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SHAREHOLDER ACTIVISM AND CORPORATE ETHICS - THE GOVERNMENT AS REFEREE

James C. Treadway, Jr.
Commissioner

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SHAREHOLDER ACTIVISM AND CORPORATE ETHICS -

THE GOVERNMENT AS REFEREE

Recent Developments In Shareholder Activism

As in most years since the late 1960's, this past year saw debates about corporate governance and the proper role of the federal government, if any, in influencing corporate management and corporate ethics. At issue was been the innocent-sounding "shareholder proposal rule," which permits shareholders to participate in their company's annual meeting by submitting proposals for inclusion in their company's proxy statement. The process sounds simple and straightforward; yet, I know of no other issue within our agency's jurisdiction which generates as much emotion and dissatisfaction. As the regulator of publicly-held companies and the protector of public investors, the Securities and Exchange Commission recently completed a study of the shareholder proposal rule and has modified -- very modestly, I might add -- that emotion-laden rule.

At the same time, perhaps for the first time, we have seen a substantial movement of large, institutional shareholders -- mutual funds, pension funds, educational and religious organizations, banks and insurance companies -- away from traditional support of management by voting in favor of proposals of dissident shareholders challenging management. This is a dramatic change in the prevailing attitude, which held that institutions should vote with management or sell out. That attitude had come to be known as the "Wall Street Rule," or more colorfully, "Voting With Your Feet."

Ten years ago such a result was virtually unknown. Shareholder challenges to management through the proxy process rarely have been successful and almost never have been supported by a majority of conservative institutional investors. During the past decade, the shareholder proposals challenging management most frequently were associated with controversial social or political issues, such as the war in Viet Nam, trade with South Africa, or the environment. Only a few institutional investors cast their lots against management, and these dissenters primarily were religious and educational institutions.

Yet, in an almost perverse sense, the aftermath of one of the most vicious corporate confrontations ever -- Bendix-Martin Marietta -- may have changed the prevailing attitude. That contest was labelled by one respected corporate head as "one of the sorriest spectacles in the history of American business."

Fearing a hostile takeover and repelled by the antics and excesses of "The Bill Agee and Mary Cunningham Show," many companies moved to discourage hostile takeovers by adopting antitakeover measures known as "shark repellents." Some attempted to set up staggered Boards of Directors, so that only a few directors can be elected in any one year and any unwelcome acquirer would not have a Board wholly responsive to its wishes for several years. Some have tried to change their bylaws and charters to require that any merger must be approved by 70%, 80% or even 90% of the shareholders. Others have tried to authorize large amounts of new stock carrying provisions that would unduly burden an acquirer, a technique known as a "poison pill."

But companies seeking shareholder approval of such measures have encountered stiff opposition, not just from individual shareholders with a political ax to grind or in pursuit of a social or ethical goal, but from institutional stockholders pursuing profits. Institutions have been in the forefront in voting down such proposals and in supporting contrary shareholder proposals just as openly as religious organizations opposed management on Viet Nam, napalm, South Africa and the Corvair. The institutions reason that such provisions make it difficult for a company to be acquired and therefore discourage offers at attractive prices. Yet, the institutional investors also recognize that such provisions insulate management from accountability for poor performance and stewardship of corporate assets which, after all, belong to the stockholders.

Shareholder Proposals and Corporate Governance

The issue of shareholder proposals is, of course, only a small part of the broader subject of corporate accountability, and that is not a new issue. Since the industrial revolution and the rise of the giant, widely-held corporation, the American public has been suspicious of corporate managers who manage a corporation's affairs without adequate shareholder scrutiny or control. In a reciprocal vein, the business community has never hidden its mistrust of dissident shareholders who promote their chosen causes and portray corporate managers in an unfavorable light. This historic tension between shareholders and management leads us to a broader question -- whether the government can act as a neutral "referee" when social and ethical issues are raised, or whether the government inevitably will find itself taking social and ethical positions despite proclaimed governmental neutrality.

I liken the Securities and Exchange Commission to a friend caught in the middle of a family feud, in this case between two of our constituencies -- public companies and public investors. We are supposed to referee disputes in an even-handed fashion according to strictly neutral rules. Yet, each side resents our involvement and feels that we are incapable of striking that magical balance which assures fairness to all with burden to none.

