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I. INTRODUCTION

As the United States disembarks the 1980s Wall Street rollercoaster, it is difficult to deny that American corporations are facing the critical task of becoming, and in some cases remaining, competitive in a global market. To survive this challenge, U.S. companies will have to perform as they have never before performed. If these companies fail, so too will their investors. It is therefore imperative for investors in U.S. corporations to understand the challenge that they face in the coming decade, and to identify ways in which investments can be both protected and enhanced. The obstacles which may impede the ability of investors to protect their interests form the basis of the barriers to which the title of this paper refers.

II. PROTECTIVE DEVICES REDUCE ACCOUNTABILITY

When an employee is underperforming, and corrective actions have been unsuccessful, simple accountability dictates that the employment should be terminated. The knowledge that one must be accountable to another creates the incentive to achieve one's goals. Conversely, if there are no effective means to monitor, evaluate, or enforce performance standards, there is no accountability; with the loss of accountability comes the loss of the incentive to perform.

Applying this theory, it seems obvious that if the management of a company is not performing as the owners of that company expect, the management should be replaced. Yet, in practice, the owners of publicly traded U.S. companies do not have this ability. Our corporations, through their own structure as well as with help from the government, have insulated themselves from meaningful accountability. This Article

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discusses some of these barriers to management accountability and proposes a few methods for shareholders to overcome them.

A. Poison Pills

The poison pill was the first insulation device to achieve widespread adoption. Though the poison pill was reportedly first developed only in 1984,[1] it was adopted by over six hundred of America's leading companies within the following five years.[2] Although the poison pill began as an antitakeover device,[3] the pill and its progeny have grown far beyond the takeover context.

The original pills were not fatal—they merely caused discomfort. For example, the acquisition of control of Crown Zellerbach by Sir James Goldsmith in 1985 demonstrated a significant shortcoming in the earlier versions of the pill.[4] This led to ongoing efforts to increase the pill's toxicity. Under the most recent version, developed by the law firm of Wachtell, Lipton, Rosen & Katz, a pill is joined with the issuance of repurchase rights. These rights, triggered whenever a person acquires fifty percent or more of the target's outstanding stock, permit their holders to sell one share of stock back to the target company at twice the price for which the stock was trading on the date of issuance of the right. Since the exercise of these repurchase rights involves a cash payment by the target company, rather than the sale of additional securities at a discount price, the economic effect on the target is much more dramatic.[5]

One criticism of poison pills is that they are nearly always adopted by a board of directors without shareholder consent. Unlike antitakeover amendments to company charters, pills do nót legally require shareholder approval. In response to shareholder complaints about the unilateral adoption of devices that make it difficult to achieve a change of control which may be desired by the shareholders, the original pills were restructured to include a shareholder approval component. Under this

1. Martin & Struxness, *A Review of Current Developments in Shareholder Rights Plans*, 2 MERGERS & ACQUISITIONS L. REP. 234 (1989).

2. INVESTOR RESPONSIBILITY RESEARCH CENTER, INC., CORPORATE TAKEOVER DEFENSES app. A at 1447 (1989). The universe consisted of all companies from the S&P 500, from the Fortune 500, and from the Forbes and Business Week 1C00s.

3. In general, the purpose of the pill is to place control over whether an acquisition goes forward with the target's board of directors rather than the target's shareholders. "If the [target's] board does not approve [the deal] and the potential acquirer proceeds with the bid anyway, the pill could be 'triggered,' causing actions that would make the target financially unattractive and/or actions that would dilute the voting power of the potential acquirer." *Id.* at x.

4. Martin & Struxness, *supra* note 1, at 236.

5. *Id.* at 242.

rendering, if a bidder satisfies certain procedural requirements, a special shareholder meeting will be called to determine whether to redeem the pill and thus permit the acquisition to go forward. This inclusion of shareholders in the decision-making process, however, is illusory. The prerequisites for bringing the issue to shareholders are so burdensome[6] that the effect of the pills remains unchanged. Boards of directors are free to determine whether they should turn the company over to someone else, regardless of the shareholders' wishes.

As noted, nearly half of America's largest companies have adopted a poison pill. Now well into their third and fourth generations, pills are so commonplace that today many corporate executives believe that failure to have a pill in place is a per se violation of their duty to the corporation.

