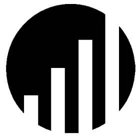

IRRC

CORPORATE

SOCIAL ISSUES

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# SEC Approves Mutual Fund Proxy Vote Reports

As expected, the SEC has adopted a rule that will require mutual funds to disclose their actual proxy votes as well as their proxy voting guidelines and procedures. The 4-1 vote in favor of the rule came at an open meeting Jan. 23. The commission also unanimously approved a companion rule requiring disclosure by investment advisers.

The final rule dropped a requirement in the original proposal that would have forced mutual funds to highlight proxy votes that are inconsistent with their policies and disclose the reasons for those inconsistencies. It also changed the timetable for reporting votes from twice to once a year. But the guts of the proposal remained intact, greatly disappointing the traditional mutual fund industry, which had lobbied hard against it and predecessor proposals for years.

The comment period on the rule had closed Dec. 6, and the seven-week approval period was relatively short for the conclusion of a rulemaking on a controversial issue. During the Sept. 19-Dec. 6 comment period, the commission received about 8,000 letters on the proposal, most in favor, in a campaign largely orchestrated by labor unions and strongly backed by social investment funds. The traditional fund industry, led by its Investment Company Institute lobbying arm, waited until the end of the comment period to weigh in, apparently in an effort to make it more difficult for supporters of the rule to have an opportunity for formal rebuttal. In their filings, the ICI and supporters of the proposal differed strongly on the costs of disclosure. (Earlier stories/*Corporate Social Issues Reporter*/October 2002 lead story and December 2002 pps. 9-10)

*Pitt had pushed hard for the proposal when the rulemaking was approved, and he again praised it as necessary to prevent mutual funds from voting in ways that conflict with fiduciary duty.*

During the seven-week interlude before final approval, the debate continued and gained some new actors. The proposal got important support in the form of a Dec. 16 letter to the SEC from two senior Republican congressmen—Rep. Michael Oxley (R-Ohio) and Rep. Richard Baker (R-La.)—who chair the House panels that oversee the SEC. "Making mutual fund voting transparent will strengthen investor confidence by providing another powerful tool to promote corporate accountability and responsibility," the letter said. Retired Vanguard Group founder John Bogle weighed in with a *New York Times* op-ed piece supporting the proposal at about the same time.

The opposition was underscored when the chief executives of two of the nation's largest mutual funds joined forces to write a January *Wall Street Journal* opinion piece blasting the proposal.

Fidelity Investments Chairman and CEO Edward Johnson and Vanguard Group Chairman and CEO John Brennan argued that requiring mutual funds to disclose their votes would politicize the process and "open mutual-fund voting decisions to thinly

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*Published by IRRC's Social Issues Service*

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veiled intimidation from activist groups whose agendas may have nothing to do with maximizing our clients' returns….The effect would be to make mutual funds the prime pressure point for every activist group with a political or a social ax to grind with corporate America," the two said.

In the week before the vote, the fund industry attempted to press home its argument that the disclosure of individual votes would be unfairly costly and burdensome by sending the commissioners and selected reporters telephone book size documents listing votes for three funds—Fidelity Spartan Market, Vanguard Balanced and T. Rowe Price Extended Market—which have more than 2,300 stock holdings.

When the vote came, four commissioners—outgoing Chairman Harvey Pitt, Democrats Harvey Goldschmidt and Roel Campos and Republican Cynthia Glassman—voted in favor, while Republican Paul Atkins cast the no vote. Pitt had pushed hard for the proposal when the rulemaking was approved, and he again praised it as necessary to prevent mutual funds from voting in ways that conflict with fiduciary duty when they were hoping for business such as 401-k management from companies in their portfolios.

In discussing his no vote, Atkins, who had originally voted in favor of the rulemaking, said he had come to agree with the traditional fund industry that the costs of the rule would outweigh the benefits. He also protested that the rule would institute reporting that was of little interest to most mutual fund investors, saying that "Mutual fund companies today have an incredibly hard time getting their own shareholders to even mail in their own proxies on fund governance matters." And Atkins objected that the rule unfairly singled out mutual funds, while insurance, pension funds and bank trust departments were not required to report votes. On that last point, Robert Plaze of the SEC Investment Management Division, which wrote the rule, responded that insurance and pension funds, rather than their beneficiaries, bear the risk of investing in companies whereas mutual fund shareholders take the risks. He pointed out that the rule does not apply to bank trust departments because they are regulated by the Office of the Comptroller of the Currency, not the SEC. *The Washington Post* Jan. 31 said the OCC was now examining the issue as a result of the SEC change. It quoted an OCC spokesman as saying: "We are reviewing the issue because of recent developments and we're planning to do the review with an eye toward possible regulatory changes."

## Reaction

Once the rule was approved, its supporters were strong in their praise. Timothy Smith, the head of the Social Investment Forum, said in a statement: "It is important to remember that corporate scandals like Enron, Tyco and WorldCom were not caused by executive greed alone. Mutual funds were among those who approved Enron's board of directors, supported CEO compensation packages, and voted against numerous corporate governance measures that may well have prevented some of the abuses we're recently witnessed."

From the other side, pronouncing the industry "disappointed," Matthew Fink, president of the ICI, said: "Making mutual funds the only investment entities required to report all of their individual proxy votes will undoubtedly embolden outside special interests. This will not serve the interests of mutual fund shareholders—to whom the industry owes its sole allegiance. We urge the SEC at a later date to revisit the effectiveness of disclosing actual proxy votes."

An outside fund industry observer had little sympathy with the industry. Donald Phillips, managing director of the fund-rating service Morningstar, told CBS.MarketWatch that by keeping relatively silent instead of expressing outrage when corporate accounting scandals were breaking, the industry had opened itself up to more regulation.

## SEC Release

The SEC posted a 49-page release discussing the new rule on its web site (www.sec.gov/ file S7-36-02) Feb. 4. Making the general case for the rule, the release argues that "shedding light on mutual fund proxy voting could illuminate potential conflicts of interest and discourage voting that is inconsistent with fund shareholders' best interests." It also speculates that requiring transparency in voting could encourage funds to get more involved in the corporate governance of the firms in their portfolios, "which could benefit all investors and not just fund shareholders."