Let me give you a sample of the comments we received this past year as we considered changes. From the shareholder side: "Your proposals would snuff out the flickering light of shareholder democracy." From a corporate commentator: "You have no legal authority to be involved in the process in the first place. But it would take us ten years of litigation to straighten out out the mess if you withdraw." With that brief summary, and planning to return to more comments later, let me try to set the related issues of shareholder democracy and government involvement in ethical issues in some historical perspective.

The Origins of Federal Corporate Regulation

The Stock Market Crash

Today's scheme of federal regulation of the corporate world had its origins, as most know, in the Stock Market Crash of 1929. In the first eight years of the 1920's, prices on the New York Stock Exchange doubled. In the eighteen months between March, 1928 and October, 1929, the value of the same shares doubled again. Then came the Crash. Between October, 1929 and July, 1932, these same stocks declined in value by 83 percent. Blue chip stocks, including General Electric and U.S. Steel, lost over 90 percent of their value. Shares in the Transamerica Corporation, which owned the Bank of America, traded as low as 2-1/8 by 1932, down from $70. Between 1923 and 1930, prestigious and ethically minded investment banking houses sold Americans $6.3 billion in foreign bonds at commissions to the underwriters of 14 percent. By 1931, these bonds were utterly worthless.

As the market declined, the stock exchanges seemed unable or unwilling to police even the most brazen forms of manipulation. "Bear raids" and massive "short sale" schemes flourished. The "bears," believing the market price of a security would decline, sold stock first and borrowed the shares from a broker to deliver to the purchaser. They profited if the price in fact declined by purchasing shares at a lower price to return to the lending broker. The exchanges had no rules requiring brokers to secure permission from clients before lending the clients' shares to the

short-selling bears. A self-fulfilling prophecy was involved. The massive short-selling assured that that the price of the security would drop precipitously. The hapless investors, from whom the "bears" borrowed the shares to sell, had their securities returned to them, worth a fraction of their original value. The "bears" walked away with nothing but profits.

As bad or worse were the commercial banks. Prior to World War I, commercial banks generally were restricted to receiving deposits and making conservative consumer and commercial loans. Dealing in corporate securities by law was the exclusive province of the investment bankers. During the 1920's, these restrictions were openly evaded. Large banks set up securities affiliates, technically separate, to deal in securities. In one instance so outrageous as to be admired, the securities company's non-voting shares were printed on the back of the bank's stock certificates. The affiliates' capital was usually supplied by the bank. Voting shares in the affiliates frequently went to the bank's management, and the securities affiliates used bank employees to recruit public investors for issues of speculative corporate securities.

For example, The National City Bank, one of the largest in America, participated through its securities affiliate in offerings of $90 million in Peruvian bonds of highly dubious quality, generating $4.5 million in commissions which were shared by bank executives. By 1933, investors had lost $75 million on these bonds. Banks whose portfolios consisted of loans to speculative enterprises and whose financial stability was linked to the securities issues underwritten by their affiliates collapsed like houses of cards, triggering a nationwide run on bank deposits. By 1933, more than 12,000 banks had shut their doors, representing more than 40 percent of all banks in existence in 1921. Reflect on that for a moment -- almost every other bank in the United States failed.

Causes of the Crash

What caused this calamity? Economists have complicated theories, but some causes are not so complicated: fraudulent sales of speculative securities; a minimum of risk disclosure, false or inadequate financial statements; primitive accounting standards; high risk investments by commercial banks using the savings of innocent depositors; and manipulative sales practices which created an artificial securities market. But behind this free-wheeling speculation were largely ignored ethical questions -- the integrity of corporate manager and their accountability to shareholders, whose money they were using to finance their excesses.

