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Is the Quest for Corporate Responsibility a Wild Goose Chase? The Story of Lovenheim v. Iroquois Brands, Ltd.

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**IS THE QUEST FOR CORPORATE RESPONSIBILITY A
WILD GOOSE CHASE? THE STORY OF *LOVENHEIM V.
IROQUOIS BRANDS, LTD.****

*D. A. Jeremy Telman***

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I. INTRODUCTION

In *Lovenheim v. Iroquois Brands, Ltd.*,¹ plaintiff Peter Lovenheim asked the D.C. District Court to enjoin defendant Iroquois Brands, Ltd.

* This article is a reprint of the article that was printed in the Akron Law Review, Volume 44, Issue 2, 2011. There was a printing error with this article and its corrections are included in this article.

** Professor, Valparaiso University School of Law. The Author is grateful to Peter Lovenheim and Ralph Halpern, for their willingness to help me reconstruct the background to this case, and also to my colleague, Rebecca Huss, who helped me to situate the case in two of its important contexts, the history of animal law and the corporate response to shareholder proposals.

(Iroquois) from omitting his shareholder proposal from the proxy materials sent out in advance of its 1985 annual shareholder meeting.² The proposal related to a French product, *pâté de foie gras*, which Iroquois distributed in the United States,³ and which constituted a tiny part of Iroquois' business.⁴ Lovenheim, the owner of two hundred shares of Iroquois' common stock,⁵ called upon Iroquois to investigate whether the French producer engaged in forced-feeding of the geese, which Lovenheim considered a form of animal cruelty, in producing the *pâté de foie gras* and, if that turned out to be the case, asked Iroquois to consider discontinuing the product until a more humane means of production could be developed.⁶

He decided to submit a shareholder proposal as permitted under SEC rule 14a-8 (the Rule)⁷ promulgated pursuant to section 14(a) of the Securities Exchange Act of 1934 (the '34 Act).⁸ Those regulations provide that a corporation must include qualifying shareholder proposals in its proxy solicitation materials distributed in advance of annual or special shareholder meetings, along with the shareholder's statement in support of the proposal.⁹ A shareholder proposal is any "recommendation or requirement that the company and/or its board of directors take action" that a shareholder intends to present at a shareholder meeting.¹⁰ The District Court granted Lovenheim's motion and preliminarily enjoined Iroquois from sending out its proxy materials without the proposal.¹¹

Lovenheim is not only a standard teaching case in corporate law courses, it is routinely cited by the Securities and Exchange Commission (SEC) in response to corporations seeking to exclude shareholder proposals from proxy materials on the ground that the proposals are not

1. 618 F. Supp. 554 (D.D.C. 1985).

2. *Id.* at 556.

3. *Id.*

4. *See id.* at 559 (finding that sales of the product accounted for none of Iroquois' net earnings and less than 0.05% of its assets).

5. *Id.* at 556.

6. *Id.*

7. 17 C.F.R. § 240.14a-8 (2010).

8. Securities Exchange Act of 1934, ch. 404, 48 Stat. 895 (1934) (codified as amended at 15 U.S.C. § 78n(a) (West 2010)) (amended by PL 111-203, 124 Stat. 1376 (July 21, 2010)).

9. *Id.* At the time, the proposal, together with the statement in support, must be no more than 200 words in length. *Lovenheim*, 618 F. Supp. at 557 n.4. The current version of the rule allows shareholders 500 words to support their proposal. 17 C.F.R. § 240.14a-8(d) (2010).

10. 17 C.F.R. § 240.14a-8(a) (2010).

11. *Lovenheim*, 618 F. Supp. at 562.

significantly related to the corporations' businesses.¹² Despite the case's prominence, its story has not been told in detail. That is a shame, because the details of the case are as surprising as its outcome must have been to Iroquois when the court granted Lovenheim the injunction he sought.

The case seems like a setup. At the time he invested in Iroquois, Lovenheim was the Government Relations Counsel for the Humane Society of the United States (Humane Society) in Washington, D.C.¹³ Lovenheim had offered the same proposal at the 1983 shareholder meeting, at which time only about 5% of the voting shares supported it.¹⁴ During oral argument, Lovenheim's counsel conceded that Lovenheim had no expectation that the proposal would succeed.¹⁵ Lovenheim himself seems to be a front for the Humane Society, and his suit appears to be a political crusade masquerading as shareholder activism.¹⁶ That is, it seems like Lovenheim was in fact far more interested in stopping animal cruelty than he was in preserving the value of his investment in Iroquois stock. After all, his proposal could not have succeeded. Had it succeeded it only would have required the corporation to form a committee to investigate the process whereby one of its products was produced. Lovenheim likely knew that no such investigation was necessary, since as far as he knew, *pâté de foie gras* was always produced through the brutal force-feeding of geese.¹⁷ And so the entire shareholder proposal process, even if successful, would have resulted in

12. A Westlaw search reveals that the case has been cited in five published cases and nearly 150 SEC No-Action Letters.

13. Joyce Tischler, *The History of Animal Law, Part I (1972-1987)*, 1 STAN. J. ANIMAL L. & POL'Y 1, 40 (2008).

14. Memorandum of Law at 2-3, Iroquois Brands, Ltd., SEC File No. 1-5387 (Jan. 30, 1984) (on file with author) (submitted to the Securities and Exchange Commission's Division of Corporation Finance appealing the Division's decision regarding the Lovenheim Shareholder Proposal for Iroquois Brands, Ltd.).

15. Transcript of Hearing on Motion for Preliminary Injunction at 5, *Lovenheim v. Iroquois Brands, Ltd.*, 618 F. Supp. 554 (D.D.C. 1985) (No. 85-0734) (on file with the author) (statement of Lovenheim's counsel: "I will be the first to admit that in the 43 years of the shareholder proposal rule only two shareholder proposals have ever been passed, and they basically had management support.").

16. One scholar claimed that Lovenheim's petition had achieved "legendary proportions" as an example of the extent to which social issue proposals had become "trivial and nonsensical." Marilyn B. Cane, *The Revised SEC Shareholder Proxy Proposal System: Attitudes, Results and Perspectives*, 11 J. CORP. L. 57, 61 (1985).

17. See Transcript of Hearing on Motion for Preliminary Injunction, *supra* note 15, at 7-8 (statement of Lovenheim's counsel acknowledging that force-feeding is the only way *pâté de foie gras* is produced).

a report which would have confirmed what the shareholders already knew when they overwhelmingly rejected the same proposal in 1983.

This Article is a Law Story.¹⁸ Law Stories have many purposes, but their main goal is to supplement and demystify the case method of legal pedagogy.¹⁹ The case method has been criticized for presenting students with the law more or less as a *fait accompli*. The case method assumes a pre-existing body of law that students passively learn rather than learning to think of the law as something that they will have a hand in shaping.²⁰ By placing the (mostly appellate) opinions that law students read in their various historical contexts, Law Stories transport students back to a point where the law was uncertain and thus enable them to better imagine alternatives to existing legal rules and to appreciate the reasoning underling those rules.

Both Peter Lovenheim and *Lovenheim*,²¹ as well as the dynamic of shareholder proposals, turn out to be far more complicated than the opinion would lead one to expect, and that is why the case provides the basis for an especially rich Law Story. First, although Peter Lovenheim looks, when we are first introduced to him, like a typical shareholder activist, who was much more interested in pushing a social agenda than in promoting good corporate governance, he is actually more like the ideal shareholder proponent. He invested in Iroquois to make a profit, and he submitted his proposal because he sincerely believed that the distribution of *pâté de foie gras* was inconsistent with Iroquois'

18. Many Law Stories are collected in Foundation Press's LAW STORIES series. A complete listing of the books in the series is provided on Foundation Press's website: West Academic, Faculty Online Store, <http://www.westacademic.com/Professors/ProductSearchResults.aspx?tab=6&series=177&searchty=peasstring=ADVANCED-SEARCH> (last visited Nov. 7, 2010).

19. See Paul L. Caron, *Back to the Future: Teaching Law through Law Stories*, 71 U. CIN. L. REV. 405, 406 (2002) (making the "modest claim" that Law Stories can enrich classroom teaching through the case method). In 2005, the JOURNAL OF LEGAL EDUCATION recognized the importance of the Law Stories approach by devoting a section of one of its issues to *Teaching Law Stories*. See Leslie Bender, *Teaching Torts Stories*, 55 J. LEG. EDUC. 108 (2005) (book review); Nancy S. Marder, *Teaching Civil Procedure Stories*, 55 J. LEG. EDUC. 138 (2005) (book review); Ajay K. Mehorata, *Teaching Tax Stories*, 55 J. LEG. EDUC. 116 (2005) (book review); Thomas Ross, *Teaching Constitutional Law Stories*, 55 J. LEG. EDUC. 126 (2005) (book review); Laura S. Underkuffler, *Teaching Property Stories*, 55 J. LEG. EDUC. 152 (2005) (book review).

20. Edward Rubin, *What's Wrong With Langdell's Method and What to Do About It*, 60 VAND. L. REV. 609, 649 (2007); see also Karl N. Llewellyn, *The Current Crisis in Legal Education*, 1 J. LEG. EDUC. 211, 212 (1948) (faulting the case method for providing solutions to the problems posed in advance and thus not encouraging students to develop their own powers of reasoning and problem-solving).

21. 618 F. Supp. 554 (D.D.C. 1985).

corporate purposes and would do harm to the corporation's reputation and thus to its good-will value.

Second, although Lovenheim's proposal did not get very many votes from his fellow shareholders, Lovenheim regarded the exercise as a success because soon after the shareholder vote, Iroquois decided to discontinue distribution of *pâté de foie gras*. His success, or what he regarded as success, led Lovenheim to pursue other social goals through the shareholder proposal mechanism. His experience as a proponent led him to work with other like-minded shareholders on issues relevant to the corporations whose shares they owned. The shareholder proposal mechanism thus stimulates shareholder involvement in corporate governance. The story behind *Lovenheim* thus illustrates the numerous legal and non-legal consequences of a legal rule.

In Part II, this Article explores the law of shareholder proposals and the reasons why the SEC and the courts permit proposals relating to social or ethical issues (social proposals) so long as those issues relate to the corporation's business. The focus here is on the regulation of such social proposals. Other regulations permitting the exclusion of shareholder proposals will be discussed only to the extent that they interact with the Rule relating to social proposals. Part III presents the complete narrative of the *Lovenheim* case, providing details that are not captured in the decision or in the limited secondary literature relating to the case. Part IV explores the legal landscape in the aftermath of *Lovenheim*. The decision may well have been a surprising one, and this final section explores the reasons why the decision remains the leading case on social proposals.

As discussed in Part IV of the Article, opinions on the value of social proposals hinge on opinions on the purposes of corporations and the roles of shareholders in the corporations in which they own shares. Corporations seem to recognize the value of permitting social proposals, as they can provide a relatively inexpensive safety valve for dissent²² and thus permit the kind of beneficial exchange between management and shareholders that promotes the legitimacy of corporate decisionmaking processes. While corporations might regard these benefits as slight, the expense of social proposals is also very small. Corporations thus have little reason to appear to be attempting to obstruct one avenue of meaningful dialogue between management and

22. Donald E. Schwartz & Elliott J. Weiss, *An Assessment of the SEC Shareholder Proposal Rule*, 65 GEO. L.J. 635, 635 (1977); Melvin Aron Eisenberg, *Access to the Corporate Proxy Machinery*, 83 HARV. L. REV. 1489, 1494 (1970).

shareholders when the traffic along that avenue relieves stress from the system and thus helps guarantee that the main arteries of commerce will not be blocked.

II. HISTORY OF SEC IMPLEMENTATION OF SECTION 14(A) OF THE SECURITIES EXCHANGE ACT OF 1934

One might reasonably ask why we permit shareholder proposals in the first place. After all, it is a fundamental premise of corporate governance that managers manage.²³ Shareholders may be the beneficial owners of the corporation, but the separation of ownership and control is one of the key advantages of the corporate form.²⁴ Although shareholder activism has always been one of the ingredients of U.S. corporate governance,²⁵ Congress had acted in the early twentieth century to limit the ability of financial institutions to participate in corporate affairs.²⁶ However, in response to its perception that corporate management was abusing the proxy solicitation process,²⁷ Congress granted the Securities and Exchange Commission (the SEC) broad power to regulate proxy solicitations in section 14(a) of the '34 Act,²⁸ and the current form of

23. See, e.g., DEL. CODE ANN. tit. 8, § 141(a) (West 2010) (“The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors . . .”); *Paramount Commc’ns v. QVC Network, Inc.*, 637 A.2d 34, 42 (Del. Sup. Ct. 1994) (“Under normal circumstances, neither the courts nor the stockholders should interfere with the managerial decisions of the directors.”); *Brooks v. Standard Oil Co.*, 308 F. Supp. 810, 814 (S.D.N.Y. 1969) (citing general corporate principles granting broad discretion to corporate management in permitting Standard Oil to exclude a shareholder proposal related to fostering the development of petroleum reserves and working to create an international regime to manage the exploitation of mineral resources).

24. JAMES D. COX & THOMAS LEE HAZEN, *CORPORATIONS* 7 (2d ed. 2003) (noting that centralized administration is a necessity in a large corporation and that shareholders as such do not participate in the day-to-day management of the corporations); Eugene F. Fama & Michael C. Jensen, *Separation of Ownership and Control*, 26 J. L. & Econ. 301, 301-02 (1983) (arguing that “separation of decision and risk-bearing functions survives . . . in part because of the benefits of specialization of management and risk bearing but also because of an effective common approach to controlling the agency problems caused by separation of decision and risk-bearing functions.”).

25. See Stuart L. Gillian & Laura T. Starks, *The Evolution of Shareholder Activism in the United States*, 19 J. APPLIED CORP. FIN. 55, 55 (2007) (noting the role of financial institutions as shareholder activists in the early 20th century).

26. See *id.* (citing the Glass Steagall Act as well as regulatory reforms that followed the 1929 stock market crash, which had the cumulative effect of widening the gap between ownership and control in U.S. public corporations).

27. See Schwartz & Weiss, *supra* note 22, at 636 (claiming that, prior to 1934, management was soliciting proxies without informing shareholders of the matters to be considered at the annual shareholder meeting and then using the favorable proxies thus obtained to control the meeting and for other questionable purposes).

28. Section 14(a) of the '34 Act provides:

It shall be unlawful for any person, by the use of the mails or by any means or

shareholder activism is a product of an SEC rule first introduced in 1942,²⁹ the predecessor to the current Rule.³⁰ The Rule requires management to include in its proxy materials, sent out in advance of annual shareholder meetings, shareholder proposals to be voted on at those meetings so long as the shareholder meets certain conditions to qualify as a proponent.³¹

Since section 14(a) simply prohibits deceptive practices in the solicitation of proxies, it is not obvious that the Rule implements the congressional legislation.³² The SEC interpreted section 14(a) as insuring fair corporate suffrage and “shareholders who were enlightened not only as to the financial condition of the corporation, but also as to the major questions of policy, which are decided at stockholders’ meetings.”³³ In order to ensure that proxy materials accurately reflected all issues that would arise at an annual meeting, the SEC interpreted its own rules to permit shareholders to present proposals at annual meetings.³⁴ As one court put it, “[C]orporate circulation of proxy materials which fail to make reference to a shareholder’s intention to present a proper proposal at the annual meeting renders the solicitation inherently misleading.”³⁵ Others have pointed out that these rules were

instrumentality of interstate commerce or of any facility of a national securities exchange or otherwise, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors, to solicit or to permit the use of his name to solicit any proxy or consent or authorization in respect of any security (other than an exempted security) registered pursuant to [section 12 of the '34 Act].