Discussing the response to arguments made during the comment period, the release takes up the point made repeatedly by the traditional fund industry—that the rule was unnecessary because fund shareholders aren't interested in proxy voting. That point, the release says, was "to some extent belied by the large number of favorable comments from individual investors that the proposal attracted." Moreover, it said, even if a majority of investors are indeed not interested, those that are "have a fundamental right to know how the fund has exercised its proxy votes on their behalf."

In discussing changes to the original proposal, the release says the requirement for disclosure of votes that are inconsistent with fund guidelines was eliminated for two main reasons: in response to the argument of rule supporters that it would lead to overly broad guidelines, and in response to the concern of opponents that it would require analysis of a large volume of votes that would be expensive to prepare and not very useful. The release indicated the requirement for semi-annual reporting in the form N-CSR was switched to annual reporting through the form N-PX largely because of cost concerns voiced by com-

mentators. In another change motivated by cost considerations, the final rule permits funds to choose to make their records available either on request or through their websites, rather than requiring them to make them available on request.

The release estimates the total costs of additional disclosure at $12,725,253. It pronounced that estimate "reasonable," and noted that it was based in part on the information provided by funds that already disclose their votes.

### Details of the Final Rule

Under the rule approved Jan. 23, mutual funds and other registered management investment companies will be required to disclose the following.

- **Investment Company Proxy Voting Policies and Procedures.** The amendments will require a fund to disclose in its registration statement the policies and procedures that it uses to determine how to vote proxies relating to portfolio securities. This disclosure must include the procedures that a fund uses when a vote presents a conflict between the interests of fund shareholders, on the one hand, and those of the fund's investment adviser, principal underwriter, or certain of their affiliates, on the other. Disclosure of proxy voting policies and procedures will apply to filings made on or after July 1, 2003.
- **Investment Company Proxy Voting Record.** The amendments will require a fund to file a new form, containing its complete proxy voting record for the 12-month period ended June 30 by no later than August 31 of each year. Funds will be required to disclose the following information for each matter with respect to which a fund was entitled to vote: information identifying the matter voted on; whether the matter was proposed by the company or shareholder; whether and how the fund cast its vote; and whether the fund cast its vote for or against management. Funds will be required to make their first proxy voting disclosures no later than August 31, 2004, for the 12 months ending June 30, 2004.
- **Availability of Proxy Voting Information to Fund Shareholders.** A fund will be required to state in its reports to shareholders that information about the fund's proxy voting policies and procedures is available without charge, upon request, by calling a specified toll-free (or collect) telephone number; on the fund's web site, if the fund chooses that alternative; and on the SEC's web site. If the fund chooses the telephone request route, rather than web site posting, it must provide the information within three days of the request. A fund will be required to state in its registration statement and reports to shareholders that the fund files its proxy voting record with the SEC and that the record is available on the SEC's web site and from the fund. A fund will be permitted to make the proxy voting record available either on its web site or upon request.

*—Carolyn Mathiasen*

# SEC Makes First 2003 'No-Action' Decisions

The Securities and Exchange Commission staff is beginning to issue "no-action" letters responding to companies' requests to omit shareholder resolutions from their 2003 proxies under the exclusions allowed by the shareholder proposal rule. So far, as is typical, many of the decisions allowing omissions have come on relatively easy calls involving resolutions that aren't from seasoned proponents, but the staff made interesting judgments on a new variation on global warming resolutions and on a proposal relating to the glass ceiling. Following is a rundown of the action to date.

### Disclose Emission Risks

A Feb. 5 no-action letter allows **Cinergy** to omit a new proposal from the Presbyterian Church asking it to report on risks associated with emissions of carbon dioxide, sulfur dioxide, nitrogen oxide and mercury, as well as the economic benefits of committing to a substantial reduction of those emissions. The staff agreed with the company that the proposal was excludable as an ordinary business issue, noting that it deals with "evaluation of risks and benefits." The proposal was submitted to four other utilities as well, where the outcomes are unclear. The SEC has been short-staffed in recent years, and not all no-action correspondence makes it to the Public Reference Room, making it difficult for IRRC and others to monitor developments. The proposal appears to have been challenged at AEP, PG&E and Xcel Energy, but not at Southern and TXU.

By contrast, the staff refused to allow **Weyerhaeuser** to omit as ordinary business a new resolution from the Sierra Club asking it to report on all fines and penalties under environmental laws, the amount of greenhouses gases emitted, and the feasibility of having the company's timber operations certified by the Forest Stewardship Council. It did require the Sierra Club to make a number of changes in parts of the supporting statement that it deemed false and misleading.

### Glass Ceiling

In a decision that "really surprised" the

proponents' lawyer, SEC shareholder proposal rule specialist Paul Neuhauser, the staff allowed **Johnson & Johnson** to omit a new resolution on the glass ceiling.

While the staff has generally agreed that the glass ceiling is a legitimate subject for shareholder resolutions (except during the period in the mid-90s when it was disallowing all employment-related issues), it bought the company's argument that this particular proposal could be excluded under section (i)(3) of the shareholder proposal as vague and indefinite. The resolved clause of the proposal asked for a report on steps the company had taken to use the Glass Ceiling Commission report.

The Feb. 7 no-action letter did not elaborate on which of the company's arguments it found persuasive. While the SEC staff in recent years has by and large been sympathetic to the proponents, it has accepted an occasional challenge on (i)(3) grounds. Most notably, in 2001, it allowed a batch of companies to exclude resolutions asking them to base global employment codes on the SA 8000 Social Accountability Standards, accepting the company's argument that the resolution was impermissibly vague because it didn't spell out what would be required. In asking for a no-action letter, Johnson & Johnson referred to that decision and argued that its resolution—which has the same resolved clause but a shorter supporting statement than other recent glass ceiling resolutions—was vague because it "is completely devoid of any description of the substantive provisions of the 'Glass Ceiling Report' or the recommendations 'flowing from it.'"

## Close Israeli Operations

**Hewlett-Packard** has gotten the green light to omit a proposal from a new proponent, Miriam Reik, asking it to close its offices in Israel, divest itself of any land owned there and send letters to Israeli officials saying that it cannot operate there while the government "ignores UN resolutions and violates international human rights standards, in its occupation of Palestinian territories."