In the celebrated study, Other People's Money, Louis Brandeis described a "financial oligarchy." The central figure was the investment banker, who eliminated competition within his industry through consolidation and combination. As railroads and public utilities likewise consolidated, they came to depend on the investment bankers to float stocks and bonds. Finally, the investment bankers became directors of the railroads and public utilities which issued the stocks and bonds, of the insurance companies and other corporate reservoirs of people's savings which bought the stocks and bonds, and of banks and trust companies which loaned their liquid capital to meet the temporary needs of the investment bankers, railroads, utilities, and insurance companies. The capital of the railroads, utilities and insurance companies in turn could be directed for deposit in the controlled commercial banks, which in turn could be directed by the investment bankers away from enterprises which might compete with their favored corporations.

The result was the complete estrangement of the stockholder from the management of the corporation the stockholder theoretically owned. In their 1932 classic work, The Modern Corporation and Private Property, Adolph Berle and Gardner Means examined the stockholder's position in the modern corporation:

> "The stockholder has changed his position in American financial life so radically that the old rules no longer apply. Originally he was supposed to be a kind of modified partner in a small enterprise, usually a business man of means, able to take care of himself, and to take active part in the counsels of his corporation. During the past generation this situation has almost completely reversed itself. There are about 5,000,000 persons in the United States who today own stock...and the number is steadily increasing. An overwhelming majority of these are "little people," that is, members of the investing public who own small blocks of stock, who know little or nothing about the corporate activities; whose advice is not sought in running the corporation and probably would be worth little if it were given.... [The stockholder] trusts implicitly to the corporate management; his function is merely to contribute the capital...."

In theory, the proxy was designed to remedy this estrangement by allowing the stockholder to appoint someone to represent him at the shareholders' meeting. But Thomas G. Corcoran, one of the members of Roosevelt's "braintrust" and a principal architect of the Securities Exchange Act of 1934, observed:

> "Proxies, as solications are made now, are a joke. The persons who control the machinery for sending out the proxies, with practically no [share] interest in the corporation, can simply keep other people from organizing, can get enough proxies to run the company. At most stockholders' meetings, no one turns up, and the proxy is always very carefully worded to approve all acts of the officers and directors for the preceding fiscal year."

Needless to say, there was no opportunity for shareholders to include proposals in the proxy statement on any issue, let alone on social or ethical issues. If you think Mr. Corcoran exaggerated the state of shareholder suffrage prior to 1934, consider the example of one public company which brazenly printed its proxy on the back of the dividend check. One endorsement fulfilled two functions. The only option was not to cash the check. Mr. Justice Brandeis observed, "[t]he fetters which bind the people are forged from the people's own gold."

Constitutional Constraints on Federal Intervention

What could be done about all this? Despite the devastation of the Crash, President Hoover had grave doubts about the constitutionality of any federal intervention in the capital markets or the corporate world, let alone intervention with ethical overtones. His fear was not unfounded. In a series of cases beginning about the time of mass industrialization in this country, the Supreme Court had invoked the due process clause of the Fifth and Fourteenth Amendments as a general substantive limitation upon the power of the government to further the public welfare by regulating private property. "Liberty of contract," a concept which had no specific constitutional blessing nor support in legal precedent but which was a creature of laissez-faire economic theory, became a vested constitutional right. Any statute which limited private property rights or freedom of contract was subject to attack. The Supreme Court readily examined any statute to determine whether it constituted a legitimate exercise of police power. Hoover himself was particularly opposed to a broad construction of the federal commerce power as a means to achieve regulation. "If we stretch the Interstate Commerce provision to regulate all those things that cross state lines," he once observed, "what becomes of the fundamental freedom and independence that can only arise from local self-government?"

Oliver Wendell Holmes, a conservative Republican who had embraced laissez-faire economics before he came to the bench, made a famous attack on the Court for injecting a laissez-faire economic theory into constitutional law in his dissent in a 1905 case, Lochner v. New York:

> "...[I]t is settled that state laws may regulate life in many ways which we as legislators may think as injudicious, or as tyrannical as this and which, equally, ...interfere with liberty of contract...The Fourteenth Amendment does not enact Mr. Herbert Spencer's Social Statics...a Constitution is not intended to embody a particular economic theory, whether of paternalism and the organic relationship of the citizen to the state or of laissez-faire. It is made for people of fundamentally differing views, and the accident of our finding certain opinions natural and familiar, or novel and even shocking, ought not to conclude our judgment upon the question whether statutes embodying them conflict with the Constitution of the United States."