Securities Exchange Act of 1934, ch. 404, 48 Stat. 895 (1934) (codified as amended at 15 U.S.C. § 78n(a) (West 2010)) (amended by PL 111-203, 124 Stat. 1376 (July 21, 2010)).

29. The Rule was first designated Rule X-14A-7. Duty of Management to Set Forth Stockholders’ Proposals, Exchange Act Release No. 3347, 1942 WL 34864 (Dec. 18, 1942).

30. Gillian & Starks, *supra* note 25, at 55.

31. In its current version, the Rule requires that shareholders hold a minimum of \$2,000 worth of shares in the corporation or more than 1% of the corporation’s outstanding shares and hold those shares for a minimum of one year prior to making the proposal. 17 C.F.R. § 240.14a-8(b)(1) (2010).

32. See George W. Dent, *SEC Rule 14a-8: A Study in Regulatory Failure*, 30 N.Y.L. SCH. L. REV. 1, 2 (1985) (noting that neither the text nor the legislative history of section 14(a) mentions shareholder proposals); Susan W. Liebler, *A Proposal to Rescind the Shareholder Proposal Rule*, 18 GA. L. REV. 425, 465-66 (1984) (arguing that the Rule is hardly likely to achieve Congressional intent to assure fair corporate suffrage).

33. *Amalgamated Clothing and Textile Workers Union v. Wal-Mart Stores, Inc.*, 821 F. Supp. 877, 882 (S.D.N.Y. 1993) (internal citations and quotations omitted).

34. *Id.*

35. *N.Y.C. Emps.’ Ret. Sys. v. Am. Brands, Inc.*, 634 F. Supp. 1382, 1386 (S.D.N.Y. 1986).

necessary in any case to safeguard the rights of shareholders recognized under state law.³⁶

A. *Implementation of the Rule 1942-1970*

In enacting section 14 of the '34 Act, Congress responded to an unpleasant by-product of the separation of ownership and control in the structure of corporations. “[A]s management became divorced from ownership and came under the control of banking groups, men forgot that they were dealing with the savings of men and the making of profits became an impersonal thing.”³⁷ Congress chose to regulate corporate proxies as one mechanism for preventing management from circumventing “fair corporate suffrage.”³⁸

1. Overview of SEC Regulation of Social Proposals

The SEC’s initial regulatory efforts in this area were directed at promoting “full and fair corporate disclosure regarding management proxy materials.”³⁹ In 1942, the SEC took the logical next step by adopting a rule that required management to include in its proxy materials shareholder proposals that constituted a “proper subject for action by security holders.”⁴⁰ This seemed to offer shareholders an extensive right to provide their input to management, but the SEC immediately saw the danger that shareholders would use the proposal mechanism to raise matters that bore little relationship to company’s affairs. In 1945, the Commission issued a release opining that “proposals which deal with general political, social or economic matters” are not proper subjects for shareholder action.⁴¹

36. See, e.g., DEL. CODE ANN. tit. 8, § 211(b) (mandating an annual shareholder meeting at which “any other proper business may be transacted”); see also Milton V. Freeman, *An Estimate of the Practical Consequences of the Stockholder’s Proposal Rule*, 34 U. DET. L.J. 549, 549 (1957) (calling fundamental aspects of Rule 14a-8 “an almost necessary consequence of the status of the individual shareholder under the laws of the various states of incorporation”). Freeman served in the SEC’s General Counsel Office from 1934-42 and as its Assistant Solicitor from 1942-46. *Id.* at 549 n.*.

37. *Med. Comm. for Human Rights v. SEC*, 432 F.2d 659, 676 (D.C. Cir. 1970) (quoting H.R. Rep. No. 73-1383, at 13 (1934)).

38. *Id.* (quoting H.R. Rep. No. 73-1383, at 13 (1934)).

39. *Id.* at 677 (citing 3 Fed. Reg. 1991 (1938); 5 Fed. Reg. 174 (1940)).

40. *Duty of Management to Set Forth Stockholders’ Proposals*, Exchange Act Release No. 3347, 1942 WL 34864 (Dec. 18, 1942).

41. Exchange Act Release No. 3638, 1945 WL 27415 (Jan. 3, 1945) (interpretation of Rule X-14A-7).

Between 1943 and 1970, shareholders submitted proposals on a variety of issues, but the main focus of shareholder activism in the years between World War II and the Vietnam War was corporate governance.⁴² Shareholders sought accountability from boards and management and improved performance that would increase the value of their shares.⁴³ There arose in the 1940s the phenomenon of the “gadfly investor.” Three such investors, Lewis and John Gilbert⁴⁴ and Evelyn Davis, still accounted for 30% of the resolutions submitted to corporations as late as 1982.⁴⁵ Their prominence among proponents led to cries that the process was being abused by people who were not interested in the economic well-being of the corporation but by people promoting “crackpot” ideas or “afflicted with an insatiate desire for personal publicity.”⁴⁶

The SEC’s approach to shareholder proposals has tended to mirror the times. As one commentator put it, in the 1950s, the SEC “added layers of conditions to the rule and gutted meaningful shareholder access.”⁴⁷ The SEC relaxed its restrictions during the Vietnam and Watergate eras before again seeking to “squelch access” during the more conservative 1980s.⁴⁸ In 1984, the SEC granted no-action letters to 78% of the corporations that requested them.⁴⁹ The trend towards a restrictive reading of shareholder rights continued into the next decade. By the mid-1990s, the SEC was 30% more likely to permit the exclusion of proposals relating to corporations’ social responsibilities than it had been in the 1980s.⁵⁰

42. See Gillian and Starks, *supra* note 25, at 56 (finding that, as late as 1978, 611 of 790 proposals received by member companies of the American Society of Corporate Secretaries dealt with governance issues).

43. *Id.* (characterizing the first three decades of shareholder proposals as “aimed at improving performance and raising share values”).

44. Lewis Gilbert had been called the “most celebrated minority stockholder.” LOUIS LOSS, 2 SECURITIES REGULATIONS 903 n.182 (2d ed. 1961). His main concerns were undeclared dividends and the installation of accounting and monitoring devices to improve directors’ accountability to shareholders. Patrick J. Ryan, *Rule 14a-8, Institutional Shareholder Proposals, and Corporate Democracy* 23 GA. L. REV. 97, 117 n.77 (1988). He and his brother accounted for nearly half the shareholder proposals offered from 1948-1951 and for nearly 2/3 of the proposals offered in 1955. Alan R. Palmiter, *The Shareholder Proposal Rule: A Failed Experiment in Merit Regulation*, 45 ALA. L. REV. 879, 897 n.74 (1994).

45. Gillian and Starks, *supra* note 25, at 56.

46. See Arthur D. Chilgren, *A Plea for Relief from Proxy Rule 14a-8*, 19 BUS. LAW. 303, 303-04 (1963) (finding it inconceivable that the majority of shareholder proposals “result from stock purchases made with any serious investment intent.”).

47. Palmiter, *supra* note 44, at 879-80.

48. *Id.* at 880.

49. Cane, *supra* note 16, at 60.

50. Palmiter, *supra* note 44, at 882, 913.

2. The Rule in the Courts

The first significant court case testing shareholders' ability to challenge management on issues of corporate governance through the mechanism of the shareholder proposal came in *SEC v. Transamerica Corp.*⁵¹ The main issue in the case was the scope of the "proper subject" for shareholder action referenced in the Rule.⁵² Transamerica argued that shareholder proposals must relate to a subject matter on which shareholders were permitted to vote under all legal requirements, including those found in the corporation's charter and by-laws.⁵³ The SEC took the broader position permitting proposals on any subject matter in which a shareholder had an interest under state law.⁵⁴

The court sided with the SEC, stressing that Transamerica's reading of the Rule would circumvent Congress' intent "to require fair opportunity for the operation of corporate suffrage."⁵⁵ Because a corporation must be run for the benefit of its stockholders and not for that of its managers,⁵⁶ management could not be permitted to place technical provisions of a corporation's charter or by-laws beyond the reach of the shareholder vote. "The control of great corporations by a very few persons was the abuse at which Congress struck in enacting section 14(a)."⁵⁷

Although it supported shareholder rights in the *Transamerica* case, between 1948 and 1954, the SEC repeatedly revised the Rule to limit the ability of shareholders to make proposals. In 1948, the SEC permitted corporations to exclude from their proxy statements proposals relating to personal grievances and proposals submitted by shareholders who did not attend the annual meeting, either in person or by proxy.⁵⁸ In 1952, the SEC made a further attempt to prevent shareholder proposals from becoming a forum for the airing of political grievances, permitting corporate managers to exclude proposals submitted "primarily for the purpose of promoting general economic, political, racial, religious, social or similar causes."⁵⁹ The propriety of this regulation was not

51. 163 F.2d 511 (3d. Cir. 1947).

52. *Id.* at 515.

53. *Id.*

54. *Id.*

55. *Id.* at 518.

56. *Id.* at 517.

57. *Id.* at 518.

58. Adoption of Amendments to Proxy Rules, Exchange Act Release No. 4185, 1948 WL 28695 (Nov. 5, 1948).

59. Amendment to Proxy Rules, Exchange Act Release No. 4475, 1952 WL 5254 (Dec. 11, 1952).

tested for nearly two decades.⁶⁰ The SEC again expanded the permissible grounds for exclusion in 1954, permitting corporate management to exclude proposals relating to “ordinary business operations,” proposals that would violate state law and resubmitted proposals that had recently been overwhelmingly rejected.⁶¹

Like these SEC revisions to the Rule, the case law in the two decades following the *Transamerica*⁶² decision was decidedly favorable to the discretion of both corporate management and the SEC, both of which inclined towards excluding proposals, especially social proposals. For example, in *Peck v. Greyhound Corp.*,⁶³ shareholder Peck brought a proposal calling on the corporation to abolish its segregated seating system in the South.⁶⁴ Greyhound sought to exclude the proposal and relied on the 1945 SEC release cited earlier,⁶⁵ stating that it was not the intent of the Rule “to permit stockholders to obtain the consensus of other stockholders with respect to matters which are of a general political, social or economic nature.”⁶⁶ The SEC staff agreed with the corporation’s assessment of the propriety of the proposal, finding that it was not on a “proper subject.”⁶⁷ The *Peck* court did not go so far as to endorse Greyhound’s interpretation of the 1945 SEC Release.⁶⁸ However, the court denied Peck’s motion to enjoin Greyhound from soliciting proxies and holding its shareholder meeting unless Peck’s proposal was included in Greyhound’s proxy materials, finding that Peck had failed to exhaust available administrative remedies.⁶⁹ The court believed that Peck must first pursue SEC review of its staff’s no-action letter before seeking the injunction.⁷⁰ In addition, the court noted that considerable deference was due to the SEC’s interpretation of its own

60. See *Med. Comm. for Human Rights v. SEC*, 432 F.2d 659, 676 (D.C. Cir. 1970) (“So far as we have been able to determine, the Commission’s interpretation or application of this rule has not been considered by the courts.”).

61. Adoption of Amendments to Proxy Rules, Exchange Act Release No. 4979, 1954 WL 5772 (Jan. 6, 1954).

62. 163 F.2d 511 (3d. Cir. 1947).

63. 97 F. Supp. 679 (S.D.N.Y. 1951).

64. *Id.* at 680.

65. See Exchange Act Release No. 3638, *supra* note 41.

66. *Peck*, 97 F. Supp. at 680 (citing Exchange Act Release No. 3638, *supra* note 41).

67. *Id.* at 680.

68. *Id.* at 681.

69. *Id.* at 680-81.

70. *Id.* at 681.

rules and also found that Peck could not establish that he would be irreparably harmed if his injunction were denied.⁷¹

The trend towards deference to SEC decisions continued in *Dyer v. SEC*,⁷² which raised the same kinds of corporate governance issues that the Third Circuit had found a proper subject for shareholder proposals in *Transamerica*.⁷³ In *Dyer*, plaintiffs sought to force management of the Union Electric Company to include in its proxy materials eleven resolutions, by-law amendments, and amendments to the articles of incorporation.⁷⁴ Some of the proposals had been the subject of a previous suit; others had been submitted and overwhelmingly rejected by shareholders in recent shareholder meetings.⁷⁵ The *Dyer* court recognized the *Transamerica* decision as one with which it needed to come to terms. However, it found the two cases easily distinguishable. In *Transamerica*, the SEC had supported inclusion of the proposals, and doing so was in accordance with Delaware law.⁷⁶ In *Dyer*, by contrast, the SEC supported the corporation's decision to exclude the proposals.⁷⁷ In addition, the court characterized as "almost fanciful" petitioners' argument that the SEC was without rational basis to exclude their proposals, which were inconsistent with Missouri law, when management had agreed to the inclusion of a substantively similar proposal that was properly submitted under Missouri law.⁷⁸

While there seems little doubt that the *Dyer* court reached the right conclusions with respect to the proposals at issue in that case, the opinion is significant in the deferential language it adopted with respect to determinations of the SEC staff.⁷⁹ The court took the lack of case law challenging SEC determinations on shareholder proposals as evidence

71. *Id.* The proposal may have been excludable in any case because it would have put the company in violation of state laws then assumed to be valid. *See Med. Comm. for Human Rights v. SEC*, 432 F.2d 659, 678 (D.C. Cir. 1970).

72. 289 F.2d 242 (8th Cir. 1961).

73. 163 F.2d 511 (3d. Cir. 1947).

74. *Dyer*, 289 F.2d at 243.

75. *Id.*

76. *Id.* at 246.

77. *Id.* at 423.

