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## NOTES

# MERGING WITHOUT PURGING: INCENTIVIZING BOARDS OF DIRECTORS TO PROMOTE DIVERSITY THROUGH M & A

HAYLEY BUCKRIDGE<sup>1</sup>

*“Standards are nothing more than structured preferences . . . [a]s a society, we have yet to look carefully beneath them to see where the seeds of prejudice are truly hidden.”<sup>2</sup>*

### INTRODUCTION

Since the last wave of corporate accounting scandals, Americans have embraced the idea of holding directors and

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<sup>2</sup> PATRICIA WILLIAMS, *THE ALCHEMY OF RACE AND RIGHTS* 103 (Presidents and Fellows of Harvard College ed., 1991).

executives accountable for their wrongdoings.<sup>3</sup> The federal government, the Securities and Exchange Commission, and the National Association of Securities Dealers have all adopted corporate governance reforms addressing corporate structure, accounting, auditing, fraud, liability, and reporting.<sup>4</sup> In addition,

<sup>3</sup> Corporate scandals have occurred with frequency throughout the history of American business, from Charles Ponzi's famous "pyramid scheme" in the 1920's to the junk bond controversies of the mid-1980's involving Dennis B. Levine, Ivan Boesky and Michael Milken. See Stephany Watson, *Fostering Positive Corporate Culture in the Post-Enron Era*, 6 TRANSACTIONS 7, 10–15 (2004). While corporate scandals are not new, they have currently received increased media attention due to broadened modern means of communication. See *id.* at 7. Disclosures at companies such as WorldCom have promoted increased scrutiny and have quickened the pace of change. See Andrew M. Fields & Phyllis Y. Keys, *The Emergence of Corporate Governance from Wall St. to Main St.: Outside Directors, Board Diversity, Earnings Management, and Managerial Incentives to Bear Risk*, FIN. REV., Feb. 1, 2003, at 1.

<sup>4</sup> Traditionally, boards of directors have consisted of both inside directors, directors who also act as officers of the corporation, and outside directors, directors not employed by the corporation in any other capacity. See Lynne L. Dallas, *The Multiple Roles of Corporate Boards of Directors*, 40 SAN DIEGO L. REV. 781, 782 (2003). So long as the directors were appropriately elected by shareholders, the corporate law provided no criteria for director eligibility. See *id.* However, the series of corporate admissions of fraud and accounting improprieties in 2002 sparked major corporate governance reforms. See Watson, *supra* note 3, at 25. After the accounting scandals struck, the public lost confidence in the stock market. *Id.* Corporate governance became a hot conversational topic and investors sought safer harbors in which to invest their money. See *id.* at 31. Thus, many of the corporate governance reforms sought to increase trust by revamping corporate boards of directors and encouraging stricter manager monitoring and accurate financial reporting. Notably, the reforms were driven by a desire to facilitate the full and fair disclosure of corporate finances. See *id.* at 32.

In 2002, The New York Stock Exchange adopted new rules that required more than one-half of the board of directors to be independent and that membership on auditing, nominating, and compensation committees be entirely composed of outside directors. See Theresa A. Gabaldon, *The Story of Pinocchio: Now I'm A Real Boy*, 45 B.C. L. REV. 829, 830 (2004).

Congress promoted the restructuring of corporate boards when it enacted the Public Company Accounting Reform and Investor Protection Act of 2002 ("Sarbanes-Oxley"), the "most expansive federal corporate governance legislation since the Great Depression." See Watson, *supra* note 3, at 25. The Act requires the national securities exchanges and NASDAQ to adopt corporate governance listing standards under which listed companies are required to create an audit committee comprised solely of independent directors. The auditing committees have the responsibility of hiring and firing auditors. See *id.* at 26–31. Before Sarbanes-Oxley, management was the auditor's client. After Sarbanes-Oxley, the auditing committee takes over this role; it evaluates and selects an auditor and takes full responsibility for making critical decisions about a firm's accounting policy. See *id.* at 26–27. Sarbanes-Oxley also requires 'rolling disclosures' of material changes in a public company's financial condition or operation. *Id.* In its effect, this Act will prevent public companies from participating in corporate restructuring, refinancing, mergers, and other important business activities under the radar. See *id.* at 26. Since September, 2003, the National Association of Securities Dealers ("NASD") requires all companies listed on the NASDAQ to have a publicly available code of conduct for all directors and employees. The NASD also puts forth heightened criteria for independent directors, auditors and nominating committees that exceed both the requirements of Sarbanes-Oxley and the NYSE. See *id.* at 30. In 2003, the NYSE submitted a corporate governance rule filing to the SEC which would require all companies listed on the NYSE to meet specific corporate

most Fortune 500 companies have established codes of conduct to ensure compliance with these newly evolving legal requirements.<sup>5</sup> Currently, while the frenzy over corporate balance sheets has died down, a less publicized but equally important issue has re-surfaced – employment discrimination based on race and gender.<sup>6</sup>

Over forty years have passed since Title VII of the Civil Rights Act of 1964 was enacted;<sup>7</sup> yet, sex and race discrimination still pervade corporate America.<sup>8</sup> Recently, in May of 2004, Boeing settled a sex discrimination lawsuit for \$72.5 million.<sup>9</sup> Only two months later, Morgan Stanley paid the Equal Employment Opportunity Commission \$54 million to settle a similar class action.<sup>10</sup> This Note suggests that corporations can decrease their

governance standards including a code of business conduct and ethics for directors, officers, and employees to foster a culture of honesty and accountability. *See id.* at 30.

<sup>5</sup> *See* Watson, *supra* note 3, at 8 (defining corporate compliance programs and reasons for establishing such programs). *See generally* Amy Borrus & Paula Dwyer, *The SEC's Top Cop*, BUSINESS WEEK, June 21, 2004, at 116 (noting various attempts at reform by SEC).

<sup>6</sup> *See* Roger Clegg, *Whistling Fairness*, NAT. REV., June 16, 2005, <http://www.nationalreview.com/clegg/clegg200506160744.asp> (advising employees to challenge employers regarding illegal preferences); *see also* Nancy R. Mandell, *\$29 Million Award to UBS Exec for Sex Discrimination is Not Enough, Says Women's Rights Advocate*, SECURITIES WEEK, Apr. 11, 2005, at 10 (discussing presence of gender discrimination on Wall Street).

<sup>7</sup> 42 U.S.C. § 2000e-2(a)(1) (2005). Title VII provides:

It shall be an unlawful employment practice for an employer . . . to fail or refuse to hire or to discharge any individual, or otherwise to discriminate against any individual with respect to his compensation, terms, conditions, or privileges of employment, because of such individual's race, color, religion, sex or national origin[.]