Holmes' dissent ultimately supplied the theoretical support for the constitutionality of much New Deal legislation.

Roosevelt's election demonstrated either that the populace rejected Hoover's concerns or that they simply did not care about abstruse constitutional debates. But those who drafted the New Deal legislation knew that Hoover's concerns were real and that legislation regulating the corporate world could be unconstitutional if too broad or too intrusive. The resulting scheme of federal regulation, which seeks to preserve the interests of capitalism, private property and freedom of corporate managers on the one hand, but to operate as a protector of individual investors and depositors, displays the draftmen's concern about overreaching. The concepts of the federal government as referee and of regulatory neutrality are the result. "Let the captains of industry go their merry way, let market forces work, but protect the uninformed, the small depositor and investor, and the disadvantaged, all with strict neutrality and in an even-handed fashion."

Banking and Securities Legislation

By May, 1933, two critical pieces of federal legislation were in place. One was the Banking Act of 1933. That Act sought to separate commercial and investment banking by restricting commercial banks to receiving deposits and making commercial loans and prohibiting them from engaging in the securities business. In effect, the Act sought to restructure banking as it had existed before 1920. The Securities Act of 1933, the second principal law, required companies to disclose extensive data when they publicly offered their securities for sale and imposed liabilities upon the company's officers and directors, independent auditors, and the

investment bankers who acted as underwriters. Notwithstanding the urgings of many advisers to Roosevelt, the Act did not give the government the power to pass on the quality of securities or to allocate capital to industries chosen by the government. In promoting the Securities Act, President Roosevelt stated: "What we seek is a return to a clearer understanding of the ancient truth that those who manage....corporations....using other people's money are trustees acting for others." That simplistic approach -- particularly the concept of a trustee acting for others -- subtly altered responsibilities within the corporate structure. The Securities Act was designed to be a "reasonable" regulation of private property by interpositioning the federal government as a neutral referee between those who used the money of others -- the corporate managers -- and those who supplied the money -- the shareholders.

The claimed neutrality of the Banking Act and the Securities Act disappointed both New Deal Reformers and Wall Street. The reformers believed Roosevelt had not gone far enough; Wall Street believed it was being penalized and restricted because of Roosevelt's moralistic criticisms. In a sense, that was correct. Roosevelt, called by many a "traitor to his class," was outraged by what he perceived to be a total lack of morality and ethics in the marketplace, particularly on the part of the investment bankers.

The immediately following Securities Exchange Act of 1934 continued to expose internal corporate workings to public scrutiny. The basic thrust of the proxy provisions of the Exchange Act was accountability through disclosure, again proclaimed neutral regulation. The legislative history of the Exchange Act characterized the deficiencies of the then-existing system:

> "[I]t is essential that [the stockholder] be 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. Too often proxies are solicited without explanation to the stockholder of the real nature of the matters for which authority to cast his vote is sought."

But the power given the Commission extended beyond disclosure. The Commission was given the power to control the conditions under which proxies could be solicited, with a view to preventing abuses. With that broad mandate, the Commission adopted the first shareholder proposal rule in the early 1940's. In congressional testimony on the rule, Commissioner O'Brien said that the motivation behind the shareholder proposal rule was:

> "The desire to approximate the widely attended town meeting type of forum characteristic of the days when nearly all corporations were closely held and geographically limited..."

From that beginning the rule evolved until it required publicly-held companies to include in their proxy materials brief shareholder proposals, but only if the company could not find one of thirteen legal reasons to exclude proposals. The responsibility for determining whether a shareholder proposal could be excluded, in a contested case, was given to the Commission, with a right of appeal to the federal courts.

Shareholder Activism in the 1970's -- New Uses of The Shareholder Proposal Rule

The 1970's

The shareholder proposal rule, with all its potential impact on corporate ethics and management integrity, received little publicity during the 1940's and 1950's. But the late 1960's and 1970's brought dramatic change. Civil rights, the environment, Viet Nam, consumer safety and other equally visible issues combined to trigger a wave of shareholder activism. Stockholders found the largely dormant shareholder proposal rule to be an effective mechanism for airing controversial social and ethical issues. This in turn caused many to question whether the claimed neutrality of the securities laws was more myth than reality, and the Commission's ability to referee disputes with moral and ethical overtones was severely tested.