B. Charter and Bylaw Amendments

Although poison pills are quite common and have acted as a general deterrent to hostile takeovers, they have not provided an infallible means of shielding management from potential change. Courts, for example, have recognized that contests for control create an inherent conflict of interest for directors, and have therefore more closely scrutinized the adoption of and the refusal to redeem a pill in the face of a hostile bid.[7]

Alterations to corporate charters have proven to be a more effective means of avoiding hostile takeovers. Unfortunately, they have also substantively reduced the shareholders' ability to participate in corporate governance. For example, classified boards and the absence of cumulative voting restrict the ability of a dissident to take control quickly. With a classified (or staggered) board, it may take several years before a dissident can be successful in electing a majority of the directors, even if a majority of the shareholders support a change of control. Likewise, cumulative voting permits minority holders to elect one or two directors, while the absence of cumulative voting can make it more difficult to elect directors outside of the management slate. Thus, both of these devices are effective means for maintaining the status quo, even if the status quo is incompetence.

Limiting the shareholders' ability to call special meetings, acting by written consent, and direct company action by a simple majority vote can also be effective antitakeover measures. By restricting the opportunity

6. For example, it is burdensome to obtain financing commitments even before it is known whether the pill will be redeemed or not.

7. *See, e.g.*, Grand Metro. Pub. Ltd. Co. v. Pillsbury Co., 704 F. Supp. 538 (D. Del. 1988).

for shareholders to take part in meetings called by management, management can control the timing, presentation, and tenor of the deliberations. Shareholders thereby lose a possible means of encouraging the company to take a different strategic direction that may enhance shareholder value.

Dual class capitalization plans with unequal voting rights also tend to place the interests of incumbent management above those of the shareholders. These plans are in direct contrast to the American cultural disposition towards one person, one vote. The Securities and Exchange Commission's rule[8] restricting such plans was invalidated by an appellate court in early 1990,[9] but that decision is, as of the date of this Article, still subject to appeal. Additionally, as of the date of this Article, unequal voting rights are still impermissible under national exchange listing standards.

C. State Legislation

1. History

Despite the general effectiveness of the devices described above, state legislative action aimed at protecting local business and trade interests has provided the most substantive invasion of shareholders' rights, all cloaked with the blessing of the government. While under certain circumstances it has been possible to avoid a poison pill through court intervention, the only way to avoid state statutes is to obtain a judicial declaration that the statutes are unconstitutional. Given the great judicial deference that is accorded to state legislatures, this is a heavy and almost insurmountable task.[10]

The first state antitakeover law was enacted in Virginia in 1968, and it inspired thirty-six states to pass similar laws over the next thirteen years.[11] In 1982 however, the U.S. Supreme Court, in *Edgar v. MITE*, struck down such a law, concluding that it interfered with interstate commerce.[12] The Illinois law at issue in *Edgar* established (as did most other state laws of this genre) more stringent notification and disclosure requirements on bidders than did the federal Williams Act.[13] Based upon both the supremacy of federal law and the commerce clause, the

8. 17 C.F.R. § 240.19-C4 (1990).

9. Business Roundtable v. SEC, 905 F.2d 406 (D.C. Cir. 1990).

10. *See infra* note 15 and accompanying text.

11. *When A State Protects A Company*, ISSUE ALERT, July-Aug. 1990, at 1.

12. *See* Edgar v. MITE Corp., 457 U.S. 624 (1982).

13. The Williams Act, 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (1988), added new sections 13(d), 13(e), and 14(d)-(f) to the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78lll

court overturned the Illinois statute.[14]

Between 1982 and 1987 few states adopted protective legislation. In 1987 however, the constitutionality of state action in this area, at least when limited to corporations with a substantial relationship to the regulating state, was reaffirmed.[15] In *CTS Corp. v. Dynamics Corp. of America*, the Supreme Court reviewed an Indiana state law that, unlike the Illinois statute overturned in *Edgar* which merely concerned notification and disclosure requirements for bidders, substantively altered the ability of a bidder to acquire, without the consent of the target company's board, voting rights to a controlling share of the target company. The Court upheld the law, determining that it neither interfered with the federal government's regulation of mergers and acquisitions nor violated the commerce clause.[16] Since the *CTS* decision, over forty states have enacted antitakeover statutes or strengthened existing statutes.[17] As of September 1, 1989, only twelve states and the District of Columbia did not have some form of protective legislation.[18]