*Id.*

<sup>8</sup> *See* Cheryl Wade, *The Impact of U.S. Corporate Policy on Women and People of Color*, 7 J. GENDER RACE & JUST. 213, 223 (2003) (highlighting recent increase in discrimination complaints filed with EEOC); *see also* Susan Meisinger, *HR must lead the fight for employment equity*, HR MAGAZINE, Mar. 1, 2005, at 12 (stating that women in the same employment positions as men are still paid less).

<sup>9</sup> *See* Richard W. Black and Christopher P. Reynolds, *The Increasing Risk of Legal Challenges to an Employer's Compensation Policies and Practices: Considerations for Compensation Self-assessment*, J. INVESTMENT COMPLIANCE, March 22, 2005, at 55 (noting that plaintiffs alleged “discrimination in pay, promotions, overtime, assignments, bonuses, and other conditions of employment”); Betsy Morris et al., *How Corporate America is Betraying Women*, FORTUNE, Jan. 10, 2005, at 64 (stating suit alleged that at Boeing, women were not promoted as quickly as men).

<sup>10</sup> *See* Susan Antilla, *Money Talks, Women Don't*, N.Y. TIMES, July 21, 2004, at A19. Adding to the list of major corporations, Publix Supermarkets paid \$81.5 million in 1997 and Home Depot paid at least \$104 million in 1998 to settle sexual harassment or sex discrimination claims. *See* Wade, *supra* note 8, at 224. While the most recent cases happen to involve sex discrimination, many race discrimination lawsuits have also resulted in multi-million dollar settlements over the past decade. Coca-Cola paid out \$192.5 million to plaintiffs to resolve a racial discrimination dispute in 2000. *See id.* In 1996, Texaco settled a racial discrimination suit for \$176 million. *See id.*

risk of being held liable for employment discrimination by effectively diversifying and integrating their workforces and developing workable diversity programs. However, effective workplace diversification is particularly difficult today as American businesses are entering into mergers and acquisitions with increased frequency to compete with large global markets.<sup>11</sup> Accordingly, this Note asserts that, more often than not, boards of directors will fail to consider diversity issues before approving mergers due to the lack of legal incentives provided by current federal and state corporate law.

Post-Enron, directors were motivated by newly enacted corporate governance reforms to take control of accounting frauds.<sup>12</sup> It is suggested that corporate governance reforms are now also necessary to encourage directors to seriously consider human issues, specifically diversity, before recommending a merger for shareholder approval. It is put forth that such reforms will encourage directors to utilize intense pre-merger deliberations and merger negotiations to make stronger commitments to diversity and establish effective diversification and integration programs.

This Note will explain how a corporation's commitment to diversity will not only facilitate a more fair and productive workforce, but will result in an overall more competitive and profitable organization. Furthermore, this Note will discuss how an effective diversification program will prevent costly and stigmatizing employment discrimination litigation,<sup>13</sup> ensure

<sup>11</sup> See Shawn Tully, *The Urge to Merge*, FORTUNE, Feb. 21, 2005, at 21 (noting the newly launched "merger wave" saw U.S. companies announce 48 deals of \$1 billion or more from Nov. 2004 through Jan. 2005). See generally Yuki Noguchi & Griff Witte, *Cingular Wins the Bidding; Firm Beats Out Vodafone With \$41 Billion Offer for AT&T Wireless*, THE WASHINGTON POST, Feb. 18, 2004, at E01 (describing merger which created largest cell phone company in United States).

<sup>12</sup> See *Where's All the Fun Gone?*, THE ECONOMIST, Mar. 20, 2004 (noting that directors have become more serious about their duties in the post-Enron era); see also Joan Harrison, *Pitching Deals to Increasingly Skeptical Boards*, MERGERS & ACQUISITIONS, Aug. 9, 2005 (stating that directors have become more involved in deals in the post-Enron era).

<sup>13</sup> See Wade, *supra* note 8, at 225 (proposing that increase of litigation is due to increased willingness of employees and shareholder activists to litigate discrimination issues); see also Morris et al., *supra* note 9, at 65-72 (noting that companies are vulnerable to sex-discrimination lawsuits and advising companies to adopt consistent procedures and established guidelines for employee advancement in order to prevent overbearing litigation).

compliance with applicable laws, and maximize shareholder wealth.<sup>14</sup>

## I. THE BOARD'S ROLE IN MERGERS AND ACQUISITIONS

Corporate governance analysis typically begins with the board of directors.<sup>15</sup> As corporations have become larger and more complex, the demands on corporate boards have changed.<sup>16</sup> Deciding whether to enter into a merger or acquisition ("M&A") is one of the most important choices a corporation makes.<sup>17</sup> As is the case with most significant corporate events, the board of directors plays a crucial role in making this choice.<sup>18</sup>

In the M&A context, directors have several legal obligations. First, state corporate law usually requires board recommendation before mergers or sales of assets can be considered by shareholders.<sup>19</sup> Shareholders are given the

<sup>14</sup> See Steven Ramirez, *A General Theory of Cultural Diversity*, 7 MICH. J. RACE & L. 33, 36–38 (2001) (theorizing that culturally diverse workforces result in wide spectrum of insights, increased creativity, and heightened productivity which economically benefit companies); see also Steven Ramirez, *Diversity and the Boardroom*, 6 STAN. J.L. BUS. & FIN. 85, 86, 97–99 (2000) (citing empirical studies showing that companies that promote diversity management have competitive advantage).

<sup>15</sup> See Eric Helland and Michael Skyuta, *Regulation and the Evolution of Corporate Boards: Monitoring, Advising, or Window Dressing?*, 47 J. L. & ECON. 167, 167 (2004) (stating that "[t]he basic unit of analysis in corporate governance is the board of directors"); see Brian Allen Warwick, *Reinventing the Wheel: Firestone and the Role of Ethics in the Corporation*, 54 ALA. L. REV. 1455, 1455 (2003) (explaining that board of directors is responsible for managing all aspects of corporation).

<sup>16</sup> See Dallas, *supra* note 4, at 782 (noting modern corporations "require more complex organizational structures, such as departments and divisions, a more diverse workforce possessing various levels and areas of expertise, and a more formalized accountability system"). See generally J. Cunyon Gordon, *Painting by Numbers: "And, Um, Let's Have a Black Lawyer Sit at Our Table"*, 71 FORDHAM L. REV. 1257, 1296 (2003) (describing argument that there is economic need for diverse workforce in modern American business world).

<sup>17</sup> See Jonathan Choslovsky, Note & Comment, *Agency Review of Health Care Industry Mergers: Proper Procedure or Unnecessary Burden?*, 10 ADMIN. L.J. AM. U. 291, 298 (1996) (stating that mergers are important sources of economic activity for corporations); see also DENNIS C. CAREY AND DAYTON OGDEN, *THE HUMAN SIDE OF M&A: HOW CEOs LEVERAGE THE MOST IMPORTANT ASSET IN DEAL MAKING* 158 (Oxford UP 2003) (stating that mergers are enduring strategy for corporations).