The SEC staff allowed the omission under a part of the shareholder proposal rule sometimes known as the "relevance clause," which it has said it finds difficult to apply, and which it did not invoke at all for social issues resolutions in 2002. That's section (i)(5), which allows companies to exclude proposals that account for less than 5 percent of business and are not "otherwise significantly related" to their business. In the case of this particular resolution the staff had a precedent—the use of (i)(5) back in 1992 to allow AT&T to omit a resolution asking it to phase out services to Israel. H-P cited that decision and argued successfully that not only did the proposal not meet the economic test, but also that the policy issue, Israel's treatment of Palestinians, was not related to its business.

## Health

The church-affiliated proponents scored a win in their new campaign asking companies with leverage in the labor markets of sub-Saharan Africa to report on the effect of deadly diseases on their operations and on measures taken in response. **Caterpillar** had argued that that proposal should be excludable under (i)(5), the relevance clause, because its operations accounted for only 1 percent of assets and 3 percent of sales and the proposal does not raise issues that are significantly related to its operations. The SEC staff rejected the argument, saying only that "We are of the view that the proposal is 'otherwise significantly related' to Caterpillar's business."

The same proposal, one of the six to multinationals on African health, has been withdrawn—at **Colgate-Palmolive**. The company reached the following agreement with lead filer Walden Asset Management and the co-proponents:

- Colgate-Palmolive will include a section on the HIV/AIDS pandemic in its planned global sustainability report for 2003. The section will report on Colgate's policy and some of the initiatives and programs in this area, similar to the information that has been provided to the resolution proponents.
- Colgate-Palmolive intends to distribute the global sustainability report to shareholders, and to others that request such information.
- Colgate-Palmolive agrees to continue a dialogue, as appropriate, with concerned shareholders about policies and practices to address the health pandemics in Africa.

A second type of resolution on African health—this one to drug companies—has passed muster at the SEC. The proposal asks six companies to establish and implement standards of response to HIV/AIDS, TB and malaria. The staff refused to agree with **Johnson & Johnson** that the proposal could be omitted on ordinary business grounds, noting that "the proposal appears to raise significant social policy issues." It also rejected arguments that the proposal was excludable under the "relevance" (i-5) and "vague and misleading" (i-3) exclusions. The proponents had rewritten a 2002 resolution dealing with the same diseases, which they had withdrawn last year because it did appear vulnerable on ordinary business grounds. After the no-action request was rejected, the company and proponents reached a withdrawal agreement; details are not yet available.

**Johnson & Johnson** was, however, allowed to omit a second health resolution asking for information on incentives to doctors and pharmacy benefit managers; in that case, the staff concluded that the proposal dealt with ordinary business operations in the form of "sale and advertising of particular products." It's not yet clear whether the same proposal was challenged by the three other recipients, Pfizer, Schering-Plough and Wyeth.

## At SEC, Pfizer Wins But Pepsi Fails

Two no-action letters from the SEC, written on the same day by the same attorney, ruled that **Pfizer** could omit a resolution requesting it to report to shareholders explaining each tax break that provides the company with more than $5 million of tax savings, but that **PepsiCo**, which received the same resolution, could not. Both companies argued in their no-action requests that the proposals, submitted by the nonprofit organization Responsible Wealth, could be omitted from the company proxy on the grounds that the resolutions pertained to "ordinary business," a justification for exclusion under SEC rule 14a-8(i)(7).

These rulings are interesting not only because one attorney wrote both on the same day, but because the SEC has been criticized in the past for its inconsistent rulings regarding similar shareholder proposals. Although on the surface the PepsiCo and Pfizer no-action letters appear to be an example of this inconsistency, further analysis of the companies' arguments shows that the SEC evaluated the legitimacy of the arguments made by both companies and based the ruling on a significant difference in their arguments.

Both companies use the ordinary business exclusion as their main justification for omission, citing the following reasons as evidence:

- the financial reporting required by the shareholder resolution is not required by law,
- the resolution improperly "micro-manages" the companies' operations,
- the resolution is not related to a significant policy issue, and finally—
- the resolution's request for a report instead of a significant policy change is irrelevant when considering exclusion under ordinary business.

Although the Pfizer arguments are more clearly articulated and provide more citation, both company no-action requests cite similar rulings made by the SEC to justify their claims.

Pfizer's success at the SEC appears to be that it persuaded the staff attorney that, as he wrote in the no-action letter to Pfizer, "There appears to be some basis for your view that Pfizer may exclude the proposal under rule 14a-8(i)(7), as relating to its ordinary business operations (i.e., disclosure of the sources of financing)." The SEC's parenthetical emphasis on "sources of financing" is key. In its no-action request, Pfizer provided citation that the SEC had ruled in the past that "sources of financing," including tax sources, are a matter of ordinary business, and therefore shareholder resolutions addressing this issue could be excluded from a company's proxy. This argument is the only argument Pfizer made that PepsiCo did not, and was, in fact, the first argument Pfizer used to justify its claim. The SEC no-action letter to PepsiCo, in contrast, states, "We are unable to conclude that PepsiCo has met its burden of establishing that PepsiCo may exclude the proposal under rule 14a-8(i)(7)."

*—Daniel McQueen*

### Charitable Contributions

A number of the early omissions involved resolutions on contributions to specific organizations, an issue that the SEC staff for years has considered a mundane, "ordinary business" matter that is for management, not shareholders, to decide. **Morgan Stanley** was allowed to rely on the ordinary business clause (i)(7) to omit a resolution from another new proponent, Robert Allen, to discontinue support for National Public Radio. The whereas clause asserted that NPR "routinely violates the Code of Ethics of the Society of Professional Journalists" in giving disproportionate weight to Arab speakers in its coverage of the Middle East.

Similarly, **SBC Communications** was allowed to omit as ordinary business a proposal from the Welt-Katzen Irrevocable Trust asking it not to support media outlets that undermine the war on terror. The supporting statement made clear that the proponent was concerned about NPR's failure to use the word terror in discussing Hamas.

Another nascent campaign appears to have been stillborn with the omission of proposals from Roberta Rubin asking companies to make donations to the Foundation for the Advancement for Monetary Education and support its proposed "new monetary structure that satisfies the needs of industrial companies." The proposal was omitted at **Eli Lilly, Intel** and **Johnson & Johnson** on ordinary business grounds and omitted at **Southwest Airlines** because the proponent failed to provide proof of beneficial ownership. Several more requests for omission of the same proposal are still pending but will presumably be granted.