State regulations began with the ostensible purpose of restricting takeovers that were viewed as harmful to the local economy. For example, soon after the *CTS* decision was announced, Boeing became concerned about a possible fifteen percent acquisition by Mr. T. Boone Pickens. Boeing turned to the Washington state legislature for help, which was quickly granted in the form of protective legislation.[19] Boeing, however, was incorporated in Delaware, not Washington. But, because Boeing accounted for an estimated eight percent of Washington employment and reportedly had contributed one hundred thirty-one thousand dollars to local political campaigns the year before, Washington's new law expressly applied to certain out-of-state companies such as Boeing.[20] Thus, under the rallying cry of protecting local employment, Washington insulated Boeing from a possible Pickens challenge. Ironically, it is Delaware, not Washington, that receives Boeing's taxes and incorporation fees.

(1988). Generally, these provisions require certain disclosures by persons acquiring, or seeking to acquire, more than 5% of any class of registrant's equity security. 457 U.S. at 627 n.2.

14. 457 U.S. at 630-34, 640-46.

15. CTS Corp. v. Dynamics Corp. of America, 481 U.S. 69 (1987).

16. *Id.* at 94.

17. *When A State Protects A Company, supra* note 11, at 3.

18. INVESTOR RESPONSIBILITY RESEARCH CENTER, INC., STATE TAKEOVER LAWS app. A at A-6 (1989).

19. WASH. REV. CODE §§ 23A.50.010-.900 (repealed 1990).

20. *When A State Protects A Company, supra* note 11, at 3.

2. Legislation Restricting Changes of Control

Paralleling the development of corporate protective devices, state takeover laws have quickly grown beyond the takeover context to be a comprehensive shield against changes to the corporate status quo. There are generally seven types of state takeover laws, many of which are used in combination. Two of these (discussed in Section C.3., *infra*) redefine the historic duty of directors to shareholders. The remaining five, discussed below, focus on changes in control of corporate management.

(a) *Control Share Acquisition Statutes*

Under these statutes, when a shareholder reaches certain thresholds of ownership (typically ten percent, thirty-three and one-third percent, and fifty percent), the shareholder must win the approval of a majority of the disinterested outstanding shares before exercising the voting rights of the control share. The bidder must satisfy significant procedural requirements before a shareholder meeting will be called to decide the issue of voting rights.[21] Some states (*e.g.*, Minnesota) require greater disclosure regarding the bidder's plans for the company. Approximately twenty-two states have adopted a form of the control share acquisition statute.[22]

Supporters consider this type of provision to be a balanced means of protecting a company from unwarranted and undesirable hostile takeovers. Opponents consider it to be a classic entrenchment device since the practical possibility of bringing the restoration of voting rights issue to the shareholders is extremely remote (*i.e.*, arriving at a definitive financial agreement with lenders or financiers is virtually impossible without having voting rights in the company). Additionally, the costs of pursuing what in effect will be two proxy contests (one to obtain voting rights and the other to acquire control) is a further deterrent to contests that could be beneficial to the shareholders' interests. To the extent that proxy contests are discouraged, management accountability is diminished. Lastly, more as a matter of principle, opponents contend that the disenfranchisement of voting power violates the democratic concept of one person, one vote.

(b) *Fair Price Laws*

If a bid does not meet certain specified "fairness" criteria (*e.g.*, it

21. These requirements typically include the filing of disclosure statements, including definitive financing plans, the request for a shareholder meeting, and an agreement to pay the expenses of the meeting.

22. INVESTOR RESPONSIBILITY RESEARCH CENTER, INC., *supra* note 18, app. A at A-4.

cannot be two-tiered), fair price laws dictate that the bid typically must be approved by a super-majority (usually two-thirds) of the shares not held by the bidder. While twenty-two states have enacted a fair price law,[23] few states have such a law standing alone. In most states, the fairness criteria applies only after the expiration of a freeze-out waiting period.