78. *Id.*

79. *See* Daniel E. Lazaroff, *Promoting Corporate Democracy and Social Responsibility: The Need to Reform the Federal Proxy Rules on Shareholder Proposals*, 50 RUTGERS. L. REV. 33, 50 (1997) (finding a deferential posture in the court's reference to a "lack of reported decisions" relating to shareholder proposals as evidencing general acceptance of the SEC's regulatory judgments in the area).

that courts and shareholders alike were willing to accept such determinations as within the province of the SEC.⁸⁰

Deference to management and the SEC characterized decisions in this area into the late 1960s, when the courts dealt another blow to shareholder activism in *Brooks v. Standard Oil Co.*⁸¹ In that case, plaintiff offered a resolution that called on Standard Oil to intensify its effort to encourage exploration of the world's continental shelves for oil reserves and to encourage the creation of an international regime over undersea mineral resources.⁸² Standard Oil notified the SEC that it intended to exclude the proposal, asserting that the proposal could be omitted because it: (1) was not on a proper subject for shareholder action; (2) related to ordinary business matters; and (3) primarily sought to promote a general economic or political cause.⁸³ Plaintiff, an attorney with expertise in the utilization of underwater mineral resources beyond national jurisdiction,⁸⁴ sought a declaratory judgment that his resolution was on a proper subject for action by shareholders.⁸⁵

The SEC issued Standard Oil a no-action letter on the ground that the proposal was not a proper subject for action by shareholders.⁸⁶ In so doing, the SEC clearly violated its own rules.⁸⁷ The Rule required that, if the corporation claimed a legal ground for the omission of a shareholder proposal, the corporation must include a "supporting opinion of counsel" with its notice of intention to omit.⁸⁸ Since Standard Oil provided no such opinion of counsel, it could not possibly have met its burden of production.⁸⁹ However, the court concluded that plaintiff was not harmed by the SEC's failure to adhere to its own procedural requirements, as Standard Oil's opinion of counsel would have relied on the same legal arguments as Standard Oil presented in the court case.⁹⁰ Moreover, citing an earlier ruling in the *Dyer*⁹¹ litigation, the court

80. See *Dyer*, 289 F.2d at 245 ("Presumably, from the lack of reported decisions, the denials of attempts by stockholders in other public holding company situations to have inclusions made in management's proxy material must generally have had their end in an acceptance of the regulatory judgment which the Commission has exercised in the particular situation.").

81. 308 F. Supp. 810 (S.D.N.Y. 1969).

82. *Id.* at 811.

83. *Id.* at 811-12 (citing 17 C.F.R. § 240.14a-8(c)(1), (2), (5)).

84. *Id.* at 811.

85. *Id.* at 810.

86. *Id.* at 812.

87. *Id.* at 813 (citing Adoption of Amendments to Proxy Rules, *supra* note 61).

88. *Id.* at 811 n.2 (citing 17 C.F.R. § 240.14a-8(d)).

89. *Id.* at 811 n.2.

90. *Id.*

91. 289 F.2d 242.

adopted a highly deferential approach to review of SEC no-action letters, accepting the SEC's judgment "unless it can be said that what has been done is without any rational basis on all the elements involved."⁹²

The only issue for the court to resolve then was whether the SEC had correctly construed New Jersey law relating to the relative powers of corporate management and shareholders. The parties agreed that there was no New Jersey authority for whether or not plaintiff's proposal was a proper subject for shareholder action.⁹³ However, the court cited both New Jersey law and the Standard Oil by-laws, which both provided in nearly identical language that "the business and affairs of [the] corporation shall be managed by its board."⁹⁴ The court further relied on case law to extend something like the business judgment rule⁹⁵ to the shareholder proposal context as well. The court cited two opinions of New Jersey's Chancery Court, one from 1891 and one from 1942. The first stated that "[q]uestions of policy of management . . . are left solely to the honest decision of the directors, if their powers are without limitation and free from restraint."⁹⁶ In the later case, the Chancery Court cited the "well-settled rule of law that questions of business policy devolve upon the officers and directors. . . ."⁹⁷ The court noted that most of the proposals that had been approved concerned matters relating to the selection, retention, and accountability of officers and directors⁹⁸ and appeared to treat that fact as evidence that corporations were only required to include such proposals in their proxy materials.

Thus, three decades after the SEC first adopted the Rule, the scope of the right of shareholders to bring proposals at annual meetings was

92. *Brooks v. Standard Oil, Co.*, 308 F. Supp. 810, 813 (S.D.N.Y. 1969) (citing *Dyer*, 266 F.2d at 38). The court also relied on *Peck* to support its deference to the SEC's construction of its own rules. *Id.* at 813 (citing *Peck v. Greyhound Corp.*, 97 F. Supp 679, 681 S.D.N.Y. 1951)).

93. *Id.* at 814.

94. *Id.*

95. The Delaware Supreme Court defines the business judgment rule as "a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company. Absent an abuse of discretion, that judgment will be respected by the courts." *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. Sup. Ct. 1984) (citations omitted), overruled by *Brehm v. Eisner*, 746 A.2d 244 (Del. Sup. Ct. 2000). See D. A. Jeremy Telman, *The Business Judgment Rule, Disclosure and Executive Compensation*, 81 TUL. L. REV. 829, 833-38 (2007) (noting that the business judgment rule has been variously understood as a presumption, a heightened standard of review and a doctrine of judicial abstention).

96. *Brooks*, 308 F. Supp at 814 (citing *Ellerman v. Chi. Junction Ry. Co.*, 23 A. 287, 292 (N.J. Ch. 1891)).

97. *Id.* (citing *Laredef Corp. v. Fed. Seaboard Terra Cotta Corp.*, 25 A.2d 433, 437 (N.J. Ch. 1942)).

98. *Id.*

narrowly circumscribed in two ways. First, the SEC was granting no-action letters with respect to all proposals except those relating to selection, compensation, and accountability of managers. Second, the courts had adopted a highly deferential approach to SEC decisions, even if those decisions were taken at the staff level. This trend was to change dramatically with the D.C. Circuit's decision in *Medical Committee for Human Rights v. SEC*.⁹⁹

B. *The Medical Committee Opinion*

The Medical Committee for Human Rights (Medical Committee) obtained, by gift, shares in the Dow Chemical Company (Dow).¹⁰⁰ On March 11, 1968, the Medical Committee's national chairman, Dr. Quentin Young, wrote to Dow and enclosed a first version of the Medical Committee's shareholder proposal.¹⁰¹ The proposal requested the Board of Directors to amend Dow's certificate of incorporation to provide "that napalm¹⁰² shall not be sold to any buyer unless that buyer gives reasonable assurances that the substance will not be used on or against human beings."¹⁰³ In the accompanying letter, Dr. Young conceded that its primary motivation was the Medical Committee's concerns for human life, but he also noted that the Medical Committee's investment advisers suggested that napalm production "is also bad for our company's business as it is being used in the Vietnamese War" in part because it was making it "increasingly hard to recruit the highly intelligent, well-motivated, young college men so important for company growth."¹⁰⁴ In addition, the letter noted that the impact on the company for its decision to manufacture napalm was global.¹⁰⁵

Dr. Young's language, espousing an economic interest in the corporation, was necessary to overcome language in the Rule that permitted a corporation to exclude a proposal "if it clearly appears that the proposal is submitted . . . primarily for the purpose of promoting general economic, political, racial, religious, social or similar causes."¹⁰⁶

99. 432 F.2d 659 (D.C. Cir. 1970).

100. *Id.* at 661.

101. *Id.*

102. *Id.* Napalm is an aluminum-based soap, which is combined with gasoline to form a syrup used in chemical warfare. *Id.* It was developed by Harvard University scientists during World War II in order to increase the range of flamethrowers while also greatly increasing the temperature at which the fuel in such flamethrowers burned. *Id.* at 661 n.1.

103. *Id.* at 662.

104. *Med. Comm.*, 432 F.2d at 662.

105. *Id.*

106. *Id.* at 676 (citing 17 C.F.R. § 240.14a-8(c) (1970)).

Still, the original proposal was susceptible to exclusion under another regulation that permitted omission of proposals seeking management action “with respect to a matter relating to the conduct of the ordinary business operations of the issuer.”¹⁰⁷

The Medical Committee had submitted the 1968 version of its proposal after the deadline for submitting such proposals and Dow, not surprisingly, refused to include it in its proxy statement.¹⁰⁸ In January 1969, having received no further communications from Dow, the Medical Committee re-submitted its proposal.¹⁰⁹ After Dow notified the Medical Committee that it intended to omit the proposal from its proxy statement, the Medical Committee sought to revise the proposal.¹¹⁰ Acknowledging that “management should be allowed to decide to whom and under what circumstances it will sell its products,” the Medical Committee nonetheless urged that “the company’s owners have not only the legal power but also the historic and economic obligation to determine what products their company will manufacture.”¹¹¹ Accordingly, the Medical Committee enclosed a revised proposal requesting that the Board “consider the advisability of adopting a resolution setting forth an amendment to [Dow’s certificate of incorporation] that the company shall not make napalm.”¹¹²

Dow was unmoved by the amendments and sent the SEC a memorandum stating its reasons for omitting the proposal.¹¹³ The SEC Division of Corporation Finance granted a no-action letter.¹¹⁴ The Medical Committee duly appealed, but the full Commission approved the recommendation of its Division of Corporation Finance.¹¹⁵ The Medical Committee next appealed that decision to the Court of Appeals for the D.C. Circuit.¹¹⁶

Given the case law since *Transamerica*,¹¹⁷ it was not entirely clear that the federal courts had jurisdiction to review SEC decisions relating to shareholder proposals, or that such review should occur in the Court

107. *Id.* at 679 (citing 17 C.F.R. § 240.14a-8(c)(5) (1970)).

108. *Id.* at 662.

109. *Id.*

110. *Id.* at 663.

111. *Id.* at 662.

112. *Id.* at 663.

113. *Id.*

114. *Id.*

115. *Id.*

116. *Id.*

117. 163 F.2d 511 (3d. Cir. 1947).

of Appeals.¹¹⁸ As the court noted,¹¹⁹ after the Southern District of New York's ruling in *Peck* that a shareholder must exhaust administrative remedies through appeal to the Commission itself before seeking review in a federal court,¹²⁰ shareholders would have faced quite a procedural conundrum if the D.C. Circuit had now ruled that exhaustion of administrative remedies barred a shareholder from review in a federal court. However, the D.C. Circuit also recognized that there was some dicta and some scholarly comment suggesting that no-action letters in the shareholder proposal context were not reviewable orders.¹²¹ Still, after an extended discussion,¹²² the D.C. Circuit concluded that the SEC determination was reviewable¹²³ in the Court of Appeals.¹²⁴

Having failed to persuade the Court of Appeals that it was without jurisdiction to review SEC decisions in such matters, the SEC nonetheless argued for a level of judicial deference to the SEC's views akin to that accorded to prosecutorial discretion.¹²⁵ The court did not feel the need to accord the SEC such deference, in large part because of evidence of frequent procedural irregularities in the SEC's internal review of shareholder proposals.¹²⁶ The most serious charge, the court noted, was

all too clearly illustrated by the record in the present case: the lack of articulated bases for past decisions encourages management to file shotgun objections to a shareholder proposal, urging every mildly

118. See *Med. Comm.*, 432 F.2d at 665 (noting that the most difficult issues in the case arise from Dow's and the SEC's claim that the SEC decision is not a reviewable order under section 25(a) of the Securities Exchange Act); *id.* at 672 (noting that "the essential question . . . is whether the district court is a more appropriate forum for adjudication of petitioner's claim than" the Court of Appeals).

119. *Id.* at 667 n.9.

120. See *supra* notes 70-71 and accompanying text.

121. See *Med. Comm.*, 432 F.2d at 666 n.5 (citing dictum from *Klasterin v. Roth*, 353 F.2d 182, 183 n.2 (2d Cir. 1965) and one article from a practitioners' publication but no holding on point). Subsequent to the *Medical Committee* case, two Circuit Courts adopted the position that SEC no-action letters are not reviewable orders. See *Amalgamated Clothing and Textile Workers Union v. SEC*, 15 F.3d 254, 257 (2d Cir. 1994) (finding that the proper course of action if a shareholder believes that a corporation has improperly refused to include a proposal is to seek judicial review of the propriety of that action in a district court); *Kixmiller v. SEC*, 492 F.2d 641, 645-46 (D.C. Cir. 1974) (dismissing action for want of jurisdiction and distinguishing *Medical Committee* on the ground that in that case the Commission had reviewed and affirmed the staff no-action recommendation and in the current case the Commission had refused comment on staff action).

122. *Med. Comm.*, 432 F.2d at 665-72.

123. *Id.* at 672.

124. *Id.*

125. *Id.* at 673.

126. *Id.* at 674.

plausible legal argument that inventive counsel can contrive, in the hope that the Commission will accept one of them.¹²⁷

The Court inferred that the effect of SEC “discretion” was to dispose of controversies through “calculated non-decisions that will eventually cause eager supplicants to give up in frustration and stop ‘bothering’ the agency.”¹²⁸ The court then proceeded with a limited review of the SEC’s determination: “if the Commission was found to have proceeded on erroneous legal principles, the Commission would be ordered to proceed within the framework of its own discretionary authority on the indicated correct principles.”¹²⁹ Although the Court deemed it “obvious to the point of banality to restate” Congress’ purpose in enacting section 14 of the Securities Exchange Act of 1934, it nonetheless noted that Congress’ intent was “to give true vitality to the concept of corporate democracy.”¹³⁰ That purpose could not possibly be frustrated by a remand to the SEC to articulate the grounds underlying the grant of its no-action letter.

The court then proceeded to a discussion of the merits of the case. As indicated above, Dow sought to exclude the Medical Committee’s proposal on two grounds: that its concerns were essentially political rather than economic and that it related to ordinary business operations.¹³¹ The court conceded that these two limitations on the corporation’s obligation to include shareholder proposals in its proxy materials were “on their face, consistent with the legislative purpose underlying section 14.”¹³² The court deemed it “fair to infer” that Congress would not have desired that proxy solicitations become a vehicle through which “malcontented shareholders [could] vent their spleen about irrelevant matters.”¹³³ Congress may well also have anticipated that “management cannot exercise its specialized talents effectively if corporate investors assert the power to dictate the minutiae of daily business decisions.”¹³⁴

Still, in language that indicated a radical shift from earlier case law, the court acknowledged the risk that the two exclusions could be construed so as to exclude almost any shareholder proposal on the

127. *Id.*

128. *Id.*

129. *Id.* at 675.

130. *Id.* at 676.

131. *Id.* at 665-72.

132. *Id.* at 678.

133. *Id.*

134. *Id.* at 679.

ground it is either too general or too specific.¹³⁵ The court found that Dow had attempted to either dash the Medical Committee's proposal against the Scylla of generality or to drown it in the Charybdis of specificity and that the SEC had accepted Dow's decision to exclude the proposal without even identifying which of these hazards had provided the substantive ground for its decision.¹³⁶

With respect to the claim that the Medical Committee's proposal was "too specific," in that it related to Dow's ordinary business operations and was thus excludable under Rule 14a-8(c)(5), the court remarked that the scope of ordinary business operations was to be determined based on governing state law.¹³⁷ However, Delaware law permits amendments to a corporation's certificate of incorporation so as to "change, substitute, enlarge or diminish the nature of the" corporation's business.¹³⁸ The court found no evidence in the record to support Dow's contention that the proposal was not for a proper purpose under Delaware law.¹³⁹ Departing from the reasoning of the *Brooks* court,¹⁴⁰ the *Medical Committee* court criticized the SEC for its "superficial analysis" of applicable state law and found that the SEC had failed to comply with its own requirement that management sustain the burden of proof when seeking to omit a shareholder proposal.¹⁴¹

The court characterized as "somewhat more substantial" Dow's argument that the proposal could be excluded as "too general" under Rule 14a-8(c)(2), which permitted exclusion of proposals that are primarily political in nature.¹⁴² However, the court was unpersuaded by the Dow's memorandum of counsel on the subject, which simply described the sorts of political protests of which Dow had been a target because of its government contracting in connection with the Vietnam War and then reached the "abrupt conclusion" that the proposal should therefore be excluded.¹⁴³ The court was unwilling to connect the dots and to treat the proposal as representing nothing more than another

135. *Id.*

136. *See id.* (stating that the SEC "made no attempt to choose between" the two "potentially conflicting arguments" and, relying on Dow's stated reasons, accepted Dow's decision to omit the proposals).