A resolution asking **Wachovia** not to contribute to a new Charlotte Uptown Arena from David Pasek, spokesman for the Arena Boycott Committee, was also omitted as ordinary business.

And **Bank of America** was allowed to rely on the ordinary business clause to omit a proposal from Virginia Brown asking it to refrain from making contributions.

The staff did require **Dow Jones** to include a proposal from John J.

Crapo asking it to report on its charitable giving policy. But it agreed with the company that it could omit the entire supporting statement under section (i)(3) of the shareholder proposal rule—vague and misleading. The company had argued that it was unintelligible.

### Other Decisions

The SEC staff has deflated United for a Fair Economy's new effort to get companies to disclose more about tax policy. It agreed with **Pfizer** that the proposal asking for detail on tax breaks that provide more than $5 million in savings raised an ordinary business issue because it dealt with "disclosure of the sources of financing." Oddly enough, the SEC staff told **PepsiCo**, which also challenged an indentical proposal on ordinary business grounds, that "We are unable to conclude that PepsiCo has met its burden of establishing that PepsiCo may exclude the proposal under rule 14a-8(i) (7). (For more on the SEC's reasoning in these two cases, see the box on p. 6.) The third resolution, to Raytheon, does not appear to have received a challenge. UFE first brought the issue up several years ago at AT&T, which let it come to a vote without going to the SEC.

**Coca-Cola** was allowed to omit part of the supporting statement of its resolution on the application of International Labor Organization standards to its operation in Colombia on grounds that it was misleading.

*—Carolyn Mathiasen*

# Hevesi Inaugurated as NY State Comptroller

Last month, Alan G. Hevesi took the helm of New York State's $102 billion common retirement fund, the second largest in the nation and one that serves more than 300,000 retirees. As New York State's 53rd comptroller, Hevesi also will keep close watch over the state's fiscal practices. Hevesi's win over Republican John Faso in November's elections marked his comeback to public office following his fourth-place showing in New York City's mayoral race in 2001. Hevesi had vacated his position as New York City's comptroller to vie for the city's top executive position that year.

In his eight years as New York City's comptroller, Hevesi had been one of the most vocal city comptrollers in the country. In addition to mounting several successful shareholder campaigns on Northern Ireland, labor rights and the environment, he successfully challenged Swiss banks to gain reparations for Holocaust victims and their families. Hevesi's approach at the time stood in contrast to his Democratic colleague on the state level, H. Carl McCall, who chose to wield shareholder power with a gentler hand. So, many are assuming that Hevesi's ascent to the state level will bring with it the strong possibility that he will employ his more activist style in managing the New York State Common Retirement System, but will he?

Hevesi has taken over the state's pension fund system at a grim time, with the economy sagging, stocks falling and Republican Governor George E. Pataki calling for across-the-board cuts of 5 percent in state spending to bridge a state budget deficit nearing $10 billion. Hevesi has said that he will reduce his 2,400-person staff, mainly through voluntary means, but possibly through forced layoffs, to cut costs. This will happen at a time when what staff is left will be conducting a comprehensive review of the state's pension fund investments, following a 20 percent drop in their value from a peak of approximately $127 billion in 2000 to $102 billion today. So, whether there will be time, resources or will to revamp the funds' proxy voting guidelines or jump on board to sponsor shareholder resolutions this year or even next is questionable. So far, there is no indication from Hevesi's staff that there are any plans in place or in the works.

### Differing Styles

As New York City's comptroller, Hevesi waged a wide range of corporate responsibility campaigns, including one in support of the Coalition of Environmentally Responsible Economies (Ceres), a partnership of companies, investors and environmental groups formed after the 1989 Exxon Valdez oil spill. In support of Ceres, New York City sponsored resolutions asking companies to adopt the Ceres Principles, a 10-point environmental code, which includes commitments to sustainable development, collaborative dialogue with stakeholder groups and verifiable forms of reporting on environmental progress.

On employment issues, Hevesi continued New York City's support of the MacBride principles, a set of nine equal opportunity principles aimed at fighting religious discrimination in employment in Northern Ireland, cofiling a number of resolutions asking companies to implement the principles. Hevesi also sat on the advisory board for Social Accountability International's SA 8000 program, a labor rights code of conduct and monitoring certification program based on the International Labor Organization's conventions and workplace health and safety standards. In 2000, he launched a shareholder campaign asking companies to incorporate the ILO's core conventions into codes of conduct and to

have independent monitors, such as those certified under Social Accountability International's SA 8000 program, to verify compliance. Under Hevesi's leadership, New York City also was the lead proponent of a 1992 resolution to Cracker Barrel Old Country Store on sexual discrimination in the workplace that set off court cases and a controversy over whether workplace issues were suitable subjects for shareholder resolutions. The SEC used the Cracker Barrel resolution as a vehicle to disallow all employment-related proposals, a decision that was finally reversed in 1998 after legal machinations and proponent protests.

While it never resulted in shareholder actions, Hevesi also played a key role in convincing Swiss banks to agree to a $1.65 billion settlement of Holocaust-related issues. He organized a network of 900 state and local finance officials to pressure the banks. The threat of sanctions by that group brought an end to delaying tactics by the Swiss banks, and the group continues to monitor how banks and companies in other areas of the world respond to Holocaust-related issues.

### A Subtler McCall

McCall's approach to shareholder activism is lower key, with a mixed record in voting and more abstentions and behind-the-scenes prodding. McCall's office responded to IRRC's 2002 proxy voting survey, furnishing a copy of a number of key votes and a copy of New York State's proxy voting guidelines. On social issues, the policy said that it casts votes case-by case "consistent with the comptroller's fiduciary responsibility to preserve the principal of the fund and maximize the long-term economic value of its investments." On environmental proposals, it said that it "generally abstains on resolutions protecting the environment" unless a "specific action can significantly improve a company's poor environmental record."

In 2002 the fund, in addition to continuing its long-standing support for MacBride proposals, voted in favor of New York City's ILO standards proposals at American Eagle, Colgate-Palmolive, Cooper Industries, Home Depot, Lowe's, Unocal and Wal-Mart and abstained on the rest. In 2001, it had abstained or voted against all sweatshop-related proposals. McCall's office told IRRC that the variations were the result of a "combination of factors, including the resolution, company performance, the response (or lack of one) to our 2001 letter sent to companies."