<sup>18</sup> See *TW Services, Inc. v. SWT Acquisition Corp.*, 1989 Del. Ch. LEXIS 19, at \*35 n.19 (Del. Ch. March 2, 1989) (stating corporate law gives board of directors critical role in mergers); see also CAREY & OGDEN, *supra* note 17, at 160 (explaining that "human talent and leadership" distinguish successful mergers from unsuccessful mergers).

<sup>19</sup> See John H. Matheson and Brent A. Olson, *Shareholder Rights and Legislative Wrongs: Toward Balanced Takeover Legislation*, 59 GEO. WASH. L. REV. 1425, 1434 (1991) (explaining that "[s]ignificant corporate transactions, such as mergers or sales of assets, typically require board recommendation before they are considered by the shareholders"); see also Kimble Charles Cannon, *Augmenting the Duties of Directors to Protect Minority Shareholders In the Context of Going-Private Transactions*, 2003 COLUM. BUS. L. REV.

advantage of not having to make this important decision until after the board has decided whether it is in their best interest.<sup>20</sup> In addition, directors have broad authority to terminate a merger agreement without seeking shareholder approval.<sup>21</sup>

Second, directors owe fiduciary duties to the corporation's shareholders.<sup>22</sup> This Note focuses on the director's fiduciary duty of care which includes both an obligation to undertake a rational decision-making process before recommending the merger to shareholders and a duty to monitor the goings-on at the corporation throughout the merger process so as to ensure compliance with applicable legal requirements.<sup>23</sup> Third, pursuant to federal securities laws, directors must disclose material information to shareholders regarding the merger transaction when submitting the merger for shareholder approval.<sup>24</sup>

191, 196 (2003) (explaining how Delaware law distinguishes between directorial duties in a merger context as opposed to a tender offer context). *See generally* In Re: Siliconix Inc., 2001 Del. Ch. LEXIS 83, at \*35 (Del. Ch. June 19, 2001) (discussing how board of directors of Siliconix made recommendation to shareholders).

<sup>20</sup> Usually, after board approval, a majority of target shareholders must then approve the merger. *See* Matheson & Olson, *supra* note 19, at 1434. In this respect, the board of directors acts as a "gatekeeper." *See* Wayne O. Hanewicz, *When Silence is Golden: Why the Business Judgment Rule Should Apply to No-Shops in Stock-for-Stock Merger Agreements*, 28 IOWA J. CORP. L. 205, 216 (2003).

<sup>21</sup> *See* Matheson & Olson, *supra* note 19, at 1434 (stating that board of directors has "ability to short-circuit fundamental changes, or, from a different perspective, [protect] the shareholders from the burdens of important decisions until their duly elected representatives have carefully considered the matter and have decided such a change is in the best interests of the corporation and its shareholders"); *see also* Hanewicz, *supra* note 20, at 238 (explaining that board of directors has broad power to unilaterally terminate a merger without shareholder approval).

<sup>22</sup> *See* Matheson & Olson, *supra* note 19, at 1455-56 (stating that directors owe fiduciary duty to shareholders to act in their best interests); *see also* Mark J. Loewenstein, *The SEC and the Future of Corporate Governance*, 45 ALA. L. REV. 783, 788 (1994) (stating that state law relies on principle that directors are fiduciaries who can be held liable to shareholders for failing to perform their fiduciary duties).

<sup>23</sup> *See* Francis v. United Jersey Bank, 432 A.2d 814, 822 (N.J. 1981) (stating that directors must monitor corporate affairs and policies); *see also* In Re Caremark Int'l. Derivative Litig., 698 A.2d 959, 970 (Del. Ch. 1996) (suggesting, in aspirational settlement opinion, that board of directors should create information and reporting system to ensure compliance with applicable legal standards). *See generally* Matheson & Olson, *supra* note 19, at 1460 (stating that "directors must act in accordance with their fundamental duties of care and loyalty").

<sup>24</sup> *See* Arthur R. Pinto, *Corporate Governance: Monitoring the Board of Directors in American Corporations*, 46 AM. J. COMP. L. 317, 334 (1998) (detailing breadth of corporate disclosure requirements); *see also* J. Robert Brown, Jr., *Corporate Secrecy, the Federal Securities Laws, and the Disclosure of Ongoing Negotiations*, 36 CATH. U. L. REV. 93, 103-06 (1986) (listing SEC-imposed disclosure requirements).

Lastly, in the context of takeovers, directors owe additional fiduciary duties.<sup>25</sup> Directors are obligated to protect the corporation and may launch takeover defense mechanisms; however, they must be able to prove that such defensive measures are the products of rational decision making processes and are proportional to the threats posed by the hostile bidder.<sup>26</sup> Further, when it is evident that takeovers will inevitably result in the sale and breakup of the corporation, the board is legally mandated to seek out the deal that will yield shareholders the most financial gain.<sup>27</sup>

#### A. *The Fiduciary Duty of Care*

The traditional purpose of the board of directors is to ensure that corporate decisions benefit shareholder interests and monitor managers in accordance with this goal.<sup>28</sup> Based on this purpose, directors owe fiduciary duties to the corporation's shareholders. These fiduciary duties include the duty of care,<sup>29</sup>

<sup>25</sup> See *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 181 (Del. 1985) (holding that, when confronted with imminent takeover, board is held to duties articulated in *Unocal*, specifically "duty to determine the best interests of the corporation and its stockholders, and impose an enhanced duty to abjure any action that is motivated by considerations other than a good faith concern for such interests"); see also *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 48–49 (Del. 1994) (explaining how once "the Paramount directors . . . decided to sell control, they had an obligation to search for the best value reasonably available to stockholders"). See generally *Paramount Communications, Inc. v. Time, Inc.*, 571 A.2d 1140, 1153 (Del. 1989) (discussing how, when evaluating a threat posed by a takeover bid, directors may consider "inadequacy of the price offered, nature and timing of the offer, questions of illegality, the impact on 'constituencies' other than shareholders, the risk of nonconsummation and the quality of securities being offered in the exchange").

<sup>26</sup> See *Unocal Corp. v. Mesa Petroleum Corp.*, 493 A.2d 946, 955 (Del. 1985) (positing that "[i]f a defensive measure is to come within the ambit of the business judgment rule, it must be reasonable in relation to the threat posed"); see also *Revlon*, 506 A.2d at 179 (holding that, "[t]he ultimate responsibility for managing the business and affairs of a corporation falls on its board of directors").

<sup>27</sup> See *Revlon*, 506 A.2d at 184 (holding that when takeover is inevitable, board must allow market forces to operate freely to ensure that shareholders will receive best price available for their equity); see also *Unocal*, 493 A.2d at 955 (Del. 1985) (explaining how director's duty, while extended to interests of shareholders, is not absolute).

<sup>28</sup> See *Revlon*, 506 A.2d at 182 (holding that board directors cannot abandon their duties of loyalty to shareholders); see also *Unocal*, 493 A.2d at 956 (discussing importance of protecting shareholders).