137. *Id.* at 680.

138. *Id.* at 680 n.29 (citing DEL. CODE ANN. tit. 8, § 242(a)(2), (d) (1968)).

139. *Id.* at 680.

140. *See supra* text accompanying notes 86-90.

141. *Med. Comm.*, 432 F.2d at 680.

142. *Id.*

143. *Id.*

example of protest tactics relating to Dow's contracts with the Department of Defense.¹⁴⁴

Here again, the court returned to Congress' intentions in passing section 14(a) of the '34 Act, whose "overriding purpose" it was "to assure to corporate shareholders the ability to exercise their right—some would say their duty—to control the important decisions which affect them in their capacity as stockholders and owners of the corporation."¹⁴⁵ In light of this congressional purpose, the court could find no reason why management should be permitted to

place obstacles in the path of shareholders who wish to present to their co-owners . . . the question of whether they wish to have their assets used in a manner which they believe to be more socially responsible but possibly less profitable than that which is dictated by present company policy.¹⁴⁶

Moreover, in this case, there was ample evidence that Dow's management was itself motivated by a political purpose and not by the profit motive. According to the court, Dow's own publications proclaimed:

[T]hat the decision to continue manufacturing and marketing napalm was made not because of business considerations, but in spite of them; that management in essence decided to pursue a course of activity which generated little profit for the shareholders and actively impaired the company's public relations and recruitment activities because management considered this action morally and politically desirable. . . . We think that there is a clear and compelling distinction between management's legitimate need for freedom to apply its expertise in matters of day-to-day business judgment, and management's patently illegitimate claim of power to treat modern corporations with their vast resources as personal satrapies implementing personal, political, or moral predilections. It could scarcely be argued that management is more qualified or more entitled to make these kinds of decisions than the shareholders who are the true beneficial owners of the corporation.¹⁴⁷

Not only did the court think that the corporation had not borne its burden under the SEC's regulations, it also asserted that the

144. *Id.* at 680 n.30.

145. *Id.* at 680-81.

146. *Id.* at 681.

147. *Id.*

regulations—at least as applied in this case—could not be harmonized with Congress’ intent in adopting section 14(a) of the ’34 Act.¹⁴⁸

The case was remanded to the SEC for reconsideration in light of the court’s opinion and with instructions that the basis for the SEC’s decision must appear in the record “not in conclusory terms but in sufficient detail to permit prompt and effective review.”¹⁴⁹ The SEC was sufficiently concerned about the consequences of the decision to appeal to the U.S. Supreme Court, which granted certiorari.¹⁵⁰ However, before the Court could decide the case, Dow included the proposal in its annual proxy materials, and it received votes from less than 3% of the shares that participated.¹⁵¹ The Supreme Court reasoned that, given this meager support for the proposal, Dow may decide to include it if it were re-submitted in the future rather than litigate.¹⁵² The facts thus no longer presented an active case or controversy, and the case was dismissed as moot.¹⁵³ The status of the D.C. Circuit’s opinion was thus unclear.

C. *The Effect of Medical Committee*

In the aftermath of *Medical Committee*, the number of shareholder proposals increased dramatically, as did the number of proposals relating to social issues.¹⁵⁴ In addition, the SEC for the first time revised the Rule in a way that restricted the ability of management to exclude such proposals from its proxy materials.¹⁵⁵ In 1972, the SEC revised the portion of the Rule relating to the exclusion of social proposals, permitting the exclusion of proposals only if they were not “significantly related to the business of the issuer or not within its control.”¹⁵⁶ In 1976,

148. *Id.*

149. *Id.* at 682.

150. SEC v. Med. Comm. for Human Rights, 401 U.S. 973 (1971).

151. SEC v. Med. Comm. for Human Rights, 404 U.S. 403, 405-06 (1972).

152. *Id.* at 406.

153. *Id.* at 407.

154. Estimates range on the number of social proposals offered during this period, but there is no doubt that there was a significant increase. See Liebler, *supra* note 32, at 431 (stating that the number of social proposals increased from six in 1972 to 322 in 1976); Schwartz & Weiss, *supra* note 22, at 637 n.11 (stating that there were 133 social proposals raised in eighty-eight separate shareholder meetings in 1976, both of which were record highs). Liebler provides a statistical breakdown on shareholder proposals between 1975-76 and 1982-83. During that period, social proposals accounted for a high of 46.3% of all proposals in 1975-76 and reached their numerical peak in 1980-81, when 372 were offered. Liebler, *supra* note 32, app. at tbl.1. Rates at which proposals were excluded pursuant to SEC no-action letters also peaked in 1975-76, when 38.5% of all proposals were excluded. *Id.*

155. Solicitation of Proxies, Exchange Act Release No. 9784, 1972 WL 125400 (Sept. 22, 1972).

156. *Id.*

the SEC again revised the Rule, eliminating all reference to social or political proposals.¹⁵⁷

As we shall see, the *Medical Committee* opinion influenced Peter Lovenheim to become a shareholder activist. He was not alone. Between 1976 and 1983, social proposals accounted for over 20% of all proposals received each year by the American Society of Corporate Secretaries.¹⁵⁸ However, after a 1983 revision of the Rule that required a proponent to own \$1,000 worth of stock in the issuer, the number of social proposals dropped by more than half.¹⁵⁹

III. FAIR IS FOWL: THE STORY OF *LOVENHEIM V. IROQUOIS BRANDS*

Peter Lovenheim was something of an amateur investor. When he found out about a company that he liked, he would buy shares. In the fall of 1981, he bought 200 shares of the common stock of Iroquois¹⁶⁰ on the advice of his fiancée, who was a nutritionist,¹⁶¹ and had recommended the Schiff line of vitamins that Iroquois distributed.¹⁶² Lovenheim also saw potential for Iroquois' stock "because of its involvement in the expanding market for health foods and natural foods."¹⁶³ Within a few months of purchasing his Iroquois stock, Lovenheim received proxy materials from which he learned that Iroquois marketed Eduard Artzner *pâté de foie gras* in the United States.¹⁶⁴ *Foie gras* is a gourmet food produced from the livers of domesticated geese raised on a carbohydrate-rich diet.¹⁶⁵

157. See Palmiter, *supra* note 44, at 911 (stating that the number of social and political proposals "exploded" after the 1976 reforms).

158. Liebler, *supra* note 32, at 466.

159. See Bruce Ingersoll, *Annual Meetings Are Much Calmer Affairs Under Changed SEC Shareholder Rules*, WALL ST. J., Apr. 24, 1985 ("The number of shareholder resolutions filed on social and ethical issues fell from 215 in 1983 to 93 [in 1984] and 83 [in 1985] . . .").

160. Affidavit of Peter C. Lovenheim at 5, *Lovenheim v. Iroquois Brands, Ltd.*, 618 F. Supp. 554 (D.D.C. 1985) (No. 85-0734) (on file with the author).

161. See PETER C. LOVENHEIM, *PORTRAIT OF A BURGER AS A YOUNG CALF: THE TRUE STORY OF ONE MAN, TWO COWS AND THE FEEDING OF A NATION* 64 (2002) (describing his wife as a nutritionist).

162. Telephone Interview with Peter C. Lovenheim (Mar. 5, 2009).

163. Affidavit of Peter C. Lovenheim, *supra* note 160, at 2.

164. *Id.*

165. F. BARBARA ORLANS, ET AL., *THE HUMAN USE OF ANIMALS: CASE STUDIES IN ETHICAL CHOICE* 227 (1998).

A. *What's Good for the Goose: Lovenheim's First Shareholder Proposal*

Lovenheim had originally been attracted to Iroquois because the corporation marketed products that promoted healthy lifestyles.¹⁶⁶ He did not think that encouraging the consumption of *pâté de foie gras* was consistent with the rest of Iroquois' product lines, nor did he think that other like-minded shareholders would want Iroquois to be involved in the distribution of *pâté de foie gras* if the production of the product involved significant animal cruelty.¹⁶⁷ Although Lovenheim was working at the Humane Society at the time of the lawsuit¹⁶⁸ and was described in the press as “an animal rights activist,”¹⁶⁹ he would later describe himself as someone who did some work for the Humane Society when he was just out of school but was not “an animal rights person.”¹⁷⁰ Lovenheim was not a strict vegetarian.¹⁷¹

The corporation's view of itself was very different from the way Lovenheim understood it. Although it did market natural foods and vitamins as two of its product lines, those product lines were by no means central to the corporation's mission or identity. Iroquois started out as a brewery and, at the time Lovenheim invested, distributed many diverse product lines, ranging from Champale to Yoohoo, through numerous subsidiaries.¹⁷²

166. *Id.* at 229.

167. Telephone interview with Peter C. Lovenheim, *supra* note 162.

168. *See* Tischler, *supra* note 13, at 40.

169. *See* Jerry Knight, *Force-Feeding Moral Issues onto Corporate Agendas*, WASH. POST, Mar. 11, 1985, at Bus. 1 (referring to the case as a “landmark lawsuit” brought by “an animal rights activist”).

170. *See* LOVENHEIM, *supra* note 161, at 192 (expressing concern, as he was preparing to visit a slaughterhouse that he might be denied entry because of the company's suspicions as to his motives). Lovenheim never wanted to become a one-issue person. Interview with Peter C. Lovenheim (Sept. 27, 2009) (audio tape on file with author). He had worked as a freelance journalist during law school, and after he graduated, his first job was with a small non-profit that promoted the legal interests of journalists in freedom of information. *Id.* Having worked on that issue for a short time, and having written a couple of pieces of journalism that related to animal law, Lovenheim then moved to a position with the Humane Society. *Id.* He was there for only a couple of years before he moved on to his next project. *Id.*

171. *See id.* at 64 (“My diet mostly reflects the ambivalence I've felt since childhood about eating animals: sometimes I have; sometimes I haven't.”). Lovenheim claims that he has been a vegetarian since *Portrait of a Burger* was published, but his son claims to have seen him eating a turkey sandwich only recently. Interview with Peter C. Lovenheim, *supra* note 170.

172. Telephone interview with Ralph Halpern (July 10, 2009).

According to Lovenheim, the process of force-feeding usually begins when the birds are four-months old.¹⁷³ At farms where the process has been mechanized, the birds are placed in a metal brace and the neck is stretched so that a funnel may be inserted 10-12 inches down the bird's throat.¹⁷⁴ Four hundred grams of corn mash are then pumped into the birds' stomachs, while an elastic band around its neck prevents regurgitation.¹⁷⁵ Where the process is done by hand, the feeder uses a funnel and a stick to force the mash down the bird's throat.¹⁷⁶ The birds are force fed for between 15 and 28 days, and shortly thereafter they are slaughtered.¹⁷⁷ During the brief period of force-feeding, the geese double their weight, but their livers swell until they account for up to 10% of the bird's total weight. An ordinary goose liver weighs about 120 grams; the liver of a force-fed bird weighs between 800 and 1000 grams.¹⁷⁸ Up to 10% of the birds die before they can be slaughtered as a result of the forced feeding.¹⁷⁹

On May 10, 1982, Lovenheim wrote to Iroquois' management and requested that it look into the possibility that the *pâté* product that it was distributing was produced through forced-feeding of geese.¹⁸⁰ The corporation did not respond to that letter or to subsequent communications.¹⁸¹ So, on December 14, 1982, Lovenheim, on his own behalf and on behalf of the Humane Society, wrote a letter to Terence J. Fox, the president of Iroquois, enclosing a shareholder proposal for inclusion in the company's proxy materials for action at the next Iroquois annual shareholder meeting to be held in May 1983.¹⁸² The letter stated that the proposal was prepared in accordance with the relevant regulations promulgated by the SEC.¹⁸³ Lovenheim also notified the corporation that he intended to attend the annual shareholder meeting.¹⁸⁴

173. Lovenheim v. Iroquois Brands, 618 F. Supp. 554, 556 n.2 (D.D.C. 1985) (citing Affidavit of Peter C. Lovenheim, *supra* note 160).

174. *Id.*

175. *Id.*

176. *Id.*

177. ORLANS, *supra* note 165, at 229.

178. *Id.*

179. *Id.*

180. Transcript of Annual Meeting of Stockholders of Iroquois Brands Ltd. 12 (May 10, 1983) [hereinafter 1983 Annual Meeting Transcript] (on file with the author).

181. *Id.*

182. Letter from Peter C. Lovenheim to Terrence J. Fox, Chairman of the Bd, Iroquois Brands, Ltd. (Dec. 14, 1982) (on file with the author).

183. *Id.* (citing 7 C.F.R. 240.14a-8).

184. *Id.*

Under the regulations operative at the time, Lovenheim was eligible to submit a proposal based on his ownership of 200 shares of stock in the corporation for at least one year prior to the shareholder meeting.¹⁸⁵ Lovenheim's proposal noted that Iroquois "strives to maintain a reputation as a distributor of wholesome foods" and characterized the proposal as seeking "to assure that [Iroquois Brands, Ltd.] is not inadvertently promoting cruelty to animals and does not risk damaging its reputation as a distributor of wholesome food products."¹⁸⁶ The proposal then asked the corporation to do the following:

[F]orm a committee to study the methods by which its French supplier produces *pâté de foie gras*, and report to the shareholders its findings, together with its opinion, based on expert consultation, as to whether or not this production method causes undue distress, pain, or suffering to the animals involved and, if so, whether further distribution of this product would risk damaging the good reputation of the Corporation and should therefore be discontinued until a more humane production method is developed.¹⁸⁷

The proposal indicates how, notwithstanding *Medical Committee*, shareholders still had to steer between the Scylla of generality and the Charybdis of specificity.

Presumably, Lovenheim knew or suspected that *pâté de foie gras* is always produced through the force-feeding of geese, and he really wanted Iroquois to stop distributing the product because its distribution encouraged what he considered a form of animal cruelty. But under the SEC rules operative at the time, shareholders could not bring proposals relating to the continuation of a particular product, as control over ordinary business operations was entrusted to management alone.¹⁸⁸ Nor could Lovenheim bring a proposal that simply denounced animal cruelty and demanded that Iroquois adopt a position consistent with his ethical objections to inhumane treatment of animals without running afoul of the SEC regulation intended to prevent the shareholder proposal from being abused as a mechanism of general political protest.¹⁸⁹ As a result, the shareholder proposal has a bit of absurdist theater about it. Proposals must ask the board to form a committee to investigate a matter and make

185. See 17 C.F.R. § 240.14a-8(a)(1) (1982).

186. Notice of Annual Meeting of Shareholders of Iroquois Brands, Ltd., scheduled on May 10, 1983, at 18 (Mar. 28, 1983) [hereinafter 1983 Notice of Annual Meeting] (on file with the author).

187. *Id.*; see also Lovenheim, v. Iroquois Brands, Ltd., 618 F. Supp. 554, 556 (D.D.C. 1985).