The state also sponsored a resolution asking ExxonMobil to adopt a non-discrimination policy that includes sexual orientation in its wording and voted for a proposal at Household International that asked the company to link executive pay to measures to prevent predatory lending. (The firm's alleged predatory lending practices were at issue in three class-action lawsuits pending against it at the time of its 2002 annual meeting.) Scott Klinger of Responsible Wealth, whose members co-filed the proposal at Household with Domini Social Investments, told IRRC last May that he credited McCall with helping to boost support for the proposal to 27 percent of the shares voted, up from just 5 percent at its first go-round in 2001. A week before the company's 2002 annual meeting, McCall said publicly that he might sell the fund's 2.5 million shares in Household if it didn't get to grips with its predatory lending problem.

It voted against proposals on drug pricing, but McCall sent letters to the recipients and five other drug firms in which the state had large holdings "to express my concern with the high price of pharmaceutical drugs and the growing public discontent with the industry's response to the issue." The state once again voted for the PCB clean-up resolution at GE, but abstained on all global warming and other environment-related proposals, keeping in step with its policy.

Despite its trend toward warming up to a number of types of social policy proposals in 2002, an article in the *Village Voice* last summer slammed McCall's proxy voting record. The *Voice* accused McCall of using "the power of the state's $112 billion pension fund to insulate major corporations from shareholder challenges on environmental, human rights and other issues, contradicting his own progressive history and casting a cloud over his gubernatorial ambitions." The *Voice* said its review of New York State's proxy voting history from 1993 through 2001 revealed "a chilling pattern of social indifference—justified by his office on the grounds of his fiduciary obligation to maximize gains for pension holders."

Contrasting McCall's approach to that of other state funds, the *Voice* noted that during the 1990s McCall voted against resolutions calling on companies to endorse the Ceres Principles 88 out of 95 times and, overall, voted against or abstained on 90 percent of shareholder proposals calling for greater environmental disclosure. Similarly, McCall abstained on 31 and voted against four out of 36 labor rights resolutions sponsored by New York City and members of the Interfaith Center. (The exception was a vote on Unocal, which had a pending lawsuit related to its operations in Burma.) His track record on tobacco was mixed, according to the *Voice*. (Readers should note that under McCall's watch, New York State sponsored a number of shareholder proposals calling on tobacco companies to take steps to stop selling to kids and end advertising targeted at underage smokers.)

In McCall's defense, his spokesman, Jeffrey Gordon, pointed to McCall's votes in favor of resolutions calling on General Electric to disclose how much it was spending on lobby-

ists to avoid responsibility for polluting the Hudson River with PCBs and for all resolutions asking companies to adopt the MacBride Principles. Gordon also noted that McCall had opened discussions with corporate executives on environmental issues instead of actively voting its proxies or sponsoring proposals, and that this tactic gave McCall greater access to top corporate executives and therefore the ability to negotiate with them.

Still, others also were critical of McCall's tenure as New York State Comptroller. Ceres executive director Robert Massie told the *Voice*, "We have been perplexed by the failure of the New York State Common Retirement System to support the Ceres principles, which are the most widely accepted, modest request from shareholders for disclosure and accountability on environmental issues." In addition, a 2001 Dow Jones news story quoted corporate governance expert Robert Monks as saying that McCall's state fund had "done virtually nothing," in comparison to New York City, California and other public pension fund systems.

## Changes Ahead?

Whether Hevesi will bring his past style of shareholder activism to his new post is still unclear. Repeated promises from Hevesi's staff to respond to questions on Hevesi's plans—if any—to revamp New York State's proxy voting guidelines or to sponsor shareholder proposals went unfulfilled for three months before IRRC published this article.

Whatever Hevesi decides on the state's proxy voting guidelines and on filing shareholder proposals, he has signaled that he intends to speak out on investor concerns. After only a few weeks in office, Hevesi wrote a letter to then SEC Chairman Harvey Pitt, denouncing SEC plans, reported in the *New York Times*, to dilute restrictions on accountants providing consulting work. "Watering down the rules does nothing to restore investor confidence," said Hevesi. "In fact, it reinforces investor perceptions that the system is not fair, keeping investors away from the markets." If the SEC passes ineffective rules, Hevesi told Pitt that he was planning to reach out "to other investors, large and small, to ensure that our interests are protected and that effective rules are instituted."

*—Peter DeSimone*

# U.S. Court Limits California Law on Slave Labor

On January 21, the U.S. Court of Appeals for the Ninth Circuit dismissed all Federal-court lawsuits filed under a California law allowing victims of forced or slave labor during the World War II era to sue companies that profited from their labor. While California courts had found that the law's central provision—an extension of the statute of limitations for forced labor claims—was a procedural matter of the sort that the U.S. Constitution allows states to control, the Federal court determined that the law amounted to the unConstitutional enactment of a foreign affairs policy by a state. This Federal decision was handed down six days after a state appellate court ruling allowing a case brought under the law to proceed in state courts. While an appeal of the Federal decision is likely, for the moment the Federal decision trumps the state decision.

## Background

The California law, enacted in 1999, passed during a time of heightened awareness of the profits that German, Swiss and other companies reaped inadvertently or deliberately from the Holocaust. In 1998, the Swiss government and Swiss industry entered into an agreement with the U.S. government and various Jewish groups (most notably the World Jewish Congress) providing restitution for unclaimed assets that had been deposited by people who had died in the Holocaust. In 1997 and 1998, California, Florida, New York and Washington state drafted legislation requiring insurance companies to publish information about unclaimed policies issued in Eastern Europe in the decades before World War II.

As part of this movement, activists began focusing on corporations that had used concentration camp inmates or forcibly displaced persons (largely Eastern Europeans but also including some Allied prisoners of war) as forced laborers. In some cases, the laborers were paid below market rate for their labor; in other cases corporations paid the Nazi government for the use of these laborers. The International Labor Organization includes in its definition of "forced labor" certain types of paid labor that a person performs under duress.

