownstein & Kirman, supra note 18, at 56.

n36. Id. at 56-57.

n37. Id. at 57.

n38. Id.

n39. Id. at 52.

n40. Brownstein & Kirman, supra note 18, at 52-53.

n41. Id. at 59-60.
n42. Id. at 60.

n43. Id.


n45. Bebchuk, supra note 29, at 844.

n46. Id. at 844-45.

n47. Id. at 845-46.

n48. Id. at 844.

n49. Id.


n56. Rahnema, supra note 9, at 276 n.11.


n62. Id. at 34.

n63. Id. at 37.

n65. Romanek, supra note 61, at 37.

n66. Id. at 36.

n67. Id. at 37.

n68. Id.

n69. Id. at 38-39.


n74. See Hannes, supra note 32, at 78-79.
n75. "Proxy cards for corporate elections typically allow shareholders to check a box authorizing the corporation to cast the shareholders' votes "for" the corporate nominees or to check a box marked "withhold vote.' They do not offer the option of voting "no.' Indeed, in an uncontested election, submitting a proxy card marked "withhold vote' is probably counterproductive, since its only effect is to validate the election by helping to establish a quorum. Refusing to return a proxy card at all might foil a quorum but could be interpreted by management as indifference, rather than opposition." Thomas W. Joo, A Trip Through the Maze of "Corporate Democracy": Shareholder Voice and Management Composition, 77 St. John's L. Rev. 735, 745 n.47 (2003).


n78. Id.

n79. Joo, supra note 75, at 744-45 (internal citations omitted).


n81. Id.


n83. 191 N.W.2d 406 (Minn. 1971).

n84. Id.; contra Credit Bureau Reports, Inc. v. Credit Bureau of St. Paul, Inc., 290 A.2d 691 (Del. 1972). See generally 50 A.L.R. 3d 1056 (noting the stockholders right to "inspect corporate books or records in pursuit
of social or political interests”).


n86. Medical Comm. for Human Rights, 404 U.S. at 406.


n89. Williams, supra note 8, at 1284-85.

n90. "Many cases have recognized the right of shareholders of a corporation at common law to inspect all corporate books and records, generally, although the right appears to be expressly or impliedly limited to documents that are relevant to shareholders' interests. Many jurisdictions have enacted statutes which grant stockholders the right to inspect particular books and records of the corporation. Under statutes of this nature, it has been held, similar to the common law rule, that shareholders have the right to inspect all books and records of the corporation, although the right of inspection appears to be explicitly or implicitly limited to documents that are relevant to shareholders' interests." 88 A.L.R.3d 663, §2(a).

n91. Id.

n92. Id.


n98. **Friedman v. Altoona Pipe & Steel Supply Co.**, 460 F.2d 1212, 1213 (3d Cir. 1972) (applying Pennsylvania law).


n100. **Bank of Heflin**, 318 So. 2d at 700.


n103. **State ex rel. Lowell Wiper Supply Co. v. Helen Shop, Inc.**, 362 S.W.2d 787, 791-92 (Tenn. 1962).

n105. See *Guthrie v. Harkness*, 199 U.S. 148, 155 (1905) ("The right of inspection rests upon the proposition that those in charge of the corporation are merely the agents of the stockholders, who are the real owners of the property" (citing *Cincinnati Volksblatt Co. v. Hoffmeister*, 56 N.E. 1033 (Ohio 1900)).

n106. Randall S. Thomas, Improving Shareholder Monitoring and Corporate Management by Expanding Statutory Access to Information, 38 *Ariz. L. Rev.* 331, 335-36 n.24 (1996) ("While these two interests are conceptually distinct, they overlap to such a great extent that the courts have frequently treated them together"). See, e.g., *Shaw v. Agri-Mark, Inc.*, 663 A.2d 464, 467 (Del. 1995) ("Inspection rights have been viewed as an incident to the stockholder's ownership of corporate property ... . As a matter of self-protection, the stockholder was entitled to know how his agents were conducting the affairs of the corporation of which he or she was a part owner").


n111. See *Williams*, supra note 8, at 1199-1200.


n113. See *Williams*, supra note 8, at 1199-1200.
n114. Id.

n115. See id. at 1199-1200 ("The capital markets in the United States are celebrated for their financial
transparency. This financial transparency derives primarily from the specific information about operating results,
presented using rigorous accounting principles, that federal securities laws require public companies to report on
a quarterly and annual basis").

n116. See Securities Act of 1934, ch. 2B, §§12(a), 13(a) (codified as amended at 15 U.S.C. §§78l(a), 78m(a)
(2000)).