(c) *Freeze-Out Laws*

If a shareholder acquires a certain threshold amount of outstanding shares (typically ten percent), then that shareholder may not merge, acquire, or otherwise combine with the company for some extended period of time (ranging from two to five years). This freeze-out does not apply, however, if the company's board approved the combination prior to the acquisition of the threshold amount. Approximately twenty-four states have enacted this type of law, including Delaware.[24] Since Delaware is the state of incorporation of the vast majority of large U.S. corporations, this type of law is most prevalent.

Obviously, this type of law is intended to discourage acquirers who cannot afford to have funds tied up for as long as five years without consummating a merger or otherwise gaining control over the target. Because of the need to obtain board approval before reaching the designated threshold amount, freeze-out laws have resulted in an increase in the number of proxy contests by holders of, for example, 9.9 percent of the company's outstanding stock. It is hoped that by obtaining a few board seats, board approval will follow and the freeze-out can be avoided.

(d) *Profit Disgorgement*

In April 1990 Pennsylvania's governor signed into law what is widely recognized to be the strongest antitakeover legislation in America.[25] One part of this expansive law requires the holder of twenty percent or more of a company's stock to pay back to the corporation any profits realized upon the sale of the stock that was held under terms that the statute characterizes as "short-term."[26] This provision applies to a holder of twenty percent of the proxies (when held for purposes of acquisition), but not to any situation in which the stock purchase had prior approval by both the shareholders and directors.

23. *Id.*
24. *Id.*
25. 15 PA. CONS. STAT. §§ 2571-2575 (1990).
26. *Id.* § 2574.

Supporters of this type of provision claim that it will discourage raiders who simply wish to reap huge profits from short-term holdings by insincerely putting a company in play. Such raiders buy a large block of a company's stock, publicly disclose an intent to acquire, and then sell (or dispose through "greenmail") after the resulting stock price escalation. On the other hand, opponents argue that the scope of this type of law goes beyond restricting insincere raiders since it imposes huge costs on any bidder that is unsuccessful in actually acquiring the company. The supporters' argument takes advantage of the public perception that all acquirers are raiders bent on destroying the local economy. This type of provision results in a significant deterrent to all takeover activity—even that activity which may be necessary to replace inefficient management.

(e) *Labor Protections*

A growing number of states[27] are adopting a myriad of different statutes aimed at protecting the labor force in the event of a takeover. Among these are the requirement that any acquirer honor existing labor contracts for a specified period, and provide statutory severance payments for employees terminated as a result of the takeover.

Supporters argue that this approach protects workers, who are most directly affected by corporate raiders. Additionally, it arguably provides stability to the corporation by improving morale and assuring continued productivity—both of which benefit shareholders—during the tenuous period of a threatened takeover. Opponents argue that the laws represent an additional cost to takeover activity, which acts as a deterrent to takeovers that may be preferred by shareholders.

3. Legislation Redefining Corporate Duty

In addition to enacting laws that focus on changes of control, a number of state legislatures are expanding beyond the context of takeovers and are substantively altering the relationship between shareholders and directors. Ironically, these laws are almost universally packaged with pure antitakeover legislation of the type described above, so that the extent of the legislative interference in principles of traditional corporate law often goes unnoticed. Thus far, states have addressed two types of issues:

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27. INVESTOR RESPONSIBILITY RESEARCH CENTER, INC., *supra* note 18, app. A at A-5; *see also* 15 PA. CONS. STAT. § 2581 (1990).

(a) *The Stakeholder Concept*

The mildest form of these new laws merely clarifies that, when considering the best interests of the corporation, directors may consider both long and short-term horizons, as well as the impact of decisions on the local community, employees, and the economy. The strongest version of these laws, however, permits directors to consider the interests of all stakeholders (*e.g.*, creditors, suppliers, the community, and employees) on an equal basis with the interests of shareholders.

In 1983 Pennsylvania's legislature adopted a relatively mild form of this law.[28] Seven years later, however, the legislature strengthened its law to declare that shareholders form only one aspect of a company's constituency base, and that no stakeholder's interest is dominant.[29] Thus, any corporate decision justifiable on the basis of some stakeholder interest will be presumed appropriate.