"California has a moral and public policy interest in assuring that its residents and citizens are given a reasonable opportunity to claim their entitlement to compensation for forced or slave labor," the law's drafters wrote in the original bill. The law limited claimants to those taken "to perform labor without pay ... by the Nazi regime, its allies and sympathizers," a category which included the Japanese, who had a massive forced-labor program in place before and during the Second World War.

In the summer of 2000, the German government and a coalition of German corporations reached a settlement with representatives of Nazi victims, providing compensation for damages including forced labor. (See *Corporate Social Issues Reporter,* April 2001 and November 2001.) This settlement meant that the primary beneficiaries of the California law were victims of the Japanese forced labor program, a group that included Chinese, Korean and Filipino civilians and Allied prisoners of war. Of the nearly 30 cases reviewed by the Federal court, only one had a victim of Nazi forced labor as its plaintiff.

## Legal Challenges

The Federal court decision stated that, by targeting victims of a specific conflict between the United States and other nations, California was effectively engaging in foreign policy. The Supreme Court "has long viewed the foreign affairs powers specified in the text of the Constitution as reflections of a generally applicable constitutional principle that power over foreign affairs is reserved to the Federal Government," the Ninth Circuit wrote, and recent Supreme Court decisions—most notably the decision invalidating Massachusetts' selective-purchasing law that penalized vendors doing business in Burma—have also shown this view. By allowing former U.S. prisoners of war to sue companies that profited from their labor, the court found that the California law contradicted the Treaty of San Francisco, which ended the Pacific war and stipulated that "the Allied Powers waive all reparations claims of the Allied Powers, other claims of the Allied Powers and their nationals arising out of any actions taken by Japan and its nationals."

While the language of the Treaty appears clear, some legal scholars (one of whom was recently confirmed as a judge in the Fourth Circuit) disagree with Federal court findings, and former POWs have called for an reversal of his ruling or new legislation that would permit claims against Japaneese companies. In the previous Congress, U.S. Representative Dana Rohrabacher (R-Calif.) introduced H.R. 1198, the "Justice for United States Prisoners of War Act," which would instruct federal courts not to interpret Article 14 of the Treaty as precluding claims by former U.S. POWs. (The bill would also allow states to extend the statute of limitations for such claims.) The bill, which had a total of 230 cosponsors, did not emerge from the Committee on the Judiciary's Subcommittee on Immigration and

Claims; however, veterans are frequently perceived in a positive light, and former POWs have argued that they are likely to die within the next 10 years, possibly inspiring prompt action on the part of Congress.

In its finding, the Ninth Circuit mentioned "some individual cases as to which federal jurisdiction may be uncertain," meaning that some former forced laborers may be able to sue companies in state courts that are more sympathetic to the law. While the finding does not mention which plaintiffs may be able to re-file in state court, the claims of Korean and Chinese former forced laborers who are residents of California would not interfere with U.S. foreign policy in the same way that the claims of former members of the U.S. military would. These groups of former forced laborers have also had some luck in obtaining judgments in Japanese courts. While the majority of lawsuits filed in Japan against companies that benefited from forced labor have been dismissed, in the past decade, five Japanese companies have made payments to former forced laborers in response to litigation in Japanese courts. While most of these payments were characterized as voluntary, in April 2002 a court ordered Mitsui Mining to pay approximately $85,000 in compensation to each of 15 plaintiffs—the first instance of a Japanese court ordering compensation to victims of forced labor. Japanese law is not as dependent on precedence as U.S. law is, so it is too soon to know whether this mandatory payment is an isolated incidence, or the beginning of a trend.

*—Jan Degges*

# U.S. Firms Make Fairness Gains in N. Ireland

Although employment in Northern Ireland at U.S. companies fell by almost 10 percent in 2002, the Catholic portion of these jobs grew slightly, in proportion with Catholics' 43 percent representation in the region's labor force. Moreover, the share of U.S. firms where either Catholics or Protestants appear to be under-represented fell to only about one-quarter, down from one-third in 2001; and at least three-quarters of these employers are taking affirmative action, most with successful results. In contrast, a large sample of non-U.S. firms employs Catholics at a lower rate than their representation in the Northern Ireland workforce. Furthermore, more than one-third of these firms appeared to under-represent either Protestants or Catholics, and about half of these companies have made no progress towards fairer representation in the last several years.

These are among the main findings of IRRC annual surveys in 2002 of the religious composition of the corporate work force in Northern Ireland. IRRC sent its survey to corporate officials of 137 U.S. privately and publicly held parent companies—with 158 separate subsidiaries or affiliates in the region—focusing in particular on the 82 public and private U.S. companies with more than 10 employees there. With funding from the California Public Employees' Retirement System, IRRC also surveyed for the second year in a row the non-U.S. Calpers portfolio companies with operations in Northern Ireland. Calpers owns shares in 77 of the 192 non-U.S. parent companies that have operations in Northern Ireland.

IRRC assessed the U.S. and non-U.S. companies' fair employment records based on their survey responses and on publicly available information. For survey respondents, IRRC examined the percentage of Protestants and Catholics in each job category against an appropriate recruitment area, with more highly skilled categories generally assumed to draw from a broader geographic area. If a company did not respond to the survey, IRRC made best efforts to determine a reasonable recruitment area for the company as a whole, using census data.

## U.S. Employment

At U.S. firms, employment at the end of 2002 dropped for the first time in years—falling to just under 20,000—after rising about 7 percent in 2001 and 15 percent in 2000, largely because of acquisitions, a phenomenon that was not repeated in 2002. Catholic representation edged up, though, to 43.4 percent, up from 42.1 percent in 2001.

Twenty-two U.S. companies that IRRC had identified as having Northern Ireland operations last year no longer have ties to the province. There were just six brand new companies to report at year-end, down from 30 in 2001, underscoring the point that 2002 was a year for U.S. firms to cut rather than establish ties to Northern Ireland. Contractions in 2002 at two big privately held U.S. employers—a chicken processor and an industrial plant—cut more than 750 jobs between them, and no sector was immune from cutbacks.