<sup>29</sup> See *Smith v. Van Gorkom*, 488 A.2d 858, 874 (Del. 1985) (discussing how director did not meet his requisite duty of care); see also *Caremark*, 698 A.2d at 970 (holding that directors owe obligation to make good faith attempt to assure that corporation information and reporting system exists).



duty of loyalty,<sup>30</sup> and duty of good faith.<sup>31</sup> This Note focuses on the director's duty of care.

Directors owe a fiduciary duty of care to the corporation and its shareholders.<sup>32</sup> In general, the duty of care requires a director to exercise "that degree of diligence, care, and skill which ordinarily prudent men would exercise under similar circumstances in like positions."<sup>33</sup> With respect to mergers and acquisitions, the board members must "act in an informed and deliberate manner in determining whether to approve an agreement of merger before submitting it to shareholders."<sup>34</sup> The duty of care is essentially a procedural obligation. In most cases, absent any showing of improper procedure in the decision-making process, the board's decision is protected by the business judgment rule.<sup>35</sup>

<sup>30</sup> See *Revlon*, 506 A.2d at 179 (discussing how directors, in discharging ultimate responsibility for managing business affairs owe fiduciary duty of loyalty to corporation and its shareholders); see also *Bayer v. Beran*, 49 N.Y.S.2d 2, 3 (N.Y. Sup. Ct. 1944) (positing that directors are fiduciaries who owe a duty of loyalty to the shareholders).

<sup>31</sup> See *Emerald Partners v. Berlin*, 787 A.2d 85, 90 (Del. 2001) (stating that "[t]he directors of Delaware corporations have a triad of primary fiduciary duties: due care, loyalty, and good faith"). See generally *Malone v. Brincat*, 722 A.2d 5, 12 (Del. 1998) (noting that the Court sought to "provide the directors with clear signal beacons and brightly lined-channel markers as they navigate with due care, good faith, and loyalty on behalf of a Delaware corporation and its shareholders").

<sup>32</sup> See *Brehm v. Eisner*, 746 A.2d 244, 256 (Del. 2000) (commenting that good corporate governance include compliance with fiduciary duties established by law); *Jernberg v. Mann*, 358 F.3d 131, 135–36 (1st Cir. 2004) (noting a director owes a fiduciary duty of fair dealing in respect to corporate actions).

<sup>33</sup> *Francis v. United Jersey Bank*, 432 A.2d 814, 821 (N.J. 1981) (noting nature and extent of duties depend on type of corporation, and size).

<sup>34</sup> In particular, General Corporation Law, 8 DEL. CODE ANN. § 251(b) (2005), states in pertinent part:

(b) The board of directors of each corporation, which desires to merge or consolidate, shall adopt a resolution approving an agreement of merger or consolidation. The agreement shall state: (1) the terms and conditions of the merger or consolidation; (2) the mode of carrying the same into effect; (3) such amendments or changes in the certificate of incorporation of the surviving corporation as are desired to be effected by the merger or consolidation, or, if no such amendments or changes are desired, a statement that the certificate of incorporation of one of the constituent corporations shall be the certificate of incorporation of the surviving or resulting corporation; (4) the manner of converting the shares of each of the constituent corporations . . . and (5) such other details or provisions as are deemed desirable . . . . The agreement so adopted shall be executed in accordance with section 103 of this title. Any of the terms of the agreement of merger or consolidation may be made dependent upon facts ascertainable outside of such agreement, provided that the manner in which such facts shall operate upon the terms of the agreement is clearly and expressly set forth in the agreement of merger or consolidation.

*Id.* (emphasis added). Additionally, a director may not relinquish such duty by allowing the shareholders to decide. See *Van Gorkom*, 488 A.2d 858 at 874.

<sup>35</sup> See *Smith v. Van Gorkom*, 488 A.2d 858, 872 (Del. 1985) (highlighting that "[t]he business judgment rule exists to protect and promote the full and free exercise of the managerial power granted to Delaware directors"); see also *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 181 (Del. 1985) (noting that, under business

There are two corporate governance philosophies underlying the director's duty of care. First, the duty of care is built upon the "judicial view of rational decision-making".<sup>36</sup> Under the judicial view of rational decision-making, courts give considerable deference to the presumed rationality of board decisions based on the theory that judges are not adequately competent to question or criticize the generally complex substantive business decisions made by directors.<sup>37</sup> Thus, so long as directors employ a systematic and thorough decision making process, courts will trust that their decisions are rational.<sup>38</sup> Generally, courts intrude upon a board's substantive decision only when it appears that directors might follow their own financial self-interest at the expense of the corporation or its shareholders.<sup>39</sup> This intervention is justified, according to courts, because the directors' actions are inconsistent with the shareholder primacy model.<sup>40</sup>

The shareholder primacy model is an additional theory upon which directors' fiduciary duties are based.<sup>41</sup> This model of corporate law defines maximizing shareholder wealth as the

judgment rule, "there is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company").

<sup>36</sup> See James A. Fanto, *Quasi-Rationality in Action: A Study of Psychological Factors in Merger Decision-Making*, 62 OHIO ST. L.J. 1333, 1386 (2001).

<sup>37</sup> See *Revlon*, 506 A.2d at 181 (noting presumption that directors acted in best interest of company); see also *Van Gorkom*, 488 A.2d at 872 (discussing importance of preserving directors' managerial powers).

<sup>38</sup> See Fanto, *supra* note 36, at 1386 (highlighting that judges understand complexities of business decisions); see also *Harbor Finance Partners v. Huizenga*, 751 A.2d 879, 901 (Del. 1999) (finding that "[i]t seems presumptuous and paternalistic to assume that the court knows better in a particular instance than a fully informed corporate electorate with real money riding on the corporation's performance").

<sup>39</sup> See *Kamin v. American Express Co.*, 383 N.Y.S.2d 807, 812 (Sup. Ct. 1976) (noting court will not interfere with boards' decision unless a case of fraud, oppression, arbitrary action, or breach of trust is made out), *aff'd*, 387 N.Y.S.2d 993 (App. Div. 1976); see also Fanto, *supra* note 36, at 1382 (stating that in mergers board behavior is instrumentally rational).

<sup>40</sup> See *Dodge v. Ford Motor Co.*, 170 N.W. 668, 684 (Mich. 1919) (stating that corporations exist for "the profit of the stockholders"); Johnathan D. Springer, *Corporate Law Corporate Constituency Statutes: Hollow Hopes and False Fears*, 1999 ANN. SURV. AM. L. 85, 87 (1999) (noting that shareholder primacy model has usually prevailed in litigation).