188. See 17 C.F.R. § 240.14a-8(c)(7) (1982).

189. See 17 C.F.R. § 240.14a-8(c)(5) (1982).

recommendations.¹⁹⁰ That way, the shareholder does not interfere with the conduct of ordinary business operations, as the final decision is left in the discretion of the board.

The corporation responded with a letter from Iroquois' General Counsel requesting certification of the number of shares owned by Mr. Lovenheim and the Humane Society.¹⁹¹ Lovenheim got back to Iroquois just five days later, providing certification of the shares owned by the Humane Society. As the SEC regulations did not require him to state the quantity of shares owned by a person bringing a shareholder proposal, Lovenheim pointed out that he did not need to provide the certification requested, but he did state that he had owned 200 shares of Iroquois common stock since 1981.¹⁹²

The corporation had no further objection to Lovenheim's proposal. It included the proposal in the proxy materials distributed in advance of its May 1983 shareholder meeting.¹⁹³ It also included its own recommendation that shareholders vote against Lovenheim's proposal.¹⁹⁴ While noting that the corporation "deplores cruelty to animals in any form and commends the Humane Society of the United States for the important work it does to alleviate such practices,"¹⁹⁵ management gave the following reasons for its opposition: (1) Iroquois exercised no control over the production of the French *pâté*; (2) the product is tested and approved by the Federal Food and Drug Administration (FDA); (3) it is unnecessary to form a panel of directors to study an issue over which the board has no control; and (4) the product in question "represents an infinitely small percent of Iroquois' sale and profits" – in fact the expert consultation called for in the

190. Proposals calling for the formation of a committee of investigation have become the norm when shareholders offer social proposals. *See, e.g.*, *Amalgamated Clothing and Textile Workers Union v. Wal-Mart Stores, Inc.* 821 F. Supp. 877, 882 (S.D.N.Y. 1993) (addressing the excludability of a proposal requesting that Wal-Mart's directors prepare and distribute reports relating to the company's equal opportunity hiring and procurement policies); *N.Y.C. Emps.' Ret. Sys. v. Dole, Food Co.*, 795 F. Supp. 95, 96, (S.D.N.Y. 1992) (addressing the excludability of a proposal requesting the Board of Directors to establish a committee for the purpose of evaluating the impact of proposals for health care reform and their impact on the company); *Austin v. Consol. Edison Co., of N.Y., Inc.*, 788 F. Supp. 192, 193 (S.D.N.Y. 1992) (addressing the excludability of a proposal requesting that shareholders adopt a non-binding resolution endorsing the idea that the corporation's employees should be allowed to retire after 30 years of service, regardless of age).

191. Letter from Ralph L. Halpern, Gen. Counsel for Iroquois Brands, Ltd., to Peter C. Lovenheim (Jan. 6, 1983) (on file with the author).

192. Letter from Peter C. Lovenheim to Ralph L. Halpern, Gen. Counsel for Iroquois Brands, Ltd., (Jan. 11, 1983) (on file with the author).

193. Notice 1983 Notice of Annual Meeting, *supra* note 186, at 17-19.

194. *Id.* at 19.

195. *Id.*

proposal would entail costs in excess of the expected profitability of the product.¹⁹⁶

As he stated he would, Lovenheim appeared at that annual shareholder meeting and presented his proposal.¹⁹⁷ In his presentation, Lovenheim offered a point-by-point refutation of management's arguments.¹⁹⁸ He pointed out that FDA regulation does not encompass any test for humane treatment.¹⁹⁹ "You can import brains pulled from the skulls of live dogs, and the FDA would accept it for importation," Lovenheim noted.²⁰⁰ Lovenheim next noted that it simply was not true that Iroquois had no control over the production of the product, since consumers can always pressure producers to change their production processes.²⁰¹ Lovenheim also addressed management's concerns about the cost of expert consultation on the matter by pointing out that the experts in question would likely be academics, who do not charge much for their services.²⁰² If the charges proved excessive, Lovenheim offered, the Humane Society would provide expert consultations at no cost.²⁰³ Finally, Lovenheim urged shareholders' to reject management's position that humane treatment of animals was simply too costly.²⁰⁴ "I say that if an investigation would cost too much, then we should stop selling the product, or if we are to continue selling the product, then we should have the investigation."²⁰⁵ Another shareholder then rose in support of Lovenheim's proposal.²⁰⁶ In the ensuing vote, Lovenheim's proposal garnered 50,000 votes, just over 5% of those cast.²⁰⁷

B. *The Goose Chase: From Proponent to Litigant*

Encouraged by this result, Lovenheim offered the same resolution the following year.²⁰⁸ He wrote well in advance to seek information

196. *Id.*

197. 1983 Annual Meeting Transcript, *supra* note 180, at 10.

198. *Id.* at 15-18.

199. *Id.* at 16.

200. *Id.*

201. *Id.*

202. *Id.* at 17.

203. *Id.* at 16-17.

204. *Id.* at 17.

205. *Id.*

206. *See id.* at 18 ("[I]t seems to me since it is such a cruel way to obtain [liver pâté], it would be a feather in Iroquois' hat to do without it.").

207. Memorandum of Law, *supra* note 14, at 2.

208. Shareholder Proposal and Supporting Statement (submitted by Peter Lovenheim for inclusion in Iroquois Brands' 1984 Proxy Statement) (included as Attachment 3 to the Affidavit of Peter C. Lovenheim, *supra* note 160) (Dec. 5, 1983) (on file with the author).

regarding the date for the upcoming shareholder meeting.²⁰⁹ To Lovenheim's surprise, the company responded this time by notifying him (through corporate counsel) that Iroquois considered the proposal excludable.²¹⁰ During the intervening year, the SEC had again revised its regulations.²¹¹

The SEC now required shareholders to own at least 1% or \$1,000 worth of the corporation's stock for at least one year prior to the submission of the proposal.²¹² In addition, the rules now permitted exclusion of proposals relating to business operations accounting for less than 5% of the issuer's total assets and for less than 5% of net earnings and gross sales and not otherwise significantly related to the issuer's business.²¹³ Thus, when Lovenheim submitted his proposal in 1983, which was virtually identical to the one submitted one year earlier, Iroquois' only response was to copy him on a letter to the SEC, which stated its intention to omit the proposal from its proxy statement on the ground that it related "to operations which account for less than 5 percent of [Iroquois'] total assets . . . and for less than 5 percent of its net earnings and gross sales . . . and is not otherwise significantly related to" Iroquois' business.²¹⁴

However, as Lovenheim pointed out in his responsive memorandum of law, Iroquois thus did nothing more than re-state the purportedly applicable SEC rule.²¹⁵ Such a simple assertion was not sufficient to meet the corporation's burden, said Lovenheim, under the applicable federal regulations.²¹⁶ In any case, Lovenheim argued, even

209. Letter from Peter C. Lovenheim to James P. McCaffrey, President, Iroquois Brands, Ltd., (Oct. 19, 1983) (on file with the author).

210. Letter from Ralph L. Halpern, Gen. Counsel for Iroquois Brands, Ltd., to Peter C. Lovenheim (Nov. 2, 1983) (on file with the author).

211. Amendments to Proxy Rules, Exchange Act Release No. 20,091, 1983 WL 33272 (Aug. 16, 1983). The story behind this revision was been told in some detail in scholarship published not long after its adoption. See Cane, *supra* note 16, at 62-67 (characterizing the SEC's motivation in formulating the revisions as proposing a total reexamination of the reasons for the rule's existence). Liebeler, *supra* note 32, at 433-37 (describing the three approaches considered by the SEC before it adopted the first of those options in the 1983 amendments).

212. 17 C.F.R. § 240.14a-8(a)(1)(i) (1984).

213. 17 C.F.R. § 240.14a-8(c)(5) (1984).

214. Letter from Ralph L. Halpern, Gen. Counsel for Iroquois Brands, Ltd., to SEC, Div. of Corp. Fin. (Dec. 13, 1983) (on file with the author) (included as Attachment 4 to the Affidavit of Peter C. Lovenheim, *supra* note 160).

215. See Memorandum of Law, *supra* note 14, at 4 ("The letter . . . contains nothing more than a simple assertion that the Proposal is covered by Rule 14a-8(c)(5).").

216. *Id.* at 5 (citing 41 Fed. Reg. § 234 at 52997 (1976)) (stating that the issuer bears the burden of demonstrating it may rely upon one of the substantive grounds for omission of a shareholder proposal).

if it were true that the product at issue did not constitute 5% of Iroquois' assets, earnings, or sales, Iroquois could not show that the product was not "otherwise significantly related" to its business.²¹⁷ Setting aside the broader social importance of animal cruelty, Lovenheim argued that, given that Iroquois was a health food company, whose major product lines included natural vitamins, herb teas and other natural foods that did not include any animal products in their ingredients, the proposal was significantly related to Iroquois' economic interests.²¹⁸ This was especially so, Lovenheim contended, because consumers of health food and natural food products are more likely to value humane treatment of animals than is the general public.²¹⁹ Lovenheim cited to Iroquois' advertisements of its products in magazines such as *Vegetarian Times* and *Prevention*, both of which clearly were marketed towards audiences concerned about animal cruelty.²²⁰

Finally, Lovenheim argued that the SEC, in using the phrase "significantly related" in the relevant regulation, did not mean to permit corporations to omit proposals that related to significant social and ethical issues.²²¹ The Commission recognized that there are many instances in which the matter involved in a proposal is significant to an issuer's business, even though such significance is not apparent from an economic viewpoint.²²²

Addressing none of the legal arguments and factual claims in Lovenheim's twenty-page memorandum, the SEC sided with Iroquois in a two-paragraph no-action letter.²²³ The SEC simply noted that "[t]here appears to be some basis for your opinion that the proposal may be omitted from the Company's proxy material under Rule 14a-8(c)(5)" and concluded that there would be no enforcement action if the Lovenheim proposal were omitted from Iroquois' proxy materials.²²⁴

Lovenheim appealed the decision of the Division of Corporation Finance to the SEC's five commissioners.²²⁵ His memorandum of law submitted to the commissioners rehearsed the arguments from his earlier

217. *Id.* at 6.

218. *Id.* at 6-7.

219. *Id.* at 7-9.

220. *Id.* at 9-10.

221. *Id.* at 13.

222. *Id.* (citing 41 Fed. Reg. 234, 52997 (1976)).

223. Response of the Office of Chief Counsel, SEC, Div. of Corp. Fin., Iroquois Brands, Ltd., SEC File No. 1-5387 (Jan 23, 1984) (on file with the author).

224. *Id.*

225. Letter from Peter C. Lovenheim to SEC (Jan. 30, 1984) (on file with the author) (appealing SEC's decision and incorporating Memorandum of Law, *supra* note 14, at 2).

memorandum, which it incorporated by reference²²⁶ and made the additional argument that the proposal was not new and had won more than 5% of votes cast at the 1983 shareholder meeting.²²⁷ The Commission declined review.²²⁸

Lovenheim attempted to settle his differences with the corporation in advance of the annual shareholder meeting. He offered to drop the shareholder proposal if Iroquois would simply agree to set up a committee to investigate the methods used for the manufacture of the *pâté* distributed by the corporation.²²⁹ Lovenheim recommended that three members of the animal protection community serve as ex officio members of the committee: one representative from American Society for the Prevention of Cruelty to Animals, one representative from the Humane Society and Lovenheim himself.²³⁰ Iroquois was not receptive to such a settlement.²³¹

Lovenheim was undeterred. In fact, the SEC's casual, unreflective decision denying review of his appeal of the SEC staff's issuance of a no-action letter infuriated and inspired him.²³² He prepared his shareholder proposal for a third time. On October 17, 1984, he sent the proposal for inclusion in Iroquois' 1985 proxy statement.²³³ Once again, Iroquois responded with a letter to the SEC stating its intention to omit Lovenheim's proposal from its proxy materials.²³⁴ This time, the corporation took the trouble to present some statistics, indicating that the *pâté* at issue accounted for less than 0.05% of the corporation's sales, less than 0.3% of its net earnings and less than 0.09% of its assets for 1982 and 1983, statistics not expected to change significantly in 1984.²³⁵

226. Memorandum of Law, *supra* note 14, at 1.

227. *Id.* at 2-3.

228. See Letter from Ralph L. Halpern, Gen. Counsel for Iroquois Brands, Ltd., to SEC Div. of Corp. Fin. (Dec. 21, 1984) (on file with the author). Lovenheim now recalls that he was motivated to pursue his law suit as much by frustration with the SEC's cavalier rejection of his legal arguments as disappointment with Iroquois' seeming indifference to his concerns. Audio tape: Interview with Peter C. Lovenheim, *supra* note 171. Lovenheim remembers having typed his legal memoranda himself, on an electric typewriter, not a word processor, after work in the evenings and on weekends. *Id.*

229. Letter from Peter C. Lovenheim to Ralph L. Halpern, Gen. Counsel for Iroquois Brands, Ltd. (Apr. 24, 1984) (on file with the author).

230. *Id.*

231. Letter from Peter C. Lovenheim to John Hoyt, President of the Humane Soc'y, (May 31, 1984) (on file with the author).

232. Interview with Peter C. Lovenheim, *supra* note 171.

233. Letter from Peter C. Lovenheim to Iroquois Brands, Ltd. (Oct. 17, 1984) (on file with the author).

234. Letter from Ralph L. Halpern to SEC Div. of Corp. Fin., *supra* note 228.

235. *Id.*

On January 9, 1985, the SEC's Division of Corporation Finance once again issued a response to Iroquois, stating that it would not recommend any enforcement action if Iroquois were to omit Lovenheim's proposal from its proxy materials.²³⁶

C. *Iroquois' Goose Is Cooked in the D.C. District Court*

As a relatively recent law graduate, Lovenheim still had a fresh recollection of *Medical Committee*.²³⁷ In Lovenheim's view, that decision compelled a ruling in his case obligating Iroquois to distribute his proposal, because it raised a socially significant issue that was related to Iroquois' business. So Lovenheim bypassed an appeal to the SEC commissioners and filed suit in the D.C. District Court²³⁸ seeking an injunction ordering Iroquois to distribute his proposal.²³⁹ This time, he retained Jonathan Eisenberg, an experienced attorney who agreed to work pro bono and to help him on the brief submitted in support of his suit for injunctive relief.²⁴⁰ Lovenheim's motivation in skipping review by the Commission may have been to save time and resources. It also may have been strategic, since at oral argument in the District Court, his counsel argued that the court owed no deference to a decision by the SEC's staff to issue a no-action letter.²⁴¹ It may well have proved harder to persuade the court that it owed no deference to the SEC Commissioners' interpretation of the agency's own rules.

Jonathan Eisenberg acknowledged during oral argument that Lovenheim did not bring the proposal because he expected it to win a majority of the shareholder vote.²⁴² Rather, the purpose was to "force management to take a hard look at the conduct they are engaged in" and

236. Response of the Office of Chief Counsel, SEC, Div. of Corp. Fin., dated Jan. 29, 1985 (on file with the author).

237. 432 F.2d 659 (D.C. Cir. 1970).