Representing a possible argument that could be used by other states attempting to expand their milder stakeholder laws, supporters of the Pennsylvania legislation claimed that it was merely a clarification of existing law. Opponents point out, however, that courts have traditionally held that, while a board may consider a myriad of interests, if there is a direct conflict, then the long-term interests of shareholders are paramount. A letter to Pennsylvania's General Assembly signed by forty-two professors of law and business noted that "[t]he law's changes in directors' fiduciary obligations fundamentally undermine century-old traditions in corporate law, and directly threaten the director-shareholder relationship."[30]

In particular, these types of laws appear to repudiate a leading Delaware[31] case, *Revlon Inc. v. MacAndrews & Forbes Holdings, Inc.*,[32] in which the court declared it inappropriate to place creditors' interests over those of shareholders. By allowing other types of interests to take dominance over shareholders' interests, the Pennsylvania law substantively reduces the rights of shareholders. Since it will always be possible for directors to point to some group's interests that are being fostered in any given decision, director accountability is significantly lessened.

28. 15 PA. CONS. STAT. § 911 (1983) (repealed by 15 PA. CONS. STAT. § 5911 (1990)).

29. *See* 15 PA. CONS. STAT. §§ 511, 1721 (1990).

30. *Board Games: Are Shareholders Getting Ripped Off?*, INSIGHT ON THE NEWS, July 1990, at 9-10.

31. Delaware cases are routinely relied upon by other states' courts when interpreting issues of general corporate law.

32. Revlon Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986).

(b) *Strengthening of the Business Judgment Rule*

American courts have typically afforded great deference to corporate managers in presuming that their business decisions were appropriately made.[33] Applying this business judgment rule, the courts have determined that, absent situations involving self-dealing or other conflicts of interest, when a board after reasonable investigation adopts a course of conduct believed in good faith to be consistent with its fiduciary duty, the courts will not second-guess that decision.[34] However, recent court decisions have imposed a heightened scrutiny of board decisions made in the context of a contest for control under the rationale that such situations create a potential conflict of interest.[35]

Some state statutes (*e.g.*, Ohio, Indiana, and Pennsylvania)[36] are beginning to strengthen this already strong protection by increasing both the amount of evidence needed and types of situations that must exist to overcome the presumption created by the business judgment rule. This legislation expressly provides that the business judgment rule (and not the heightened scrutiny standard) applies in situations involving contests for control, including decisions regarding whether to continue as an independent corporation, redeem a poison pill, or opt out of the law.[37] Further, the Pennsylvania law declares that a decision by disinterested directors will be presumed to be in the best interests of the corporation, and that this presumption will be avoided only with clear and convincing evidence that the decision was not made in good faith.[38] These changes will provide corporate directors with additional insulation from liability, and thus will further reduce accountability to shareholders.

With fifty different systems of corporate law in the United States, and with significant taxation and regulatory income to be generated from attracting businesses, all states are competing in what has been called a "race to the bottom."[39] Regardless of who wins this race to provide job security to corporate managers, shareholders are the losers.

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33. *See In Re* RJR Nabisco, Inc. Shareholders Litig., [1988-1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 94,194 (Del. Ch. 1989); Paramount Communications v. Time Inc., 571 A.2d 1140 (Del. 1990).

34. *See* Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984).

35. Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985).

36. INVESTOR RESPONSIBILITY RESEARCH CENTER, INC., *supra* note 18, at 11; *see also* 15 PA. CONS. STAT. §§ 511, 1721 (1990).

37. 15 PA. CONS. STAT. §§ 511, 1721 (1990).

38. *Id.* §§ 511(f), 1721(g).

39. *See, e.g.*, Fischel, *The 'Race to the Bottom' Revisited: Reflections on Recent Developments in Delaware's Corporation Law*, 76 NW. U.L. REV. 913 (1982).

III. INVESTOR RESPONSES

Statistics indicate that the ownership of U.S. corporations is becoming increasingly concentrated in institutions, approximately forty-four percent of which are public and private pension funds.[40] This trend is important because pension fund trustees have a fiduciary duty to maximize trust fund assets, while still operating within the parameters of a prudent investor.[41] How, then, can pension fund trustees reconcile their duty to maximize with the growing economic evidence that protective devices such as those discussed have a negative impact on investment value?[42] With the existence of such devices in any given company quickly becoming more of a norm than an exception, divesting oneself of all offending, and hence less profitable, companies is obviously both impractical and imprudent.