<sup>41</sup> See *Gabaldon*, *supra* note 4, at 835-37 (noting managers are agents of shareholders and that shareholder primacy model is based on conclusion that "the interests of shareholders are preferred over those of others with interests in the firm"). See generally Lyman P.Q. Johnson & David Millon, *Recalling Why Corporate Officers are Fiduciaries*, 46 WM. & MARY L. REV. 1597, 1643 (2005) (stating that "the board should attend first and foremost to interests of shareholders").

director's primary function.<sup>42</sup> Under the shareholder primacy model, directors must act in the best interests of shareholders. Thus, so long as directors make decisions in accordance with this profit maximization goal, they satisfy their duty of care.<sup>43</sup>

Under the shareholder primacy model, directors are under no legal obligation to consider the interests of any other stakeholders in the corporation, including employees, suppliers, or members of the community.<sup>44</sup> Under state corporate law, directors are generally not held liable for decisions that negatively impact non-shareholder constituencies.<sup>45</sup>

### 1. The Duty of Care: Grossly-Negligent Decision Making

Directors can breach their duty of care in two ways: 1) through grossly negligent decision making<sup>46</sup> or 2) by failing to monitor compliance with legal obligations.<sup>47</sup> A director makes a grossly negligent decision when she fails to reasonably investigate and duly deliberate before making a decision.<sup>48</sup> Due deliberation is not specifically defined in the pertinent case law; however, in the merger and acquisition context, directors must inform themselves about the merger and make a rational business

<sup>42</sup> See *Kamin*, 383 N.Y.S.2d at 812 (finding that “[a]ll directors have an obligation, using sound business judgment, to maximize income for the benefit of all persons having a stake in the welfare of the corporate entity . . .”); see also *Gabalton*, *supra* note 4, at 835–36 (noting shareholders’ interest is preferred above all others).

<sup>43</sup> See *Gabalton*, *supra* note 4, at 835–37 (noting directors are responsible for maximizing value for shareholders). See generally *Johnson & Millon*, *supra* note 41, at 1647–49 (noting strong need for fiduciary duty to supplement need to monitor agents).

<sup>44</sup> See *Johnson & Millon*, *supra* note 41, at 1643–45 (stating whenever a conflict between interests of shareholders and non-shareholders arise directors should only consider shareholders’ interests). See generally *Gabalton*, *supra* note 4, at 836–37 (noting only those that have interaction with corporation are stakeholders).

<sup>45</sup> See *Johnson & Millon*, *supra* note 41, at 1643 (positing that recent doctrinal developments suggesting that directors should, at least, be permitted to consider the well being of non-shareholders). See generally *Gabalton*, *supra* note 4, at 1643–1645 (noting that “[i]t is easy to understand . . . why little attention needs to be devoted to external law” in light of the fact that “those who have no interaction with a corporation or its products are likely to be regarded as non-stakeholders”).

<sup>46</sup> See *Kamin v. American Express Co.*, 383 N.Y.S.2d 807, 811 (Sup. Ct. 1976), *aff’d*, 387 N.Y.S.2d 993 (App. Div. 1976) (stating directors are not chargeable with ordinary negligence); see also *Smith v. Van Gorkom*, 488 A.2d 858, 873 (Del. 1985) (confirming gross negligence is proper standard for determining fault).

<sup>47</sup> See *Francis v. United Jersey Bank*, 432 A.2d 814, 822–23 (N.J. 1981) (charging directors with duty to keep informed); see also *In Re: Caremark Int’l. Derivative Litig.*, 698 A.2d 959, 967 (Del. Ch. 1996) (stating breach of duty may arise in two ways).

<sup>48</sup> See *Francis*, 432 A.2d at 822 (explaining that director’s duty to not make a grossly negligent decision requires her to have “at least a rudimentary understanding of business of corporation” or, in other words, to become familiar with the fundamentals of corporation’s business).

decision that, if recommended, will benefit the corporation and its shareholders.<sup>49</sup> Before a merger is completed, the corporate officers promote it, the directors recommend it or decline to recommend it to shareholders, and, in the instance the merger proposal gets the board's approval, the shareholders vote on it.<sup>50</sup> Because the ultimate decision must be made by the corporation's shareholders, the directors have a duty to disclose to the shareholders all material information necessary for the shareholders to make a competent decision.<sup>51</sup>

Courts are generally deferential to a board's decision so long as the board does not "totally overlook facts called to their attention."<sup>52</sup> Whether a court feels a board's decision is substantively wrong does not provide grounds for director liability.<sup>53</sup> If a court finds that the process undertaken by the board was "rational" and "employed in a good faith effort to

<sup>49</sup> See *Kamin*, 383 N.Y.S.2d at 810–13. In *Kamin*, the court found that the board of directors did not breach its duty of care when it made a decision to issue dividends in kind as opposed to selling shares in the corporation. *Id.* at 810. Shareholders argued that the board breached its duty of care because the decision to issue dividends in kind resulted in adverse tax consequences for the corporation. *Id.* The *Kamin* court did not analyze whether the board's decision was substantively sound; instead, it held in favor of the directors because they informed themselves of the adverse tax consequences before making the decision, carefully considered and unanimously rejected the action proposed by the shareholders at a special memorialized formal meeting, and discussed other factors which led them to their decision. *Id.*; see also James A. Fanto, *Braking the Merger Momentum: Reforming Corporate Law Governing Mega-Mergers*, 49 BUFF. L. REV. 249, 306 (2001). Fanto argues that corporate law, by imposing fiduciary duties, strengthens the decision-making of the board. *Id.*

<sup>50</sup> See *Barris Industries, Inc. v. Bryan*, 686 F.Supp. 125, 130 (E.D. Va. 1988) (noting that Virginia law requires that no shareholder voting take place on merger proposals until the board of directors has drafted formal merger plan and submitted it to shareholders); see also *Kansas City Power & Light Co. v. Western Resources*, 939 F. Supp. 688, 689 (W.D. Mo. 1996) (discussing that certain forms of mergers are allowed, but only after shareholder vote).

<sup>51</sup> See *Malone v. Brincat*, 722 A.2d 5, 14 (Del. 1998) (discussing how Delaware law allows shareholders to sue directors who deliberately misinform them about the business of corporation); see also *Jackson Nat'l Life Ins. Co. v. Kennedy*, 741 A.2d 377, 388 (Del. Ch. 1999) (noting that the board of directors of a corporation owe a "fiduciary duty of disclosure" to stockholders when they seek stockholder action).

<sup>52</sup> See *Smith v. Van Gorkom*, 488 A.2d 858, 881 (Del. 1985) (holding that directors liable for breach of their duty of care because board entered into merger without gathering all pertinent information regarding monetary value of deal and without providing shareholders with information necessary to give informed approval of recommendation); see also *Kamin v. American Express Co.*, 383 N.Y.S.2d 807, 811 (Sup. Ct. 1976) (finding that plaintiffs must do more than simply allege that directors made imprudent decision in order to win judgment in court).