238. Section 27 of the '34 Act, 15 U.S.C. § 78(a)(a), has been construed as permitting appeal of a no-action letter directly to the Federal District Court. *See Lovenheim, v. Iroquois Brands, Ltd.*, 618 F. Supp. 554, 558 (D.D.C. 1985). (noting the parties' agreement that section 27 governs and that jurisdiction was proper because Lovenheim had alleged that Iroquois violated securities laws in the jurisdiction by causing misleading proxy materials to be mailed there).

239. *Lovenheim*, 618 F. Supp. at 556.

240. Tischler, *supra* note 13, at 41-42.

241. *See* Transcript of Hearing on Motion for Preliminary Injunction, *supra* note 15, at 17-18 (statement of counsel for the Plaintiff contending that because Lovenheim had not sought Commission review there was no reason for the court to show deference to the SEC staff's issuance of a no-action letter).

242. *Id.* at 5 (acknowledging that shareholder proposals almost never succeed); *See also* Dent, *supra* note 32, at 4-5 ("[N]o shareholder proposal opposed by management . . . has ever come close to receiving a majority shareholder vote.").

to “ask themselves whether they can defend that” conduct.²⁴³ Eisenberg contended that the effectiveness of this tactic was evidenced by the fact that in 1982, thirty-two shareholder proposals had been withdrawn as moot, suggesting that the corporations chose to adopt the measures proposed rather than put them to a shareholder vote.²⁴⁴ Eisenberg reminded the court that the proposal had won 5% of the shareholder vote when it had been included in Iroquois’ 1983 proxy materials and stated that if the proposal were again included, he believed there to be “a significant chance” that Iroquois would decide to discontinue distribution of the product.²⁴⁵

On the law, Eisenberg encouraged the court to consider the relevant regulation, 14a-8(c)(5), as constituting a two-part test, both of which have to be met for the corporation to be permitted to exclude a proposal.²⁴⁶ Lovenheim did not challenge Iroquois’ claim that the economic portion of 14a-8(c)(5) was met,²⁴⁷ but Eisenberg stressed that in 1976 the SEC rewrote the regulation, removing language that permitted the corporation to omit a proposal “if it is submitted primarily for general political, social ends” and adding language permitting omission of proposals that are not economically significant and “that are not significantly related to the issuer’s business.”²⁴⁸

The effect of the change was, in Eisenberg’s view, to eliminate from the SEC’s regulation any indication that social proposals “were suspect.”²⁴⁹ Since the 1976 changes, the SEC had required that all social proposals be included so long as the issuer’s business was in any way implicated in the proposal.²⁵⁰ Eisenberg’s argument suggests that the SEC learned from *Medical Committee* and sought to avoid a head-on collision with the judiciary over whether or not it could permit exclusion

243. *Id.* at 5-6.

244. *Id.* at 6. *But see* Dent, *supra* note 32, at 21-22 (arguing that it is extremely unlikely that corporate management would change policies in response to shareholder proposals that are resoundingly defeated).

245. *Id.* at 7.

246. *See id.* at 9 (“As a two part test it is stated in the conjunctive not the disjunctive. So you clearly have to meet both parts of the test in order to omit the proposal.”).

247. *See id.* at 8 (“[W]e do accept that this proposal is not economically significant under the SEC’s 5 percent test”). *See also* Lovenheim, 618 F. Supp. at 559 (“Plaintiff does not contest that his proposed resolution relates to a matter of little economic significance . . .”).

248. Transcript of Hearing on Motion for Preliminary Injunction, *supra* note 15, at 12-13.

249. *Id.* at 13.

250. *See id.* at 13-14 (suggesting that the SEC wanted to comfort people when it changed the rule again in 1982 by pointing out the SEC did not intend to change its policies with respect to requiring that proposals relating to social, political, and ethical issues be included in proxy materials).

of social proposals without undermining Congress' intent in passing section 14(a) of the '34 Act.²⁵¹

The requirement that the proposal be significantly related was met here, Eisenberg contended, because Iroquois made \$70,000 worth of sales in *pâté de foie gras*.²⁵² If the issue was significant and the corporation was doing even "one completely outrageous thing a year," Eisenberg maintained, the corporation could not refuse to include a proposal relating to that conduct on the ground that it was not economically significant, in that the conduct did not relate to 5% of the corporation's assets.²⁵³

Counsel for Iroquois stressed that the connection between the issue raised by the proposal and Iroquois' business was "de minimis," and that the SEC could not possibly have intended to require corporations to include in proxy statements every single social proposal that had any conceivable connection to the corporation's operations.²⁵⁴ *Pâté de foie gras* accounted for only a tiny portion of Iroquois' business.²⁵⁵ According to the affidavit of its president, Iroquois had annual revenues of \$141 million, \$6 million in annual profits and \$78 million in assets.²⁵⁶ Its sales of *pâté* amounted to just \$79,000, resulting in a net loss of \$3,121.²⁵⁷ The company valued its total assets related to *pâté* at \$34,000.²⁵⁸ Accordingly, Iroquois thought it was well within its rights under the relevant SEC rule to deny Lovenheim's request.

Iroquois argued, in essence, that the main point of 14a-8(c)(5) was to make certain that proposals relate to significant portions of the issuer's business, even if they raise significant political, social or ethical issues.²⁵⁹ Corporations are business entities. They and the SEC are primarily interested in economic matters, Iroquois argued, with respect

251. *See id.* at 14 (arguing that the history of the regulation "suggests very, very strongly that in response to the *Medical Committee* decision, the commission learned that it couldn't exclude proposals raising significant ethical or social issues that were related to the issuer's business").

252. *Id.* at 15-16.

253. *Id.* at 16.

254. *Id.* at 21-22 (statement of Hadrian Katz, counsel for Iroquois).

255. *Lovenheim, v. Iroquois Brands, Ltd.*, 618 F. Supp. 554, 558 (D.D.C. 1985).

256. *Id.*

257. *Id.*

258. *Id.* at 558-59.

259. *See* Transcript of Hearing on Motion for Preliminary Injunction, *supra* note 15, at 23 (contending that Plaintiff's construction of the Rule would delete the economic tests from the rule and allow in any proposal that relates to an important social issue).

to proxy statements as in all other areas.²⁶⁰ *Medical Committee*, as Iroquois understood it, stood only for the proposition that a corporation may not exclude a proposal simply on the ground that it raises ethical and philosophical issues.²⁶¹ The opinion did not require the inclusion of proposals that are of no real economic significance to the corporation.²⁶²

The court sided with Lovenheim on the decisive point. Although *Medical Committee* was decided under an earlier version of the Rule and the economic significance of Dow's production of napalm was not an issue in the case, the court noted that the D.C. Circuit, in deciding *Medical Committee*, had assumed that "napalm was not economically significant to Dow."²⁶³ After a brief review of the Rule, the court concluded that there was simply no evidence that the SEC intended to limit its understanding of the "significance" of a proposal to economic criteria, as Iroquois suggested it should.²⁶⁴ The court recognized the social significance of Lovenheim's proposal and the fact that it "implicate[d] significant levels of sales" for Iroquois.²⁶⁵ It therefore granted Lovenheim the injunctive relief he sought.²⁶⁶

The court's factual findings were significant. As evidence of the social significance of Lovenheim's proposal, the court provided only a footnote referencing Lovenheim's brief.²⁶⁷ Lovenheim had argued that humane treatment of animals is a "foundation of western culture."²⁶⁸ In support of this argument, he cited the Seven Laws of Noah,²⁶⁹ as well as animal protection statutes beginning with one enacted by the Massachusetts Bay Colony in 1641.²⁷⁰ By the time of the litigation, such statutes had been enacted in all fifty states.²⁷¹

A court might have considered such evidence as strikingly weak, as none of it specifically addressed a state interest in regulating the force-

260. See *id.* at 24 ("The criterion for the inclusion of material in corporate annual reports in filings with the SEC in proxy statements and in all other areas, is the economic materiality of the issue.").

261. *Id.*

262. *Id.*

263. *Lovenheim*, 618 F. Supp. at 560 (citing *Med. Comm. for Human Rights v. SEC*, 432 F.2d 659, 681 (D.C. Cir. 1970)).

264. *Id.* at 561.

265. *Id.*

266. *Id.* at 562.

267. *Id.* at 559 n.8.

268. *Id.*

269. See *Genesis* 9:4 (prohibiting consumption of flesh taken from a live animal).

270. *Lovenheim*, 618 F. Supp. at 559 n.8.

271. *Id.*

feeding of geese.²⁷² At the time the case was decided, Lovenheim could not have cited to a single federal, state, or locality that had attempted to regulate the force-feeding of geese.²⁷³ Indeed, at oral argument, Iroquois' counsel made the policy argument that corporations should not have to decide "which issues are sufficiently important to be put to the shareholders on philosophical and ethical terms and which issues are not."²⁷⁴ Iroquois' counsel obviously thought that the issue of force-feeding of geese in France was not significant,²⁷⁵ a view apparently shared by "proxy resolution aficionados."²⁷⁶ Even Lovenheim's counsel came very close to conceding that the issue was not as significant as the use of napalm raised in *Medical Committee*.²⁷⁷ Neither party offered expert testimony on the political, social, or ethical significance of the issue. One is hard pressed to imagine where such expertise would reside or why it should reside in a corporation, in the SEC, or in a court.²⁷⁸

272. Better evidence of the social significance of Lovenheim's proposal was furnished in Lovenheim's affidavit, which cited efforts by "leading organizations in the field of animal care" to discourage the practice of force-feeding. *Id.* Still, it is not clear why the fact that some organizations with a special interest in an issue raise that issue should be treated as evidence of widespread concern.

273. The first such regulation was introduced in California in 2004. Under the new law, as of July 1, 2012, "[a] product may not be sold in California if it is the result of force feeding a bird for the purpose of enlarging the bird's liver beyond normal size." CAL. HEALTH & SAFETY CODE § 25982 (West 2009). The City of Chicago attempted a ban on *foie gras* in 2006, but it apparently was not enforced. *See, e.g.,* Josh Noel, *Let 'em Eat Foie Gras, They Declare; Almost 4 Months After Ban, A Number of Restaurants Appear to be Dishing Up the Delicacy with Impunity*, CHIC. TRIB., Dec. 21, 2006, at C1 (suggesting the city's Department of Public Health was hesitant to fine restaurants that ignored a ban on the product); Josh Noel et al., *Chicago's Wild Foie Gras Chase: Mayor Daley Calls the Ban the 'Silliest' Law. Restaurants Across Town Serve up the Delicacy in Defiance. Now the Question is Whether City Officials Will Actually Try to Enforce the New Law*, CHIC. TRIB., Aug. 23, 2006, at C1 (reporting brisk sales of *foie gras* after Mayor Daley denounced a ban on the product as the "silliest law" ever passed by the City Council). The ban was officially lifted in May 2008. Mark Caro & Dan Mihalopoulos, *Daley Special: Foie Gras Back on the Menu*, CHIC. TRIB., May 15, 2008, at A1.

274. Transcript of Hearing on Motion for Preliminary Injunction, *supra* note 15, at 25.

275. *See id.* ("Now, I am prepared to concede today, with tongue a little bit in cheek . . . that their issue about the geese in France is a very important issue.")

276. *See Cane, supra* note 16, at 61 (noting the notoriety of Lovenheim's proposal).

277. Comparing the Lovenheim case to *Medical Committee*, Eisenberg said, "We think that although this case arises in a less – not less serious, in a different faculty context, that the issue again is pretty much the same." Transcript of Hearing on Motion for Preliminary Injunction, *supra* note 15, at 12.

278. *See Palmiter, supra* note 44, at 905-06 ("Rule 14a-8's 'proper subject' jurisprudence flounders without any hope of judicial or legislative correction.")

Determining which issues are “important” is not within the institutional competence of any of those bodies.²⁷⁹

Leaving significance aside, there was also the question of what constitutes “significantly related” to the business operations of the issuer.²⁸⁰ Lovenheim’s counsel offered that a proposal advocating that the corporation cease doing business in South Africa would be excludable if the corporation did not in fact do business there and that a proposal like Lovenheim’s would not have to be submitted to the shareholders of IBM if IBM did not import *pâté de foie gras*.²⁸¹ But Iroquois’ counsel countered that “clever and imaginative lawyers will always be able to think of some tenuous link to the business of the corporation.”²⁸² A shareholder might argue that there is a significant relation between IBM’s business operations and *pâté de foie gras* if it offers the delicacy for purchase in its employee cafeteria once a month.²⁸³ In response, Eisenberg noted that the problem had not arisen; IBM shareholders had brought no proposals objecting to the items on the menu in the employee cafeteria.²⁸⁴

Nor is the basis clear for the court’s finding that sales of *pâté de foie gras* “implicated significant levels of sales” for Iroquois Brands.²⁸⁵ The court had earlier noted that, because sales of *pâté de foie gras* accounted for only \$34,000 of the company’s assets, and that sales of *pâté de foie gras* had resulted in a net loss, the proposal implicated “none of the company’s net earnings and less than 0.05% of its assets.”²⁸⁶ In a footnote, the court noted that the result in the case would have been different if the proposal had no “meaningful relationship to the business of” the corporation.²⁸⁷ Still, the court’s willingness to accept as socially significant any proposal relating to a subject about which some national non-profit organizations had expressed concern, coupled with its willingness to think it significantly related to a business if it accounts for 0.05% of a corporations’ assets, suggested that

279. See *id.* at 910 (“[T]he current rule’s attempt at merit regulation lays on the staff the impossible task of deducing what should be of interest to investment-minded and public-minded shareholders and what should not be of interest.”).

280. Transcript, Hearing on Motion for Preliminary Injunction, *supra* note 15, at 13.

281. *Id.* at 15.

282. *Id.* at 27.

283. *Id.* at 26.

284. *Id.* at 28.

285. Lovenheim v. Iroquois Brands, Ltd., 618 F. Supp. 554, 561 (D.D.C. 1985).

286. *Id.* at 559-60.

287. *Id.* at 561 n.16.

corporations could be obligated to distribute shareholder proposals on nearly any subject that in any way related to their businesses.

There was a great deal of media interest in the case, with articles appearing in *The Washington Post*,²⁸⁸ *The Los Angeles Times*,²⁸⁹ and *The Wall Street Journal*,²⁹⁰ among other newspapers.²⁹¹ The *Washington Post* was especially vocal in its support for Lovenheim's brand of shareholder activism: "There isn't a company in the country that couldn't benefit from 10 tough questions from stockholders at its annual meeting this year. But there probably isn't one company in 10 that will face them."²⁹² Given the timing of the opinion, Iroquois had to acquiesce, as there was insufficient time to appeal the decision before the next annual shareholder meeting,²⁹³ which was held just weeks after the District Court's decision.²⁹⁴

Lovenheim attended the meeting, as required under the regulations, and he presented his proposal to the shareholders and their proxies. The reception was far from warm.²⁹⁵ Lovenheim's proposal received less than 8% of the votes cast by Iroquois' shareholders.²⁹⁶ As a result, Iroquois would not be required to include Lovenheim's proposal or another proposal on the same subject matter for three years.²⁹⁷ Despite the court victory and the publicity, ordinary shareholders were unmoved.²⁹⁸ Or were they? Within months of the shareholder meeting,

288. Philip Smith, *Shareholders to Be Given Pâté Question*, WASH. POST, Mar. 28, 1985, at E3; Jerry Knight, *Force-Feeding Moral Issues onto Corporate Agendas*, WASH. POST, Mar. 11, 1985, at Bus. 1.