Members of the Bush administration are also concerned with the lack of corporate accountability, as it affects the ability of U.S. corporations to effectively compete for equity in a global market. Both the Securities and Exchange Commission (SEC) and the Department of the Treasury have identified this issue as one of key importance.[43]

One solution to the corporate accountability problem which has been adopted by a number of pension funds is to aggressively exert the shareholders' ownership rights to achieve corporate accountability. Such a policy merges the pension fund's corporate ownership rights and responsibilities with its primary duty to the fund's beneficiaries. This is not a novel approach. As early as 1934 Benjamin Graham and David Dodd, the founders of fundamental stock analysis, tried to encourage investment managers to exercise their ownership rights: "The choice of a com-

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40. Brancato, *Who Owns Corporate America? The Momentum of the Big Investor*, DIRECTORS & BOARDS, Winter 1990, at 38.

41. *See, e.g.*, 29 U.S.C. § 1104(a)(1)(A) (1990); CAL. CONST. art. XVI, § 17.

42. *See, e.g.*, S.L. NESBITT, THE IMPACT OF "ANTI-TAKEOVER" LEGISLATION ON PENNSYLVANIA COMMON STOCK PRICES (1990); Karpoff & Malatesta, *The Wealth Effects of Second-Generation Takeover Legislation*, 25 J. FIN. ECON. 291 (1990); ANALYSIS GROUP, INC., THE ECONOMIC EFFECTS OF POISON PILLS (1989); Ryngaert & Netter, *Shareholder Wealth Effects of the Ohio Antitakeover Law*, 4 J.L. ECON. & ORGANIZATION 373 (1988); Pound, *The Effects of Anti-Takeover Amendments on Takeover Activity: Some Direct Evidence*, 30 J.L. & ECON. 353 (1987); Jarrell & Poulsen, *Shark Repellents and Stock Prices*, 19 J. FIN. ECON. 127 (1987).

43. *See, e.g.*, R. Glauber, Competitiveness in the 1990s and Beyond (Feb. 5, 1990) (statement before Treasurer's Conference, sponsored by the Financial Executives Institution); P. Lochner, Institutional Investors and Corporate Governance (June 14, 1990) (remarks before the Conference on the Fiduciary Responsibilities of Institutional Investors, New York University); R. Breeden, Acquisitions and Takeovers: What Lies Ahead for Shareholder Rights? (Apr. 26, 1990) (remarks before the Twelfth Annual Institute on Acquisitions and Takeovers).

mon stock is a single act; its ownership is a continuing process. Certainly there is just as much reason to exercise care and judgment in *being* a stockholder as in *becoming* a shareholder."[44]

To date, attempts by pension funds to restore accountability have taken two general forms: those that are company-specific, and those that are directed more globally toward altering the American corporate culture.

Although reform on a company-by-company basis is tedious, it can result in important changes. Historically, when first entering the field of investor activism, most pension fund trustees have initially focused their attention on shareholder proposals. These proposals, which are submitted to a recipient company pursuant to procedures prescribed in SEC rule 14a-8, are limited to certain issues,[45] and may sometimes only be precatory in nature.[46] In addition, because the existing proxy process is designed with a bias in favor of management,[47] these proposals are extremely difficult to pass. The lack of confidential voting and unequal information and access represent additional hurdles for the proponent shareholder.

While shareholder proposals rarely pass, the likelihood of their success is increasing.[48] This enlarged level of support, along with the growing volume of proposals and the diversity of sponsors, has attracted the serious attention of many companies. As a result, many corporate managers are willing to voluntarily adopt the more moderate proposals (*e.g.*, confidential voting), and are offering other significant concessions to avoid putting radical proposals to a shareholder vote. For example, in the 1990 proxy season, both Occidental Petroleum and TRW voluntarily agreed to permit large shareholders to meet with directors to discuss issues of corporate governance and performance, in exchange for the withdrawal of a shareholder proposal which would have created a formal and permanent shareholder advisory committee.[49]

44. B. GRAHAM & D.L. DODD, SECURITY ANALYSIS 508 (1st ed. 1934).

45. For example, shareholder proposals may not undertake an issue within the company's ordinary business.

46. *I.e.*, be in the form of a recommendation from shareholders to directors.