<sup>53</sup> See *In Re Caremark Int'l. Derivative Litig.*, 698 A.2d 959, 968 (Del. Ch. 1996) (noting that "[w]here a director in fact exercises a good faith effort to be informed and to exercise appropriate judgment, he or she should be deemed to have satisfied the duty of attention").

advance corporate interests,” board members will generally not be held personally liable for a duty of care breach based on grossly negligent decision-making.<sup>54</sup>

## 2. The Duty of Care: The Duty to Monitor

Historically, a board's duty of care only included the duty not to engage in grossly negligent decision making.<sup>55</sup> However, *In re Caremark International, Inc. Derivative Litigation* established that corporate directors can also be held personally liable for failing to adequately “[monitor] . . . the enterprise to assure that the corporation functions within the law to achieve its [business goals].”<sup>56</sup> This aspect of the director's duty of care has become known as the duty to monitor.<sup>57</sup>

A determination regarding whether a board has breached its duty to monitor is fact intensive. *Caremark* provides guidance as to the factors used by courts in determining whether a duty to monitor breach has occurred.<sup>58</sup> *Caremark*, a managed-care healthcare provider that received reimbursements from Medicare and Medicaid, was investigated for possible Anti-Referral Payments Law (ARPL) violations in 1991.<sup>59</sup> After learning of the violations, *Caremark* officers instituted a program that provided greater supervision of its 7000 employees and several revisions to

<sup>54</sup> See *Caremark*, 698 A.2d at 967. State corporate law statutes such as Delaware General Corporation Law § 102(b)(7) also make it difficult for shareholders to hold directors liable for duty of care breaches. See 8 Del. Code. Ann. § 102(b)(7) (2005). In particular, Section 102(b)(7) provides that a company's certificate of incorporation may contain a provision limiting a director's liability for her breach of fiduciary duty as long as the provision does not limit her liability for breach of her duty of loyalty or good faith. See Arthur B. Laby, *Resolving Conflicts of Duty in Fiduciary Relationships*, 54 AM. U.L. REV. 75, 148 (2004).

<sup>55</sup> See Watson, *supra* note 3, at 16 (highlighting that “[b]efore *Caremark*, a corporate director's duty of care was widely interpreted as having been fulfilled so long as the director did not engage in outlandish acts of neglect.”); see also *Van Gorkom*, 488 A.2d at 873 (holding that, in determining whether a board's decision was informed, the gross negligence standard should be applied).

<sup>56</sup> *Caremark*, 698 A.2d at 969.

<sup>57</sup> See Primo Fontana, Comment, *CERCLA Derivative Suits*, 27 B.C. ENVTL. AFF. L. REV. 741, 746 (2000) (positing that “*In re Caremark International Derivative Litigation* has led some to believe that directors and officers may have an affirmative ‘duty to monitor’ the behavior of subordinate employees”). See generally Watson, *supra* note 3, at 19 (noting that this breach of the duty of care is also referred to as an active breach).

<sup>58</sup> It is important to note that because *Caremark* was a settlement decision, it has no precedential value and remains only aspirational.

<sup>59</sup> See Watson, *supra* note 3, at 16 (noting that ARPL prohibits healthcare companies from making payments in exchange for Medicare and Medicaid patient referrals).

its internal compliance manual.<sup>60</sup> It received reports from an outside auditor stating that there were no “material weaknesses in Caremark’s conflict control structure,” and appointed a compliance officer.<sup>61</sup> In addition, Caremark’s board kept careful meeting minutes, reflecting that it was “aware of Caremark’s various efforts to assure compliance with the ARPL and other kickback laws.”<sup>62</sup>

Despite its best reform efforts, Caremark was indicted by a federal grand jury. Following the indictment, five separate shareholder derivative actions were filed against Caremark’s directors.<sup>63</sup> Caremark entered a proposed settlement agreement in the shareholder derivative suits which required the Delaware Chancery Court’s approval.<sup>64</sup> In determining whether the settlement was reasonable, the court needed to address the shareholder’s claim and ask whether Caremark had breached its duty to actively monitor Caremark’s corporate performance by allowing a situation to develop which exposed it to enormous legal liability.<sup>65</sup>

While such a duty to monitor had not been recognized in the past, the Delaware court held that a director’s obligation includes a duty to attempt in good faith to assure that an adequate corporate information and reporting system exists.<sup>66</sup> It added that a director’s failure to do so could render the director liable for losses caused by non-compliance with applicable legal standards.<sup>67</sup> Elaborating on this standard, the court stated that

<sup>60</sup> See Watson, *supra* note 3, at 17 (stating that these changes took place both before and during investigations into Caremark).

<sup>61</sup> Watson, *supra* note 3, at 17.

<sup>62</sup> Watson, *supra* note 3, at 17.

<sup>63</sup> See *In Re Caremark Int’l. Derivative Litig.*, 698 A.2d 959, 971 (Del. Ch. 1996) (commenting on shareholder derivative claims of director fault); see also Watson, *supra* note 3, at 17 (noting that five stockholder derivative actions were filed in Delaware Chancery Court).

<sup>64</sup> *Caremark*, 698 A.2d at 972.

<sup>65</sup> See *id.* at 967 (noting that director may breach duty of care and liability may attach from “an unconsidered failure of the board to act in circumstances in which due attention would have arguably prevented the loss”).

<sup>66</sup> See *id.* at 969–70 (holding that board must use its good faith judgment to ensure that information will come to it in timely manner so that it may satisfy its obligations to corporation).

<sup>67</sup> See *id.* at 970 (finding that “a director’s obligation includes a duty to attempt in good faith to assure that a corporate information and reporting system, which the board concludes is adequate, exists, and that failure to do so under some circumstances may, in theory at least, render[s] a director liable for losses caused by non-compliance with applicable legal standards”).

the system must be timely and accurate, must contain legal compliance and business performance information, and must enable information to flow to the board in the ordinary course of business.<sup>68</sup> In conclusion, the court determined that Caremark's compliance program met the enumerated standard and thereby found that the directors had not breached their duty to monitor. It resultantly also approved the board's settlement agreement.<sup>69</sup>

Extrapolating from the standard articulated in *Caremark*, it appears that a board will not be held to breach its duty of care for failure to monitor if it undertakes a reasonable investigation, duly deliberates, and concludes that the establishment of a compliance program is not in the shareholders' best interests. In other words, it seems that if the board undertakes a cost-benefit analysis and finds that the likelihood of its employees violating applicable law multiplied by the cost of fines associated with violations of the law is less costly than installing an efficient compliance system, a court will defer to the board's decision. Thus, it is asserted that the duty to monitor can also be satisfied by a board's decision not to install a compliance program. In this regard, it is suggested that the company's bottom line, or economic interest, in ensuring compliance with the law determines whether the board will strictly monitor compliance with the law.

### *B. The Unocal and Revlon Duties*

When a corporation decides to engage in a "mergers of equals," a merger in which both companies retain their shareholders, directors are only legally obligated to comply with their traditional fiduciary duties of care, loyalty, and good faith.<sup>70</sup>

<sup>68</sup> See *id.* (elaborating on meaning of "adequate," board noted that system should be "reasonably designed to provide to senior management and the board itself timely, accurate information sufficient to allow management and the board, each within its scope, to reach informed judgments concerning both the corporation's compliance with law and its business performance").