289. Michael A. Hiltzik, *Ruling Aids Resolutions on Ethical Issues*, L.A. TIMES, Mar. 28, 1985, at B2.

290. Ingersoll, *supra* note 159.

291. Timothy Bannon, *Where's the Liver?*, UPI, MAR. 2, 1985, available at, LEXIS, News.

292. Knight, *supra* note 288.

293. Ralph Halpern, Iroquois' general counsel at the time of the litigation recalls that there was no time to appeal the decision before the annual shareholder meeting. Telephone interview with Ralph Halpern, *supra* note 172.

294. Tischler, *supra* note 13, at 42. The District Court's order is dated March 27, 1985. *See* Lovenheim, 618 F. Supp. 554. Iroquois' shareholder meeting was held six weeks later, on May 14, 1985. *See* Iroquois Brands, Notice of Annual Meeting of Shareholders (Apr. 12, 1985) (on file with the author).

295. Telephone interview with Peter Lovenheim, *supra* note 162.

296. Stipulation of Dismissal at 1, Lovenheim v. Iroquois Brands, Ltd., 618 F. Supp. 554 (D.D.C. 1985) (No. 85-0734).

297. *Id.* (citing 17 C.F.R. § 240.14a-8(c)(12)).

298. *See* Tischler, *supra* note 13, at 42 (describing the proposal as having been "roundly defeated").

Iroquois sold the unit responsible for importing *pâté de foie gras*, announcing that it now considered the issue put behind the company.²⁹⁹

Lovenheim comes on the tail end of a period in the history of shareholder proposals when individual shareholders were the dominant shareholder activists.³⁰⁰ In the 1980s, institutional investors, first church groups and then pension funds, began to play a leading role in promulgating shareholder proposals.³⁰¹ *Lovenheim* is a paradigmatic transitional case because, although Peter Lovenheim brought his proposal in his own behalf, he also did so on behalf of the Humane Society of the United States.³⁰² Moreover, Lovenheim worked closely with organizations opposed to animal cruelty in attempting to use his shareholder proposal as part of a broader strategy to persuade Iroquois to stop marketing *pâté de foie gras*. His case suggests the difficulties an individual investor might face in trying to put pressure on a corporation through the mechanism of the shareholder proposal and thus illustrates why the transition from individual shareholder activists to institutional activism might have occurred.

D. *Lovenheim's Further Adventures in Animal Law*

After his experience with Iroquois, Lovenheim, having returned to his native Rochester, began offering his services as a sort of freelance

299. ORLANS, *supra* note 165, at 231, (citing personal correspondence with Ralph L. Halpern, Jaeckle, Fleischmann & Mugal (Apr. 13, 1988)). Although Lovenheim believes that his shareholder proposal and the adverse publicity associated with it influenced Iroquois' decision to discontinue the product, Halpern contends that he remembers quite clearly that the controversy over Lovenheim's proposal had nothing to do with the corporation's decision to discontinue a product that was a tiny portion of its business and had never been profitable for the corporation. Telephone interview with Ralph Halpern (July 10, 2009).

300. See Gillian & Starks, *supra* note 25, at 56 (providing a short history of shareholder activism and noting that the eclipse of individual investors as the proponents of shareholder proposals began in the mid-1980s).

301. See Ryan, *supra* note 44, at 157-59 (1988) (reporting that institutional investors targeted around fifty corporations for shareholder proposals in 1987). Church sponsored proposals accounted for 10.97% of all shareholder proposals in the 1979-80 proxy season and 14.02% of such proposals in 1982-83. Liebler, *supra* note 32, app. at tbl.2. In the twenty-first century, pension funds such as the California Public Employee Retirement System (CalPERS) have taken a leading role in the shareholder proposal movement. Press Release, Ca. Pub. Emp. Ret. Sys., CalPERS Steps up Pace of Shareholder Activism, (Aug. 13, 2007), CALPERS.CA.GOV available at <http://www.calpers.ca.gov/index.jsp?bc=/about/press/pr-2007/aug/steps-up-shareowner-activism.xml> (last visited Aug. 23, 2009). In 2007, CalPERS alone filed thirty-three shareholder proposals. *Id.* Recently hedge funds have assumed a new prominence among proponents. See Gillian & Starks, *supra* note 25, at 68 (describing hedge funds as a dominant force in the shareholder activism arena).

302. Letter from Peter C. Lovenheim to Terrence J. Fox, *supra* note 182.

drafter of shareholder proposals for non-profit organizations.³⁰³ He worked with People for the Ethical Treatment of Animals (PETA), and helped them start an ongoing program aimed at bringing animal protection issues to the attention of corporations through shareholder proposals.³⁰⁴ Lovenheim also teamed up with Henry Spira, a brilliant tactician in the art of “constructive shaming,” which involves pressuring corporations into cooperating with advocates for the ethical treatment of animals.³⁰⁵ Spira’s biographer, Peter Singer, describes him as follows:

Henry Spira [was] a bushy-haired New York high school teacher who spoke with a broad accent that came from years spent on ships as a sailor in the merchant marine and on the General Motors assembly line in New Jersey. [Revlon’s vice president for investor relations, Roger] Shelley saw that Henry’s clothes were crumpled, that he rarely wore a tie, and that when he did, he seemed incapable of getting it to meet his collar.

But that wasn’t all that Shelley noticed: “There was not one ounce of product on his body that was produced by an animal, and that included his belt, that included shoes, that included everything . . . Here was a man who did what he said he would do.”³⁰⁶

Singer chronicles Spira’s career as an advocate for animals. From 1975-1977, Spira organized a campaign to end animal experimentation at New York’s Museum of Natural History.³⁰⁷ Spira and his colleagues not only highlighted the suffering of the animals that were the subject of the experiments³⁰⁸ in the museum, they were also able to show that the research was more or less useless.³⁰⁹ The museum closed and dismantled its laboratories.³¹⁰

Spira next pressured Amnesty International into ceasing its support for a group of scientists that was torturing pigs in order to learn whether

303. See Peter Lovenheim, *Stock in “Unsavory” Companies Is Potent Tool to Influence Option*, NONPROFIT TIMES, Oct. 1, 1990, at 29 (describing Lovenheim as a New York based attorney who prepares and files shareholder proposals for nonprofits).

304. Tischler, *supra* note 13, at 43.

305. See generally PETER SINGER, *ETHICS INTO ACTION: HENRY SPIRA AND THE ANIMAL RIGHTS MOVEMENT* (1998).

306. *Id.* at x.

307. *Id.* at 54-74.

308. See *id.* at 66 (describing experiments on cats involving deafening, blinding, destruction of the sense of smell, removal of brain parts, severing of nerves in the penis and castration).

309. See *id.* at 67 (reporting that *Science* staff writer Nicholas Wade discovered that 14 of the 21 scientific papers produced by the researchers had never been cited and the others were cited infrequently).

310. *Id.* at 71.

torture could be conducted without leaving visible traces.³¹¹ There followed a successful campaign to repeal New York's Metcalf-Hatch Act, which allowed medical researchers to seize unclaimed dogs and cats from animal shelters.³¹² Spira then launched a series of campaigns against corporations engaged in inhumane treatment of animals, including: a largely successful campaign to get Revlon to develop new ways to test eye irritancy and thus to stop blinding rabbits in order to test the safety of its products;³¹³ a campaign that greatly reduced the use of a brutal product safety process, LD50, which involves determining the dose at which a substance is lethal to 50% of the animals tested;³¹⁴ and a far less successful effort to expose inhumane treatment of chickens by the Perdue Farms corporation.³¹⁵

Spira next teamed up with Temple Grandin, a designer of livestock handling facilities and a Professor of Animal Science at Colorado State University, to replace the "shackle and hoist" method for the ritual slaughter of cattle with a more humane upright restraining system that Grandin designed.³¹⁶ There followed an equally successful campaign to end the USDA's policy of face-branding Mexican cattle.³¹⁷ Aiming at a larger impact on the farm animal industry, Spira next targeted McDonald's.³¹⁸ Spira's usual strategy was to use the threat of adverse publicity to bring corporations to the table. He would send to corporations drafts of full-page ads destined for major newspapers. The ads illustrated animal cruelty associated with the corporation's business. If the corporation did not agree to talk, the ads would appear. With Lovenheim's assistance, Spira supplemented that tactic with a shareholder proposal, calling on McDonald's to form a committee to investigate the effect of factory farming on animals used in McDonald's food products.³¹⁹

Together, Lovenheim and Spira were able to persuade McDonald's to adopt three basic principles to help assure humane treatment of the

311. *See id.* at 75-77 (describing Spira's victory in a short, cerebral campaign, which Spira celebrated by becoming a member of Amnesty International).

312. *Id.* at 78-83.

313. *Id.* at 86-111.

314. *Id.* at 114-29.

315. *Id.* at 142-49.

316. *Id.* at 156-60.

317. *Id.* at 161-64.

318. *See id.* at 166 (indicating that Spira's aim was to get McDonald's to give 0.01% "of its gross revenues to fund a research center dedicated to finding alternatives to stressful confinement of factory farming.").

319. Tischler, *supra* note 13, at 43.

animals used in McDonald's products.³²⁰ In the several years Lovenheim worked with Spira, he claims they never had to actually bring a proposal to a vote in a shareholder meeting. Spira had won a reputation for openness to reasonable compromise. He worked with corporations until they agreed to adopt measures that would enhance their reputations for corporate responsibility. The result was almost invariably at least a partial adoption of the substance of the proposals that Spira and Lovenheim brought.³²¹

Lovenheim's story thus suggests that shareholder proposals have consequences that go beyond their effects on the corporation to which the proposal originally relates. Peter Lovenheim began as an amateur investor who chose to put a relatively small amount of money into corporations in which he believed. He then learned that one of those corporations was engaged in a business practice of which he disapproved and which he considered inconsistent with the business model that had led him to invest in the first place. He raised his voice, but both the corporation and the SEC would not hear his complaints. This response turned Lovenheim into a litigant and, briefly, into an activist. He shared his expertise in writing shareholder proposals with others who shared his political goals. And one thing led to another. For a time at least, Peter Lovenheim was transformed by his experience as a proponent into someone who worked with others to promote social change through mechanisms that were not limited to the shareholder proposal mechanism.

IV. SHAREHOLDER PROPOSALS AND THE SEPARATION OF OWNERSHIP AND CONTROL

*Lovenheim*³²² and *Medical Committee*³²³ illustrate the determination and resolve required of any shareholder who wants to get a proposal before the shareholders of a corporation. In both cases, the proponents of the proposal either represented or had the strong, active support of an organization. Lovenheim was an attorney who was not intimidated by the procedural hurdles shareholders face. As such, he was exceptional. It is in fact very rare—and it was even rarer at the time of *Lovenheim v. Iroquois Brands*—for disappointed proponents to

320. *Id.* at 43-44.

321. Telephone interview with Peter Lovenheim, *supra* note 162.

322. 618 F. Supp. 554 (D.D.C. 1985).

323. 432 F.2d 659 (D.C. Cir. 1970).

challenge no-action letters.³²⁴ Up until 1990, there were only thirteen reported cases reviewing SEC determinations on shareholder proposals.³²⁵ As the *Medical Committee* court noted, the SEC's process for reviewing proposals was far from transparent and often resulted in corporations being permitted to omit proposals for reasons that were not effectively communicated to the proponents of those proposals.³²⁶

For opponents of shareholder proposals, the fact that the proponent in *Medical Committee* was an organization that promoted social causes and that Lovenheim had close ties with such an organization highlights the problem of shareholder social proposals. Opponents of shareholder proposals view shareholders primarily as passive investors seeking an economic return.³²⁷ So viewed, their only interest in political or social issues ought to be with the effect of such issues on the return on their investment in the corporation. As one critic of the Rule put it: "Stockholder participatory democracy is a myth; investors do not buy stock in public companies with any serious expectation of influencing management."³²⁸ The Wall Street Rule is the only practical rule by which sensible investors are governed. Small investors who do not like management sell their shares.³²⁹ If the issue is essentially an economic one, say the social proposal skeptics, then it ought to be left for corporate managers to decide in the exercise of their business judgment.³³⁰ If the issue is not economic, then it has no business being before any corporate body.

Lovenheim conceded that his proposal was likely to fail and that, even if it passed, it would require only that the corporation form a committee to study the methods used in the production of *pâté de foie gras* and to make recommendations for further distribution of the product in light of its findings.³³¹ The *Lovenheim* court made clear that

324. Palmiter, *supra* note 44, at 881.

325. *Id.*

326. *See Med. Comm.*, 432 F.2d at 674 (noting that "the shareholder often has no idea why his proposal was deemed unworthy or what he can do to cure its defects for subsequent proxy solicitations").

327. Cane, *supra* note 16, at 61.

328. Liebler, *supra* note 32, at 447.

329. *Id.* at 447. Liebler defines the Wall Street Rule as "the practice by investors unhappy with management of selling their shares in the market rather than trying to alter management's behavior or the management team." *Id.* at 447 n.123.

330. *See Cane*, *supra* note 16, at 61 (noting that those who view shareholders as passive investors tend to think shareholder proposals ought to be permitted only when they relate to internal corporate governance issues or with issues that have a demonstrable economic effect on the corporation).

331. *Lovenheim v. Iroquois Brands, Ltd.*, 618 F. Supp. 554, 561 (D.D.C. 1985).

the proposal's poor prospects for success did not excuse the corporation from its obligation to distribute the proposal.³³² It is hard to imagine why the SEC would have intended to permit corporate resources to be utilized in such a way. And yet, in the two decades since *Lovenheim* was decided, neither Congress nor the SEC has taken action to reign in social proposals. On the contrary, the SEC routinely cites to *Lovenheim* in denying no-action letters to corporations.³³³ This final section offers an explanation of why that is the case.

A. *The Costs and Benefits of Shareholder Proposals*

In connection with its 1984 revisions to Rule 14a-8, the SEC circulated a questionnaire in order to gauge interested parties' attitudes towards shareholder proposals. Nearly three of four respondents agreed or strongly agreed that shareholder proposals are "a waste of management's time and the corporation's money."³³⁴ Most respondents did not agree that proposals are an efficient or effective outlet for concerned shareholders, although the votes were more evenly split on whether the proposals are an "effective way of keeping management aware of shareholder concerns."³³⁵

Although corporation counsel tends to regard shareholder proposals as a nuisance,³³⁶ the overall costs associated with such proposals do not seem to be that significant.³³⁷ One scholar estimated the total cost at about \$15 million/year as of 1992.³³⁸ In 1975-1976, AT&T estimated that it spent \$112,450 in including five proposals in its proxy materials, while it spent \$41,140 on eleven others that it omitted.³³⁹ A 1981

332. *See id.* (finding that Iroquois misstated the significance of the Rule, which the court viewed as guaranteeing shareholder access to proxy statements "whether or not their proposals are likely to pass and regardless of the immediate force of the resolution if enacted").