Dow Chemical Company and napalm provided the focus for the first severe test. Simmering criticism of Dow entered a new stage in 1970 when shareholders sought to include in Dow's proxy statement proposals to amend Dow's corporate charter to prohibit sales of napalm to any buyer unless the buyer gave reasonable assurance that the substance would not be used against human beings. The stockholders cast this ethical issue in economic terms, claiming that the manufacture of napalm was undermining Dow's efforts to recruit intelligent, well-motivated employees from college campuses and was adversely affecting Dow's growth.

Dow sought to omit the proposal on two grounds. Dow invoked that part of the rule which permitted a company to exclude proposals submitted primarily to promote "general economic, political, racial, religious, social or similar causes" and proposals relating to "the conduct of the ordinary business operations of the company." Dow claimed that the decision to manufacture a

particular product involved "ordinary business operations" and cited general opposition to the war in Viet Nam to demonstrate that the proposal primarily promoted a "political, social or similar cause."

The Commission concurred in Dow's decision. The shareholders sought judicial review of that decision. The reviewing Court ordered the Commission to reconsider its decision, holding that

> "[n]o reason has been advanced...which leads to the conclusion that management may properly place obstacles in the path of shareholders who wish to present their co-owners, in accord with applicable state law, 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."

The Court pointed out that Dow's own publications indicated

> "that the decision to continue manufacturing and marketing napalm was made not <u>because</u> of business considerations, but <u>in spite</u> 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 the management considered this action morally and politically desirable."

Noting that "the proper political and social role of modern corporations" and "the substantive wisdom or propriety of particular corporate political decisions" were outside the scope of the Court's decision, the Court nonetheless strongly endorsed shareholder review of corporate decisions with political or ethical implications.

Almost simultaneously occurred Campaign GM, which grew from the efforts of a group of young lawyers interested in reforms directed "toward institutions of government and the courts -- to begin facing an entire spectrum of social wrongs." The founders believed that these objectives could not be accomplished "without a commitment of corporate institutions, which have enough power to implement or deny national goals."

Three stockholder proposals were submitted to General Motors:

- One called for an amendment to GM's charter to limit operations to those consistent with "public health, safety, and welfare."

- The second sought the establishment of a shareholder committee on corporate responsibility, composed of representatives of environmental, civil rights, labor, academic, and other groups.

- The third sought public interest representatives on GM's Board of Directors.

Lines were quickly drawn. GM announced its intention to exclude all of Campaign GM's proposals, claiming they had been submitted primarily to promote "general economic, political, racial, religious, social or other similar causes." GM management also be claimed that the proposals related to "ordinary business operations." In a seventy-page letter to the Commission, GM argued that the securities laws gave shareholders access to management's proxy materials to contact fellow shareholders only on matters concerning them in their capacity as corporate owners. GM charged that Campaign GM was not interested in communicating with fellow shareholders as such, but in their capacity as public citizens.

Campaign GM questioned how GM could characterize the same proposals as "ordinary business matters" and as "general economic, political, racial, religious, social or other similar causes." In its submission to the Commission, Campaign GM explained that

> "this is an effort to adapt the tool of shareholder democracy for the less pecuniary side of stock ownership. No one seriously challenges the use of the proxy machinery when it is employed to seek greater rewards for their ownership, and the same permissiveness should prevail when proxy machinery is sought to be used to assert the responsibility of ownership. Just as the first is not the exclusive domain of management, neither is the second."

Contrary to its decision to support management in the DOW case, the Commission decided that two of Campaign GM's proposals qualified for inclusion in GM's proxy statement, the resolution to expand the Board of Directors to allow for public representatives and the resolution to establish a shareholder committee on corporate responsibility. This decision allowed the proposals to be distributed to GM's 1.3 million shareholders and gave the dissidents an opportunity to engage GM's management in a discussion of social and ethical issues at the company's annual meeting. GM's 1970 annual meeting was a watershed, lasting 6-1/2 hours. 3,000 people attended. Management handily defeated all proposals.