47. For example, shareholder proposals, combined with their supporting statements, are limited to 500 words, while the company's opposition is unlimited.

48. During the 1990 proxy season, at least sixteen proposals received the support of the majority of proxies voting on the issue. This is compared to only three during the 1989 proxy season. *Shareholders Score Unprecedented Victories In 1990*, [7 No. 3] CORP. GOVERNANCE BULL. 54 (1990).

49. R. Koppes, 1990 Corporate Governance Report 4-5 (July 10, 1990) (memorandum to members of the California Public Employees' Retirement System Board of Administration).

Litigation is another company-specific method for challenging corporate behavior. Lawsuits, however, are generally time-consuming, expensive, ineffective, and largely profitable only for the attorneys. Additionally, due to recent statutory changes, such as the strengthening of the business judgment rule, the judicial system provides near-illusory protection for shareholders.

Direct, informal communications with companies, again on a company-by-company basis, can be less adversarial than either shareholder proposals or litigation. Such communications, however, are typically dependent upon the investor and the company's executives having the time and resources necessary for a face-to-face meeting. If an investor has holdings in more than a few companies, such meetings can become a significant drain and test to the investor's resolve. Also, informal meetings may lack the structure of a more institutionalized forum, and agreements that are reached through these informal methods are generally not subject to enforcement. However, inasmuch as any widespread change in corporate governance depends upon the attitudes of the individual participants, direct communication provides an opportunity for an exchange of ideas, with the possibility of incrementally altering attitudes.

Direct, company-specific measures would undeniably be more effective if the company's shareholders could form a cohesive force requiring management attention. The combined economic power of institutional investors is extraordinary. Pension funds control assets with an estimated value between 1.5 and 2.6 trillion dollars, and could own as much as fifty percent of all corporate equity by the year 2000.[50] When institutions do agree on an issue, their strength is unquestionable. For example, though a number of quite active and vocal institutions were unable to prevent the 1990 adoption of Pennsylvania's antitakeover statute, fear that these institutions would abandon Pennsylvania corporations led to an astonishing number of companies opting out of the statute's protections.[51]

Such solidarity, however, is a rare achievement. As similar as the functions of most pension funds are, fund trustees are nevertheless reluctant to combine forces or to entrust decision-making authority to others. Additionally, limited expertise and resources within the funds themselves

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50. *The Power of Pension Funds*, BUS. WEEK, Nov. 6, 1990, at 154; Light, *The Privatization of Equity*, HARV. BUS. REV., Sept.-Oct. 1989, at 62; *America's Shareholders Break Into the Boardroom*, ECONOMIST, Apr. 1989, at 75.

51. At least eighty-five corporations have followed this path. [7 No. 4] CORP. GOVERNANCE BULL. (1990).

often prevents trustees from becoming active as often as theory would dictate.

IV. CONCLUSION

While incremental, company-specific accomplishments may occur, reform of the corporate system as a whole represents the most effective means of providing shareholders with the protection they seek. While members of the SEC have publicly embraced many corporate governance concepts,[52] the SEC's authority to regulate beyond the narrow context of proxy disclosure is in question given a recent appellate court decision invalidating the Commission's one share, one vote rule.[53]

On the other hand, a federal system of corporate law which establishes certain minimum levels of accountability beneath which no state may regulate is an option which would certainly provide the greatest protection for shareholders against the onslaught of local parochialism. Such an option may, at a time when the banner of state's rights is firmly in place, appear politically unlikely in the immediate future. However, the success of future efforts to lift the barriers that reduce corporate accountability to shareholders will depend upon the federal government taking a leadership role in curtailing divisive and defensive actions by state governments. Without such efforts, the global competitiveness that politicians crave and the equitable treatment which is necessary to attract investors to the U.S. capital market cannot be achieved.

52. *See supra* text accompanying note 43.
53. *See* Business Roundtable v. SEC, 905 F.2d 406 (D.C. Cir. 1990).