n119. Rachel Cherington, Securities Laws and Corporate Social Responsibility: Toward an Expanded Use

n120. Id. at 1447 (citing 15 U.S.C. §§13-14 (2004)).

n121. Patricia Romano, Sustainable Development: A Strategy that Reflects the Effects of Globalization on
(1994)).

n122. Cyrus Mehri, Andrea Giampetro-Meyer & Michael B. Runnels, One Nation, Indivisible: The Use of
Diversity Report Cards to Promote Transparency, Accountability, and Workplace Fairness, 9 Fordham J. Corp.

n124. Id.


n126. Id. §229.401-05.

n127. Id. §229.103.

n128. Id §229.303.

n129. Id. §229.101; see also 17 C.F.R. §229.103.

n130. Stephen F. Diamond, The Petrochina Syndrome: Regulating Capital Markets in the Anti-Globalization Era, 29 J. Corp. L. 39, 77 (2003) ("The SEC already requires companies to disclose details about their environmental liabilities, potential problems related to intellectual property, and relationships with employees. The SEC long ago agreed to increase disclosure of so-called "soft" information, such as projections about the future course of a company's business model").

n131. Romano, supra note 121, at 110.

n132. See Cherington, supra note 119, at 1441, 1448.
n133. See Williams, supra note 8, at 1206.

n134. Cherington, supra note 119, at 1441-42.

n135. SEC Scrutinizing Foreign Registrants Regarding Dealings in Countries Under U.S. Sanctions, Prac. L. Inst. Order No. F0-00AN, at 81 (Dec. 2001) ("These include Iran, Iraq, Libya, Sudan, Cuba, and the Taliban in Afghanistan. U.S. companies are prohibited from engaging in any business activity in these countries. OFAC also enforces other restrictions on certain business activities with North Korea, Sierra Leone, Burma (Myanmar), Syria, the UNITA faction in Angola, and specified parties in the Federal Republic of Yugoslavia").


n138. Id. at 951.


n143. Id. at 504.

n144. 15 U.S.C. §7264 §406 (2004). It provides, in pertinent part:

The Commission shall issue rules to require each issuer, together with periodic reports required pursuant to section 13(a) or 15(d) of the Securities Exchange Act of 1934, to disclose whether or not, and if not, the reason therefor, such issuer has adopted a code of ethics for senior financial officers.

(c) Definition. In this section, the term "code of ethics" means such standards as are reasonably necessary to promote -

(1) honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships;

(2) full, fair, accurate, timely, and understandable disclosure in the periodic reports required to be filed by the issuer; and

(3) compliance with applicable governmental rules and regulations.


The regulation makes precise, in absence thereof, the social, environmental and ethical considerations which the company must respect in management of purchase or sale of securities as well as in the exercise of any rights attached thereto. The annual report of the fund shall declare their application according to conditions defined by the Commission of Stock Market Operations. (Author's translation).

Id. See also National public policies in the European Union: UK, available at


n147. See Gioseffi, supra note 142, at 524.


n149. Gioseffi, supra note 142, at 524.

n150. Crusto, supra note 148, at 483.

n151. Cherington, supra note 119, at 1448.

n152. Id. at 1449.

Any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered ... any manipulative or deceptive device or contrivance 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.

Id.

n154. 17 C.F.R. §240.10b-5 (2006). Rule 10b-5 provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

Id.; see also Cherington, supra note 119, at 1441 n.53.

n156. Cherington, supra note 119, at 1450-51.

n157. See Crusto, supra note 148, at 497-98.

n158. S.E.C., Staff Accounting Bulletin No. 99, 64 Fed. Reg. 45150-01, 45151 (Aug. 19, 1999) (codified at 17 C.F.R. §211 (2000)). (It contains the most recent authoritative literature on materiality: "[a] matter is material if there is a substantial likelihood that a reasonable person would consider it important.") Moreover, "environmental risks and liabilities are among the conditions that, if undisclosed, could impair the public's ability to make sound investment decisions. For example, the discovery of extensive hazardous waste contamination ... [or] impending environmental regulations could affect a company's future financial position ... ." Crusto, supra note 148, at 498 (quoting Letter from John B. Stephenson, Director, National Resources and the Environment, to Senator Jon S. Corzine (D.-N.J.) (Aug. 4, 2004) (GAO-04-1019R)).

n159. Cherington, supra note 119, at 1449.