<sup>69</sup> See *In Re Caremark Int'l. Derivative Litig.*, 698 A.2d 959, 972 (Del. Ch. 1996) (stating that proposed settlement "appears to be an adequate, reasonable, and beneficial outcome for all of the parties").

<sup>70</sup> See *Fanto*, *supra* note 36, at 1338 (likening merger of equals to partnership); see also Janet E. Kerr, *Delaware Goes Shopping For a "New" Interpretation of the Revlon Standard: The Effect of the QVC Decision on Strategic Mergers*, 58 ALB. L. REV. 609, 611 n.10 (1995) (quoting LOU R. KLING & EILEEN NUGENT SIMON, *NEGOTIATED ACQUISITIONS OF COMPANIES, SUBSIDIARIES, AND DIVISIONS* 22.01[1] (1994) and describing merger of equals as when "two companies of approximately the same size combine in a stock-for-

However, many acquisitions are not amicable deals and occur in the form of takeovers.<sup>71</sup> In the context of takeovers, a board's legal duties are compounded.<sup>72</sup>

When a board decides it is going to take defensive measures to protect a corporation from an unwanted takeover bid, it must abide by, what are called, *Unocal* duties;<sup>73</sup> directors must be able to prove that they responded to a takeover bid in good faith and after reasonable investigation and that the response they adopted was proportionate to the threat posed by hostile bidder.<sup>74</sup>

The *Unocal* duties are also a product of the shareholder primacy approach to corporate governance.<sup>75</sup> Liability attaches to the board only when shareholders can first prove that the directors' interests in the transaction were conflicted – that the directors' decision to defend against the takeover was primarily motivated by pecuniary self-interest.<sup>76</sup> Courts will not scrutinize

stock exchange with the ratio based upon their relative size or upon the ratio of their unaffected trading prices”).

<sup>71</sup> See *Paramount Communications, Inc. v. Time, Inc.*, 571 A.2d 1140, 1150 (Del. 1989) (noting the existence of hostile tender offers); see also *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 176 (Del. 1985) (commenting on the circumstances surrounding a takeover threat).

<sup>72</sup> See *Paramount Communications, Inc. v. QVC Network*, 637 A.2d 34, 42 (Del. 1994) (stating that enhanced scrutiny of directors' conduct will occur when conduct embodies measures in response to threat of corporate control); see also *Time*, 571 A.2d at 1150–51 (discussing responsibilities of board in the event of takeover); *Revlon*, 506 A.2d at 180 (emphasizing that the business judgment rule is applicable to the decisions of directors responding to takeover threats provided that the principles of care, loyalty, and independence are satisfied). See generally *Unocal Corp. v. Mesa Petroleum Corp.*, 493 A.2d 946, 954 (Del. 1985) (explaining that when faced with pending takeover, the actions of the board are subjected to judicial examination before protection of business judgment rule is conferred).

<sup>73</sup> See *Time*, 571 A.2d at 1151 (referring to an analysis of whether there was a proper exercise of business judgment); see also *Unocal*, 493 A.2d at 956 (delineating the duties).

<sup>74</sup> See *QVC*, 637 A.2d at 45 (stating that directors must show they were adequately informed and acted reasonably); see also *Unocal*, 493 A.2d at 955 (explaining that directors satisfy burden of showing they had reasonable grounds for making decision “by showing good faith and reasonable investigation”).

<sup>75</sup> See *Unocal*, 493 A.2d at 956 (stating that “minority stockholder shall receive the substantial equivalent in value of what he had before”); see also Stephen M. Bainbridge, *Pre-commitment Strategies in Corporate Law: The Case of Dead Hand and No Hand Pills*, 29 IOWA J. CORP. L. 1, 35 n.276 (2003) (arguing that *Unocal* duties and shareholder primacy are compatible). But see Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 308 (1999) (arguing that *Unocal* “squarely rejects shareholder primacy in favor of the view that the interests of the ‘corporation’ include the interests of non-shareholder constituencies”).

<sup>76</sup> See *Unocal*, 493 A.2d at 956 (ruling that board's decision to fight Mesa was not primarily motivated by pecuniary self-interest); see also Kerr, *supra* note 70, at 637 (1995) (noting that in absence of self-interest, the actions of an independent board are protected by the business judgment rule, provided that the *Unocal* duties are met).



the director's business decisions in the takeover context unless there exists a judicial concern that board members may be focusing more on maintaining their board positions than on shareholder interests.<sup>77</sup>

Under the *Unocal* duties, directors are entitled to consider the impact of its decision on non-shareholder constituencies, but they are obligated only to act in the best interest of shareholders.<sup>78</sup> Thus, boards cannot justify their takeover defense mechanisms if they do not further the shareholder profit maximization goal, even if they are in the best interest of non-shareholder constituencies.<sup>79</sup>

In addition to *Unocal* duties, directors owe further duties to shareholders when the sale or break up of the company becomes inevitable.<sup>80</sup> In this case, the duty of the board<sup>81</sup> switches from protecting the corporation to maximizing the sale price (the short term profits) for shareholders.<sup>82</sup> Again, the rationale beneath this

<sup>77</sup> See *Unocal*, 493 A.2d at 958 (ruling that "unless it is shown by a preponderance of the evidence that the director's decisions were based on perpetuating themselves in office" court will not substitute its own judgment for board's judgment); see also Charles M. Elson, *The Duty of Care, Compensation, and Stock Ownership*, 63 U. CIN. L. REV. 649, 656-57 (1995) (describing "captured board" syndrome and its relation to board member priorities).

<sup>78</sup> See *Unocal Corp. v. Mesa Petroleum Corp.*, 493 A.2d 946, 955 (Del. 1985) (stating that "corporate directors have a fiduciary duty to act in the best interests of the corporation's stockholders"); see also Robert E. Bull, Note, *Directors' Responsibilities and Shareholders' Interests in the Aftermath of Paramount Communications v. Time, Inc.*, 65 CHI.-KENT L. REV. 885, 914 n.214 (1989) (arguing that directors are supposed to make business decisions in shareholders' best interest).

<sup>79</sup> See *Unocal*, 493 A.2d at 955 (announcing that boards must act in the best interest of their stockholders.); see also Cheryl L. Wade, *For-Profit Corporations that Perform Public Functions: Politics, Profit, and Poverty*, 51 RUTGERS L. REV. 323, 331 (1999) (noting that many scholars believe that "the responsibilities of corporate managers do not extend beyond shareholder interests").