Sixty-five publicly held (and 17 privately held) U.S. companies have subsidiaries or affiliates that employ more than 10 workers in Northern Ireland. *(Detailed information on companies in Northern Ireland is available from IRRC's Northern Ireland Service.)*

**Religious composition:** There are now 10,273 Protestants and 7,873 Catholics at U.S.-associated firms (see table). This constitutes a net drop since last year of 473 jobs for Catholics and 1,189 jobs for Protestants, with Protestants losing jobs at twice the rate as Catholics. Increases in 2001 had

## Employees at U.S. Firms in Northern Ireland

| | *2000* | *2001* | *2002* |
|---|---|---|---|
| Protestant | 10,910 [57.6%] | 11,462 [57.9%] | 10,273 [56.6%] |
| Catholic | 8,024 [42.4%] | 8,346 [42.1%] | 7,873 [43.4%] |
| Other | 776 | 932 | 861 |
| No data* | 793 | 1,188 | 896 |
| Total | 20,503 | 21,928 | 19,903 |

Percentages given do not include employees classified as "other" or "undetermined."
*Includes 171 in 2000, 360 in 2001 and 310 in 2002 at firms with 0-9 Catholics or Protestants.

been roughly proportionate to each group's representation in 2000.

Catholic representation at all U.S. companies has risen after a drop in the mid-1990s. Employment shifts at existing U.S. Northern Ireland employers have produced Protestant job losses in numbers disproportionate to their former overall representation, while Catholics have gained newly created jobs in proportions greater than their former overall representation. In the high tech sector, where Catholics are well represented, major job additions in the last three years seem to have outweighed subtractions, although the full impact of high tech sector retrenchment has yet to show up completely in data reported to IRRC by U.S. companies in Northern Ireland.

Taken together, U.S. companies appear to reflect the working age population breakdown of Northern Ireland. Overall census figures released in late December 2002 show that the entire population of Northern Ireland in 2001 was 44 percent Catholic, lower than the expected 46 percent. The Equality Commission estimates, based on government surveys, that Catholics now make up 43 percent of the smaller group of economically active workers; this figure will be tested against the actual census figures when they are released in mid-2003. Catholics accounted for 39.3 percent of fulltime workers at private sector firms with more than 25 employees whose religion was identified in Equality Commission monitoring for 2001, the latest available data, up from 34.6 percent in 1990.

### Fair Employment Signs at U.S. Firms

IRRC identified companies that do not appear to achieve fair participation for Protestants or Catholics, then looked at three key indicators that provide a good sense of the fair employment record of U.S. firms as a whole in Northern Ireland:

- *affirmative action* efforts taken because Catholics or Protestants are under-represented in a firm's work force,
- the *impact* these efforts have had in moving firms towards fair representation where it is lacking, and
- the number and disposition of *discrimination complaints* filed at individual companies and at the entire universe of U.S. firms.

**Firms with underrepresentation:** At about one-quarter of the U.S. firms with more than 10 workers, Catholics or Protestants do not appear to achieve fair participation, despite affirmative action efforts. Catholics appear to be under-represented at 12 companies, and Protestants at nine. IRRC reached these conclusions after comparing each firm's work force to a customized recruitment area, using detailed local census data and taking a number of company-specific factors into account. Some conclusions about Protestant underrepresentation may be undermined by demographic change over the last decade.

Nearly all of the companies that currently appear to have an underrepresentation of Catholics seem to have made progress towards fair participation within the last five years. But there has been little change at three companies—**AES**, **DuPont** and **Crane**—where Catholics do not seem to be fairly represented; the work forces of each of these firms have been falling, giving the companies little opportunity to effect change.

Change towards fairer participation at firms with a low number of Protestants appears less prevalent in IRRC's sample of companies where several years of employee data are available for assessment. Just two of the companies that appear to have Protestant underrepresentation at present have made progress since 1998—**Openwave Systems** and **SMTEK International**, while the rest—**Analog Devices, Bemis**, CCC Network Systems (a private firm), **Interface, Solectron's** Stream International and **Terex**—have stayed about the same or seen a drop in Protestant proportions. The Protestant drops have occurred whether jobs were lost or gained overall.

**Affirmative action:** U.S. employers that are undertaking affirmative action are using a number of methods. Links with particular schools are most popular, but companies also are meeting with local community or church leaders. Some companies—**Baker Hughes** and **Crane**, among the companies that have resolutions on the issue—use ads that specifically encourage Protestants or Catholics to apply. **Sanmina-SCI** has bussed employees from specific areas, while

**3M** has sponsored Catholic sports teams. (3M is one of the firms that has reached an agreement to implement the MacBride principles.)

A few U.S. firms have addressed the issue of industrial location, long a sore point with equality advocates critical of government policy. Equality activists point out that most of Northern Ireland investment and industry tends to be in Protestant-dominated areas, making it more difficult for Catholics to achieve fair participation in the overall work force. The U.S. companies that are in predominantly Catholic areas, or those that have expanded into such areas, include in West Belfast a recent plant expansion from **Caterpillar's** F.G. Wilson and a facility run by **Analog Devices**. A U.S. firm in the rural and mostly Catholic hinterland where little other industry exists is Finlay Hydrascreens of Omagh, owned by **Terex**.

A handful of companies—**AVX**, **Caterpillar**, **Sanmina-SCI**, **KeySpan** and **Xerox**—are taking part in the British government's New Deal program that aims to move the long-term unemployed back to work. As Catholics remain disproportionately represented in that pool, the program and participation in it may have an effect on reducing the long-standing unemployment differential between Northern Ireland's two communities, but the program has many skeptics.

The operations of at least 14 U.S. companies have developed affirmative action plans with the assistance of the Equality Commission; of the firms receiving shareholder proposals, these include **Baker Hughes** and **Crane**, neither of which has a MacBride implementation agreement.

**Progress toward fair participation:** Many of the companies with formal affirmative action agreements are making solid progress towards their goals to achieve fairer work force participation; some are not. Among the companies where MacBride shareholder proposals are pending, the laggards include:

- **Bakers Hughes**, which has seen the proportion of Catholics at its Hughes Christensen plant drop recently and is still the most one-sided of all substantial U.S. employers, saw the Catholic share of the work force rise 4 points to nearly 10 percent in 2002; and
- **Crane**, whose Stockham Valve operation has hemorrhaged workers, has seen an already low proportion of Catholics drop to 12 percent or less.