333. *See, e.g.*, Raytheon Co., SEC No-Action Letter, 2009 WL 890011, at *7 (Mar. 30, 2009) (citing to *Lovenheim*, 618 F. Supp. 554 in denying corporation's request for a no-action letter); Denny's Corp., SEC No-Action Letter, Denny's Corporation, 2009 WL 772857, at *13 (March 17, 2009).

334. *See Cane, supra* note 16, at 70 (reporting that 72.9% of respondents agreed that shareholder proposals are a waste of time and money).

335. *See id.* (reporting that while only 28.7% found proposals an efficient outlet for concerned shareholders and only 32% found proposals effective, 41% agreed that the proposals are effective for keeping management informed, with only 42.6% disagreeing with that statement).

336. *See Chilgren, supra* note 46, at 304 (outlining the course of a typical shareholder proposal from the corporation's perspective and highlighting the expense to the corporation at each stage).

337. *See id.* at 305 (providing a conservative estimate of the cost to the corporation per proposal of "\$1,700 of good hard cash.").

338. Palmiter, *supra* note 44, at 883.

339. Liebler, *supra* note 32, at 454.

survey of eighteen major corporations indicated an average cost of \$94,775 per proposal submitted.³⁴⁰ In the past two years, the SEC has responded to between 300 and 450 requests for no-action letters each year.³⁴¹ Around the time of the Lovenheim case, the SEC reported that it devoted only 1,208 staff hours per year to the review of shareholder proposals and requests for no-action letters, a rough equivalent to the time of one full-time employee.³⁴² And subsequent to that report the Rule was amended³⁴³ to require that proponents own significant amounts of stock for one year before submitting their proposal, thus eliminating the danger that proponents with no real interest in the corporation abuse the shareholder proposal mechanism in order to get their ideas before millions of investors at the corporation's expense.³⁴⁴ Even the most determined opponents of the proposal concede that its costs both to corporations and to the SEC are not very significant.³⁴⁵

As Lovenheim understood at the outset, shareholder proposals can succeed in affecting corporate policy even if they do not come close to winning the shareholder votes necessary for adoption. They thus can be a highly effective way to persuade corporate management to adopt socially responsible positions. From a policy perspective, the costs of shareholder proposals to the SEC and to corporations thus should be balanced against the possible benefits that derive from such proposals. The best evidence that such benefits exist is that numerous ideas for reform of corporate management originated in shareholder proposals but have been subsequently adopted and implemented by management.³⁴⁶

340. *Id.*

341. Division of Corporation Finance Shareholder Proposal No-Action Letters Issued Under Exchange Act Rule 14a-8, available at <http://www.sec.gov/divisions/corpfin/cf-noaction/14a-8.shtml> (last visited Aug. 29, 2009).

342. Proposed Amendments to Rule 14a-8, Exchange Act Release No. 19,135, 47 Fed. Reg. 47,420, 47,423 n.15 (Oct. 14, 1982).

343. See 17 C.F.R. § 240.14a-8(b) (2010) (requiring that proponents own at least \$2,000 worth of stock or 1% of the shares entitled to vote).

344. See Liebler, *supra* note 32, at 425-26 (criticizing the rule for allowing proponents with only one share of stock to reach millions of investors while bearing little or none of the costs associated with the distribution of their proposals).

345. See Dent, *supra* note 32, at 15 (conceding that the SEC estimate of staff time spent dealing with shareholder proposals is "surprisingly low"); Liebler, *supra* note 32, at 454 (concluding that the costs are "not insignificant" but also are not "a substantial portion of the gross national product").

346. See Palmiter, *supra* note 44, at 897-98 (citing: Lewis Gilbert's advocacy of more liberal dividend policies and consistent financial accounting; shareholder proposals calling for compensation and nominating committee comprised solely of outside directors and improved mechanisms for disclosure of executive compensation; and the significant number of proposals that have been withdrawn after a negotiated settlement with management); *but see* Dent, *supra* note 32,

Because proponents benefit corporations and their fellow shareholders, SEC rules that force corporations to bear the costs of such proposals make sense. Without them, because proponents of such proposals do not benefit in a manner that is proportionate to their contribution of time and effort,³⁴⁷ shareholders would not be adequately incentivized to bring potentially beneficial proposals.³⁴⁸ Viewed from this perspective, the Wall Street Rule is inefficient. Proponents with ideas about how to improve corporations are a resource to the corporation. If their main recourse is to invest elsewhere, the corporation's resources are dissipated.

One scholar has characterized the Rule as a tax imposed on corporations that pays for a useful mechanism of corporate governance.³⁴⁹ Corporations may well regard this "tax" as cheaper and less onerous than government regulation.³⁵⁰ Shareholder proposals facilitate communication between a corporation's management and its owners in a manner that is more open, clear and specific than any other mechanism for communication between management and shareholders.

B. The Efficacy of Shareholder Proposals

Justifications for the existence of shareholder proposals relating to social issues come in two varieties. One variety focuses on the nature of corporations. It views shareholders not as passive investors but as owners who have—and should have—an interest in the social and political impact of a corporation.³⁵¹ From this perspective, shareholders have not only a right but a duty to try to influence corporate management to adopt socially responsible policies. In the years following the *Medical Committee* decision, scholars found ample evidence that corporations were adopting policies on social issues that were either directly or at least apparently stimulated by shareholder proposals.³⁵²

at 19-22 (calling the effect of shareholder proposals infinitesimal and questioning the factual basis for claims that corporations actually respond to shareholder proposals).

347. Palmiter, *supra* note 44, at 896 (noting that the proponent of a value-enhancing proposal will only benefit in proportion to her shareholdings).

348. *See id.* (summarizing collective action, free-riding and rational apathy problems that the rule requiring corporations to assume costs of shareholder proposals is meant to address).

349. *See id.* at 898 ("[T]he rule acts as a tax on public companies and their shareholders.").

350. *Id.* at 899.

351. Cane, *supra* note 16, at 61.

352. *See* Schwartz & Weiss, *supra* note 22, at 642-43 (finding the Rule justified "by the major constructive impact it has had on actual corporate behavior" and citing "numerous instances" in which corporations have taken actions consistent with such proposals); *see id.* at 643-47 (describing

The other variety is Melvin Eisenberg's safety valve theory; that is, the idea that shareholder proposals provide a useful safety valve in that they permit shareholders to raise their concerns before management and their fellow shareholders in a public forum in which the corporation's leadership must provide some sort of response.³⁵³ As indicated above,³⁵⁴ the safety valve comes at relatively low cost to the corporation.³⁵⁵

But both varieties of defenses of the shareholder proposal process ultimately sound in a theory of the corporation that recognizes that corporations have a role in society that is too large to be reduced to economics. Even those who continue to maintain that corporations exist "primarily to earn a profit for [their] shareholders,"³⁵⁶ acknowledge that the law now recognizes "a greatly enlarged social duty and responsibility of businesses" to care for the "comfort, health and well-being of their employees."³⁵⁷ In fact, corporations' social duty extends well beyond the well-being of their employees, and there is actually very little support, either in case law or in statutes, for the notion that corporations exist primarily for the benefit of their shareholders.³⁵⁸ Rather, corporate management is permitted to justify its decisions not only with reference to shareholder interests, but also with reference to the interests of other stakeholders, which may include the interests of creditors, employees, customers, and the industry as a whole or even the community at large.³⁵⁹

The case that best illustrates this principle is *Shlensky v. Wrigley*,³⁶⁰ in which minority owners in the corporation that owned the Chicago

the impact of shareholder proposals in promoting: divestment from South Africa; disclosure of affirmative action and equal opportunity employment programs; disclosure of compliance with Arab nations' boycott of Israel; and various initiatives known collectively as "Campaign GM" and designed to promote more responsible corporate governance).

353. *Id.* at 635; Eisenberg, *supra* note 22, at 1494.

354. *See supra* text accompanying notes 323-31.

355. *See Cane, supra* note 16, at 57 (characterizing the cost of shareholder proposals to corporate management as "relatively slight").

356. COX & HAZEN, *supra* note 24, at 63; *see also* Dodge v. Ford Motor Corp., 170 N.W. 668, 684 (Mich. Sup. Ct. 1919) ("A business corporation is organized and carried on primarily for the profit of the stockholders.").

357. *Id.* at 66.

358. *See* Lynn A. Stout, *Why We Should Stop Teaching Dodge v. Ford*, 3 VIRG. L. & BUS. REV. 163, 172 (2008) (concluding that corporate charters, state corporation codes and case law provide no support for the notion that shareholder wealth maximization is a primary purpose of corporations).

359. Lawrence E. Mitchell, *A Theoretical and Practical Framework for Enforcing Corporate Constituency Statutes*, 70 TEX. L. REV. 579, 579 n.1 (1992) (listing twenty-eight jurisdictions that permit corporate boards to consider the interests of constituencies other than shareholders).

360. 237 N.E.2d 776 (Ill. App. Ct. 1968).

Cubs brought suit alleging that the corporation's directors had breached their duty of care by refusing to install lights at Wrigley Field.³⁶¹ The shareholders were armed with evidence that the introduction of night games would boost attendance at Cubs games, since they could show that the White Sox drew more fans at night games on days when the Cubs played day games, but the teams attracted roughly equal crowds when both played day games.³⁶² The President of the corporation, Philip K. Wrigley,³⁶³ offered two reasons for refusing to install lights: his belief that baseball is a daytime sport; and his concern about the effect of lights and night baseball on the surrounding neighborhood.³⁶⁴ The court permitted the corporation to place its commitment to certain ethical or aesthetic principles ("baseball is a daytime sport") and to the Wrigleyville neighborhood ahead of the economic interests of its shareholders.³⁶⁵

The law on corporate charitable giving is consistent with this expansive understanding of the purpose of corporations. Corporations are permitted to make charitable donations without any sort of requirement that they justify those donations in economic terms.³⁶⁶ In the landmark case, *A.P. Smith Mfg. Co. v. Barlow*, the New Jersey Supreme Court enthusiastically embraced the principle that corporations must supplement their wealth maximizing pursuits with a sense of their social and ethical responsibility to be good corporate citizens.³⁶⁷

When the wealth of the nation was primarily in the hands of individuals they discharged their responsibilities as citizens by donating freely for charitable purposes. With the transfer of most of the wealth to corporate hands and the imposition of heavy burdens of individual taxation, they have been unable to keep pace with increased philanthropic needs. They have therefore, with justification, turned to corporations to assume the modern obligations of good citizenship in the same manner as humans do.³⁶⁸

The court noted that its understanding of the need for corporate social responsibility was shared by Congress and state legislatures which

361. *Id.* at 777.

362. *Id.* at 778.

363. *Id.* at 777.

364. *Id.* at 778.

365. *Id.*

366. *See A.P. Smith Mfg. Co. v. Barlow*, 98 A.2d 581, 583 (N.J. Sup. Ct. 1953) (permitting the corporation to make a charitable donation to Princeton University, in part because capitalism and free enterprise depend on the continued existence of private and independent universities).

367. *Id.* at 586.

368. *Id.* at 585-86.

had enacted statutes to encourage corporations to make charitable contributions.³⁶⁹ At the time *Barlow* was decided, twenty-nine states had passed statutes permitting corporations to make charitable contributions.³⁷⁰ The Model Business Corporations Act recognizes that corporations have the same power as an individual to do “all things necessary or convenient to carry out its business and affairs, including *without limitation* power: . . . to make donations for the public welfare or for charitable, scientific, or educational purposes.”³⁷¹

The Rule and the SEC’s permissive approach to social proposals are understandable in light of the broader doctrine of corporate purposes. Corporations do not exist primarily to maximize shareholder wealth. Corporations have become important and powerful legal persons. Social norms, embodied in laws regulating corporate governance do not condone the sort of amoral conduct that would result if corporations were to conceive of themselves purely as vehicles for the production of wealth. Moreover, in exercising their business judgment for the benefit of the corporations that they manage, corporate officers and directors do not want shareholder wealth maximization to define their decision-making processes. Enjoying as they do the benefits of deference to their business decisions that may be influenced by factors other than wealth-maximization, corporate managers cannot deny shareholders the ability to contribute to the decision-making process through social proposals.

V. CONCLUSION

Judging by the few court cases that address social proposals, one could easily conclude that cases like *Lovenheim* are akin to nuisance suits that have no impact on corporate governance because the proposals never win anything approaching a majority of the shareholder vote. However, the cases themselves do not tell the full story behind social proposals. While we cannot know for certain whether Peter Lovenheim’s proposal was the last straw that led Iroquois to discontinue its distribution of *pâté de foie gras*, it is clear from his subsequent

369. *Id.* at 586; *see id.* at 587 (citing language from 1950 New Jersey statute permitting corporate charitable donations not in excess of 1 percent of capital and surplus, unless authorized by shareholders, in order that “encouragement be given to the creation and maintenance of institutions engaged in community fund, hospital, charitable, philanthropic, educational, scientific or benevolent activities or patriotic or civic activities conducive to the betterment of social and economic conditions.”).

370. *Id.* at 587.

371. MODEL BUS. CORP. ACT § 3.02(13) (2003) (emphasis added).

experiences that social proposals can influence corporate decision-making processes.

But are social proposals desirable? If U.S. citizens want regulations preventing the distribution of products that promote inhumane treatment of animals, if they want to outlaw cluster bombs, if they want universal health care for all citizens or residents, or if they want all corporations to embrace affirmative action and renounce all forms of discrimination based on gender, race, religion, national origin, sexual preference, or gender-identity, why is the political process inadequate? Why should corporations foot the bill for the dissemination of all proposals relating to social issues of any significance that also have some sort of relation to the corporation's business?

As this Article has argued, the answer lies in the purpose of corporations. Opponents of social proposals tend to view corporations as vehicles for the generation of wealth, and they view shareholders as passive investors concerned only with maximizing the return on their investment.³⁷² This view of corporations appears to be too narrow. Both courts and legislatures permit corporate boards, in managing their corporations, to consider many factors other than shareholder wealth maximization. The SEC's and the courts' permissive approach to social proposals is thus consistent with other bodies of law that recognize that, because of the increasingly important role of corporations as legal persons within our society, there is a general expectation that corporations will behave responsibly.

While it is difficult to prove that shareholder proposals help them to do so, the cost to corporations and to society of social proposals is minimal. The best evidence that their usefulness outweighs the costs associated with social proposals may be the failure of corporations to mobilize to oppose them. Corporate managers may recognize the value of exchange with their shareholders on social issues, and they may also grudgingly appreciate the consciousness-raising effect that social proposals can have. Iroquois Brands' leadership may not have thought of itself as a corporation that catered to people committed to healthy lifestyles. However, because of Peter Lovenheim's proposal, it learned that it had a reputation for promoting food choices consistent with the humane treatment of animals. That information was likely useful to the corporation, even if the process through which the corporation achieved enlightenment involved some pain and even some embarrassment.

372. See *supra* text accompanying notes 314-16.