Yet, with a resounding victory, GM's management almost immediately took several actions which closely paralleled Campaign GM's demands. A public policy committee composed of five outside directors was named to monitor social performance; GM named its first black director; and a special committee of scientists was formed to study the environmental effects of GM products.

Would these changes have occurred if the Commission -- the government -- had not required GM to include the proposals in its proxy statement? Many say no. And if governmental regulation forced these social and ethical issues to be aired, which in turn led to change, can it be said that the government was neutral?

Many undoubtedly recall that the Episcopal Church first introduced to corporate proxy materials the now familiar subject of investment in South Africa. In 1971, the Church submitted a resolution calling for GM to withdraw its manufacturing operations from South Africa. The Presiding Bishop attended GM's annual meeting and spoke in favor of the proposal. The proposal received the support of only 1% of the shares voted, but received considerable attention when the Reverend Leon Sullivan, the first black member of the Board of Directors of GM, announced that he disagreed with the other Directors and supported the proposal.

The 1982 Review

A dozen years of continued dispute and broad dissatisfaction followed, although nothing as spectacular as Dow and Campaign GM came along. That brings us to 1982. For the year ended June, 1982, 973 shareholder proposals were submitted to 358 public companies. But remember that there are almost 10,000 public companies. Almost half of all stockholder proposals submitted were either withdrawn or accepted uncontested. Similarly, in the 1983 proxy season, only 111 management-opposed resolutions that raised social or ethical questions were voted on by shareholders of only 73 companies. The 111 proposals are those which made it into the proxy statement and were not withdrawn or successfully contested by management before the Commission. The resolutions which received the highest percentage of favorable votes were in three categories -- South Africa, energy, and labor relations. All but one of the high-scoring resolutions were church-sponsored.

The 1982 and 1983 statistics show that the number of proposals is small, that not many proposals make their way into the proxy statement, and that management usually defeats them handily. Yet we at the Commission discovered the depth of emotion attached to this rule when we recently considered revising it in response

to the continuing complaints from corporate executives who claim that the 1970's have left them victims of social engineering, from shareholders who see management as insensitive to all social and ethical issues, and from both sides who see the Commission as an ineffective judge of social and ethical issues.

The Three Proposals

The Commission published for public comment three alternative proposals.

1. The first proposal called for keeping the shareholder proposal process largely intact, modifying slightly the bases for exclusion, but imposing for the first time an ownership eligibility requirement.

2. The second proposal contemplated that the shareholders of an issuer could decide the extent of shareholder access to the proxy statement. Any such plan would require initial shareholder approval and periodic reapproval and amendments could be proposed by the Board of Directors or by any shareholder. This proposal was generally considered to be advantageous to management, which rarely has difficulty in garnering support for its positions and which could develop a plan unfriendly to shareholder activists. The proposal also would have removed the Commission from our role as referee, a move with some attraction.

3. The third proposal went to the other extreme. A corporation would have been required to include in its proxy material all shareholder proposals not improper under state law and not related to the election of directors. This approach would have eliminated eleven of the existing thirteen grounds for the exclusion of proposals, and thus much debate. Disputes would be resolved by the courts, not by the Commission. As with the second proposal, the Commission would have been relieved of making judgments on non-legal, social, ethical and business issues.

Those disposed toward Proposal 2 or 3 were quick to point out that the Commissioners have no particular expertise when it comes to social or ethical issues. We have different professional backgrounds -- three lawyers, an economist and an investment banker; none of us has formal schooling in the field of ethics; our geographic origins differ -- Utah, California, New York, New Jersey,

and South Carolina; ages range from the 30's to 60; the religious composition is diverse; and political affiliations by law must be varied. So why would anyone consider this group better equipped than the general population to pass upon difficult social and ethical issues? For those of us who are not certain that we are the sole repository of all ultimate wisdom, those arguments had some appeal. So we proposed change.