n160. Letter from Honorable John B. Stephenson, Ranking Minority Member, Committee on Environment and Public Works, to Senator Jon S. Corzine (D.-N.J.) (July 14, 2004) reprinted in GAO-04-808, Environmental Disclosure: SEC Should Explore Ways to Improve Tracking and Transparency of Information (2004) ("Environmental risks and liabilities are among the conditions that, if undisclosed, could impair the public's ability to make sound investment decisions. For example, the discovery of extensive hazardous waste contamination... [or] impending environmental regulations could affect a company's future financial position"). Id.


n162. Id. at 413.


n164. Cherington, supra note 119, at 1446.
n165. See, e.g., Kasky, 45 P.3d at 248.

n166. Cherington, supra note 119, at 1446.

n167. Cherington, supra note 119, at 1446.

n168. See, e.g., Hemming v. Alfin Fragrances, Inc., 690 F. Supp. 239, 244 (S.D.N.Y. 1988) (holding that advertising in the New York Times Magazine, although widely distributed, was not sufficient to establish the "in connection with" requirement for Rule 10b-5 because it was aimed at consumers rather than investors). But see In re Carter-Wallace Inc. Sec. Litig., 150 F.3d 153, 156-57 (2d Cir. 1998) (holding that advertisements in medical journals may meet the "in connection with" requirement).

n169. Charles Mark Holt, B. Alford v. Shaw: North Carolina Adopts a Prophylactic Rule to Prevent Termination of Shareholders' Derivative Suits through Special Litigation Committees 64 N.C. L. Rev. 1228, 1228-29 n.1 (1985) ("A shareholders' derivative suit is an action brought by one or more shareholders of a corporation to enforce a corporate cause of action against officers, directors, or third parties" (citing Ross v. Bernhard, 396 U.S. 531, 534 (1970))).


n172. Id. at 1036.

n173. Id. at 1035.
n174. *Id. at 1036.*


n176. *Id.*

n177. *Id.*

n178. Robert E. Jones et al., Rutter Group Practice Guide: Federal Civil Trials and Evidence ch. 2-B §2:60 (citing *Ross v. Bernhard,* 396 US 531, 532-533 (1970) (“The right to jury trial attaches to those issues in derivative actions as to which the corporation, if it had been suing in its own right, would have been entitled to a jury”)).


n180. The universal rule that a shareholder must exhaust intracorporate remedies before bringing a derivative action is most often cited to. *Id. at 460-62* (The rationale for the demand requirement derives from a recognition of corporate managers' and directors' authority to bring a corporation's cause of action and from goals of judicial economy because many claims may be settled within the corporate structure). See, e.g., *Barr v. Wackman,* 329 N.E.2d 180, 185-86 (1975) (board of directors can often correct alleged abuses without resort to the courts.); see also Holt, supra note 169, at 1229.


n182. *Id.*

n183. Deborah A. DeMott, Shareholder Derivative Actions Law and practice. §5:2 (1987 & Supp. 2006);
but see *Eye Site, Inc. v. Blackburn*, 796 S.W.2d 160 (Tex. 1990).


n185. Id.

n186. *Id. at 151*.


n188. Sirodoeva-Paxson, supra note 184, at 151.

n189. Kleinberger, supra note 187, at 1208.

n190. Sirodoeva-Paxson, supra note 184, at 151.


n192. See id.

n193. *Fed R. Civ. P. 23(1)*.


n197. Dubinsky, supra note 3, at 1152 ("In the human rights class action, the tension between individual claimants and the group as a whole can be heightened").

n198. See, e.g., Tylka v. Gerber Prods. Co, 178 F.R.D. 493, 497-98 (N.D. Ill. 1998) (narrowing the class definition after plaintiffs had failed to show that the "nuances of 50 consumer fraud statutes" could be manageably litigated in one suit).

n199. Mejdrech v. Met-Coil Sys. Corp., 319 F.3d 910, 910-12 (7th Cir. 2003) (certifying class only with respect to one common question of causation and refusing to certify it with respect to individual claims of harm).

n200. Dubinsky, supra note 3, at 1187.

n201. See, e.g., Cicippio v. Islamic Republic of Iran, 18 F. Supp. 2d 62, 69 (D.D.C. 1998); Nat'l Coal. Gov't of the Union of Burma v. Unocal, Inc., 176 F.R.D. 329, 360 (C.D. Cal. 1997) ("equitable tolling is available where (1) defendant's wrongful conduct prevented plaintiff from asserting the claim; or (2) extraordinary circumstances outside the plaintiff's control made it impossible to timely assert the claim").