**Discrimination complaints:** Since 1994, complainants lodged at least 193 formal discrimination grievances against the subsidiaries or affiliates of 43 of the U.S. companies with current operations in Northern Ireland. Throughout its history, though, the FET has formally determined discrimination has occurred at only three U.S. companies—**BE Aerospace**, **Visteon** (spun off from Ford Motor in 2000), and an affiliate of **General Electric**. But these firms and 10 others have settled a total of 30 cases with complainants, often but not always admitting in the process that discrimination had occurred and generally paying some form of compensation.

More cases were pending against U.S. firms at the Fair Employment Tribunal as of November 2002 than ever before—64 compared with 58 in October 2001 and 27 in 2000. Five or more cases are pending against subsidiaries of **Caterpillar**, OSI Industries (private) and Seagate Technologies (private), while subsidiaries or affiliates of **BE Aerospace**, **General Electric** and **Interface** each had four cases pending.

## Response to the U.S. Survey

The response rate to IRRC's survey went up a little in 2002, after dropping in the late 1990s. Sixty percent of the public and private U.S. companies with more than 10 employees in Northern Ireland responded in some fashion in 2002.

In the key group of 33 non-respondent firms that employ more than 10 people in Northern Ireland, 10 opened or acquired the Northern Ireland operation in the last three years, six have long-term operations and have never responded to the survey, six have responded fully at least once sometime in the past, and four promised to respond but did not. Sixteen of the 33 are privately held. In general, companies may not be responsive because of the newness of their operations, the lack of shareholder pressure on the issue, a corporate culture that is not disposed toward disclosure, or the relatively small size of the parent company. Smaller, less widely held companies generally have provided less information over the years, although there are notable exceptions. These firms also have been many of the recent entrants to Northern Ireland, particularly in the high-tech sector that was booming until recently.

Ten companies with more than 10 employees have been added to IRRC's list of companies in Northern Ireland in the last three years and have provided no substantive response to the survey; four of these are private. Eleven firms with long-term operations employing more than 10 workers have never responded, including publicly traded **BE Aerospace**, **Crane**, **Sanmina-SCI**, **Segue Software** and **Valence Technology**. Other public firms that did not reply in 2002 and had more than 100 employees in Northern Ireland were **Berkshire Hathaway**, **General Electric**, **Openwave Systems** and **TJX**.

## Non-U.S. Companies

Catholics again appear to be better represented at publicly traded U.S. firms in Northern Ireland than at the non-U.S. publicly traded firms IRRC surveyed for Calpers. These companies, which represent 105 employers in Northern Ireland, employ almost 36,000 people in the province, nearly 38 percent of whom are Catholics. The difference between U.S. companies and the non-U.S. firms sampled was less

## Old News on U.S. Companies Appears in Iraqi Declaration

The 12,000-page weapons program account that the Iraqi government submitted to the United Nations in December included the names of 78 companies that Iraq said had provided it with necessary materials for its chemical, biological and nuclear weapons programs. While the names of these companies were redacted from all copies of the report provided to the press and nations that are not members of the U.N. Security Council, the German newspaper *Die Tageszeitung* obtained an unredacted leaked copy. That list was reprinted by www.thememoryhole.org, a website that "exists to preserve and spread material that is in danger of being lost, is hard to find, or is not widely known," according to the site. "The emphasis is on material that exposes things that we're not supposed to know (or that we're supposed to forget)."

The U.S. government has charged Iraq with having recycled large portions of the U.N. declaration from earlier reports, and it happens that 15 of the 24 U.S.-based companies on the *Tageszeitung* list are also on a list of companies that made U.S.-approved exports to Iraq's atomic weapons program between 1985 and 1990. The list, compiled by Gary Milhollin and Diana Edensword of the Wisconsin Project on Nuclear Arms Control and released in 1992, was based on U.S. Department of Commerce export licensing records. IRRC found no recent evidence of the existence of two U.S. companies on the *Tageszeitung* list. The most recent information regarding Semetex, one of these two companies, is from 1991, and the most recent information regarding Alcola is from 1989.

The list also names the "US Ministries of Defense, Energy, Trade and Agriculture" and the Lawrence Livermore, Los Alamos and Sandia National Laboratories among other U.S. entities that supplied Iraq's weapons programs.

A predecessor company to one of the U.S. companies on the list, Hewlett-Packard, was recently fined by the U.S. Department of Commerce for the illegal transfer of sensitive technology. At least 10 times, Hewlett-Packard precursor Digital Equipment Corp. illegally exported controlled computer items to South Korea or allowed their illegal re-export from Hong Kong to China and from Singapore to India. The Department of Commerce has made no allegations regarding any exports by Hewlett-Packard to Iraq. In October, Hewlett-Packard paid a $39,000 civil penalty.

substantial, though, than in 2001, when Catholics accounted for only 34 percent of the work force of the non-U.S. firms examined. Full comparisons are not possible, however, given the somewhat different composition of each year's sample. Catholics or Protestants appear to be clearly under-represented at one-quarter of the employers examined.

IRRC received complete or partial responses from 33 of the parent companies surveyed, with companies reporting on the number of their employees by religion and job category. Forty-one of the parents surveyed provided minimal or no responses.

- Catholics or Protestants did not appear to be fairly represented at 26 of the 105 employers examined; Catholics appeared to be clearly under-represented at 17 companies and Protestants at nine. Possible underrepresentation appeared to exist at another 28 employers. Among the companies clearly lacking in fair participation at present, there has been change in work force composition in the last several years at about half of the firms, out of the group of 17 companies where sufficient data were available to examine long-term trends. Little or no change toward more equal representation occurred for the other half.
- Companies that responded to the survey reported using a full range of affirmative action measures prescribed by Northern Ireland's fair employment law, including the use of goals and timetables.
- IRRC found that non-U.S. companies and U.S. firms have lost discrimination cases filed against them at the Fair Employment Tribunal in Belfast in similar small proportions. But compared to U.S. firms, the non-U.S. companies examined were less likely to settle cases, less likely to have cases dismissed, and more likely to have cases lodged against them resolved rapidly.

Sixteen of the non-U.S. companies in the Calpers' portfolio in 2002 meet the conditions U.S. firms achieve to reach agreements on MacBride implementation. These firms indicated their policies currently reflect the standards of the MacBride code and said they would cooperate with independent IRRC monitoring of their fair employment practices. Several others indicated their policies were consistent with the MacBride principles, but were unwilling to submit to regular monitoring.

*—Heidi Welsh*

(continued on p. 24)