We received more than 400 comment letters in response. With rare exception, the comments were laced with emotion. A Roman Catholic Nun who handles shareholder proposals for the Sisters of Charity of Nazareth recalled with pride that she had been "a real thorn in the sides of corporations." A senior vice president of Bank of America griped that in recent years "the Bank's proxy statement read like a current events magazine." One writer urged the Commission to "preserve free enterprise." A state senator urged the Commission to "allow shareholders the freedom to govern their own affairs." Another writer urged us to "spike the gad-flies." A well-known stockholder activist accused us of treating the small stockholder as insignificant: "Perhaps Chairman Chad [sic] should have been made Secretary of the Treasury and Don Regan Chairman of the SEC because Merrill Lynch never found a small stockholder to be so unimportant."

And how did the vast majority recommend that we do all of this? Essentially by doing nothing, by leaving this maligned process, criticized as unfair to all, intact. That's right, leave it alone, leave the Commission in its role as a misguided, ineffective arbiter seeking a totally elusive goal of neutrality.

The Current Rule

The only modest changes we adopted require that a proponent must own $1,000 worth of stock and must have held that stock for at least a year. I might add that this change found little acceptance from many stockholder activists, who argued that it was the importance of the issue, not the size of the investment, that mattered. In addition, a proponent is now limited to one proposal for each company instead of two. The modified rule retained the existing thirteen grounds for excluding stockholder proposals. The grounds under which most shareholder proposals are most likely to be contested are:

- If the proposal relates to a personal claim or grievance against the corporation. A new section adds that the proposal may be excluded "if it is designed to result in a benefit to the proponent or to further a personal interest, which benefit or interest is not shared with the other security-holders at large;"

- If the proposal relates to matters that account for less than 5% of the assets, net earnings and sales at the end of the most recent fiscal year "and is not otherwise significantly related to the issuer's business." In other words, if a proponent is not able to meet the asset requirement test, he still may argue that his proposal is significantly related to the issuer's business.

- If the proposal is beyond the company's power to effectuate;

- If the resolution deals with the ordinary business operations of the corporation;

- If the proposal is "substantially the same subject matter" as one voted on by stockholders within the last five years that has not received enough votes for resubmission. Levels for resubmission were raised from 3% to 5% the first year and from 6% to 8% the second. Several shareholder proposals received more than 3% of the vote this year but less than 5%, and hence will be ineligible for resubmission during 1984.

What Did We Learn?

The time has come to try to draw some conclusions.

My first conclusion is that it apparently was necessary for us to have this debate. Fifty years of federal regulation have not removed the tensions between corporate managers and shareholders. Unless and until one side or the other -- managers or stockholders -- is given clear dominance, the tensions and debate will continue. As long as that is the case, and as long as the federal government attempts to serve as a neutral referee, neither side will be totally satisfied. The alternatives to the Commission as a neutral referee include, at the outer edges, a total withdrawal of the government from ethical issues, an approach rejected during the reconsideration of the rule, and direct ethical decision-making by the federal government, which smacks of a theocracy.

My second conclusion is that the recent debate affirms the legality of a federal presence in the corporate world, even if that governmental involvement in ethical issues, particularly if that presence is cloaked with a claim of neutrality. In fact, only a very few of the 400 commentators even questioned the legality and propriety of an almost pervasive federal presence.

My third conclusion is that few on either side, shareholder or corporate manager, really wish to see the federal government removed from dealing with ethical and social issues. Notwithstanding constant criticism about the degree of governmental involvement in our lives, sometimes in bombastic tones, very few truly seem to want a total withdrawal of the federal government.

My fourth conclusion is that our performance as a proclaimed neutral referee never will be totally satisfactory as long as the issues stockholders wish to place before their fellow stockholders have ethical or overtones.

My final conclusion is that governmental neutrality is a myth and that true neutrality is impossible. Yet, as long as we strive for neutrality, we legitimize the entire process and our involvement, even in the areas of ethics and morality.

My conclusions leave uncertainty and doubt about the proper role of the federal government in the field of ethics, and I acknowledge that I have delivered my comments without answering any questions. But I understand that closing on such a note is appropriate in this Cathedral. I am told that Dean McGehee is fond of saying that his responsibility is to bring doubt to the faithful. That was not my goal when I first began to prepare these comments, but perhaps that is where I end, on a note of doubt, leaving you to continue this debate.

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