<sup>80</sup> See *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 184 (Del. 1985) (holding that when takeover is inevitable the board must allow market forces to operate freely to ensure that shareholders will receive their best price available for their equity). See generally *Paramount Communications, Inc. v. QVC Network*, 637 A.2d 34, 43 (Del. 1994) (finding that the sale and break-up of the company was deemed inevitable when QVC entered into a merger where change of control would take place).

<sup>81</sup> See Kerr, *supra* note 70, at 620 (noting that "the duty of the board of directors to maximize share value is now referred to as the Revlon duty"); see also Wells M. Engledow, *Structuring Corporate Board Action to Meet the Ever-Decreasing Scope of Revlon Duties*, 63 ALB. L. REV. 505, 505 (1999) (highlighting that *Revlon* held that when sale or breakup of the corporation becomes inevitable, board's primary function shifts to maximizing sale value of the company).

<sup>82</sup> See Douglas G. Baird, *The New Face of Chapter 11*, 12 AM. BANKR. INST. L. REV. 69, 75 n.29 (2004) (noting the duty to maximize stockholder value when a takeover or breakup of a company becomes inevitable); see also Brian K. Kidd, Note, *The Need for Stricter Scrutiny: Application of the Revlon Standard to the Use of Standstill Agreements*, 24 CARDOZO L. REV. 2517, 2542 (2003) (discussing *Revlon's* holding that "once the sale of a

duty is based on the shareholder primacy model. Directors must, above all else, act to maximize profits for shareholders.<sup>83</sup> Shareholder primacy is even more pronounced in this context given that when the sale and break-up of the corporation becomes inevitable, directors are actually prohibited from considering non-shareholder interests.<sup>84</sup>

### C. Federal Regulations Applicable to Directors in M&A Context

As state corporate laws require that directors disclose to shareholders all relevant information regarding mergers and acquisitions so that shareholders may competently decide whether to approve the proposed merger, federal securities laws also place great emphasize on informed decision-making in public companies.<sup>85</sup> Specifically, under the federal proxy rules, public companies must solicit shareholder votes in a systemized manner and disclose to the shareholders considerable information about “the transaction, the parties involved, the reasons for it, its risks and the merger consideration.”<sup>86</sup> The federal rules also demand that the corporation give its shareholders adequate time to consider the merger before casting their votes.<sup>87</sup>

corporation becomes inevitable, the target board has a duty to conduct a fair bidding auction and obtain the highest possible sale price for the corporation”).

<sup>83</sup> See *Reylon*, 506 A.2d at 182 (stating that when breakup or sale becomes inevitable, duty of board becomes “maximization of the company’s value at a sale for the stockholders’ benefit”); see also Nancy A. Peterman & Sherri Morissette, *Director’s Duties in the Zone of Insolvency: The Quandary of the Nonprofit Corp.*, 23-2 AM. BANKR. INST. J. 12, 12 (2004) (stating that in general, board of directors “only owes a fiduciary duty to its shareholders to maximize profits and shareholder wealth”).

<sup>84</sup> See *Reylon*, 506 A.2d at 176 (ruling that actions taken by directors during takeover threat require “rationally related benefit accruing to the stockholders”); see also Wai Shun Wilson Leung, *The Inadequacy of Shareholder Primacy: A Proposed Corporate Regime that Recognizes Non-Shareholder Interests*, 30 COLUM. J.L. & SOC. PROBS. 587, 611 (1997) (describing shareholders’ interests as paramount in hierarchy of board priorities).

<sup>85</sup> See Arthur R. Pinto, *Corporate Governance: Monitoring the Board of Directors in American Corporations*, 46 AM. J. COMP. L. 317, 334 (1998) (detailing breadth of corporate disclosure requirements); see also J. Robert Brown, Jr., *Corporate Secrecy, the Federal Securities Laws, and the Disclosure of Ongoing Negotiations*, 36 CATH. U. L. REV. 93, 103-06 (1986) (listing SEC-imposed disclosure requirements).

<sup>86</sup> See Fanto, *supra* note 49, at 307 (listing the information required for disclosure under the Federal Proxy Rules); see also 15 U.S.C. § 78n(a) (2005) (governing the solicitation of proxies); 17 C.F.R. § 240.14a-2 (2005) (listing types of solicitations federal regulations apply to).

<sup>87</sup> Under federal proxy rules, “shareholders [must] receive considerable disclosure about the transaction, the parties involved, the reasons for it, its risks and the merger consideration, as well as have time to evaluate the information and to decide whether to cast their vote in support of the merger.” See Fanto, *supra* note 49, at 307. Specifically, 15 U.S.C. 78n(c) provides, in relevant part:

## II. EQUAL OPPORTUNITY AND SEXUAL DISCRIMINATION LITIGATION

### A. *The Emerging Trend in Employment Discrimination Litigation*

The corporate accounting scandals of 2002 received maximum media attention. Company names such as Enron, WorldCom, Tyco, and Arthur Anderson were thrust onto front-page news and into the public discourse. Conversely, the problem of racial and sexual discrimination in the corporate workplace has received considerably less public attention though it has been a major issue facing women and minorities for centuries.<sup>88</sup> Recently, however, there has been a significant rise in employment litigation<sup>89</sup> and legal and human resource experts predict that the number of lawsuits will increase exponentially.<sup>90</sup> Specifically, the U.S. Chamber of Commerce's litigation center has estimated

Information to holders of record prior to annual or other meeting. Unless proxies, consents, or authorizations in respect of a security registered pursuant to section 12 of this title [15 USCS § 78I], or a security issued by an investment company registered under the Investment Company Act of 1940 [15 USCS §§ 80a-1 et seq.], are solicited by or on behalf of the management of the issuer from the holders of record of such security in accordance with the rules and regulations prescribed under subsection (a) of this section, prior to any annual or other meeting of the holders of such security, such issuer shall, in accordance with rules and regulations prescribed by the Commission, file with the Commission and transmit to all holders of record of such security information substantially equivalent to the information which would be required to be transmitted if a solicitation were made, but no information shall be required to be filed or transmitted pursuant to this subsection before July 1, 1964.

15 U.S.C. § 78n(a) (2005).

<sup>88</sup> See, Joe R. Feagin et. al., *The Many Costs of Discrimination: The Case of Middle-Class African Americans*, 34 IND. L. REV. 1313, 1343 (2001) (noting lack of media attention on workplace discrimination even though victims of such suffer psychological harm in addition to real harm of non-promotion). See generally Rosemary Barnes, *Still On The Outside*, SAN ANTONIO EXPRESS NEWS, April 2, 2005, at 10H (quoting Wesley Poriotis, chairman of Wesley, Brown, Bartle & Roldan, leading minority executive recruitment firm based in New York as stating that “[i]t’s been this sad, same story for 30 years. What we hear from corporations is that diversity is important, but not for critical positions”).

<sup>89</sup> See Wade, *supra* note 8, at 225 (proposing that increase of litigation is due to increased willingness of employees and shareholder activists to litigate discrimination issues); see also Morris et al., *supra* note 9, at 65–72 (noting that companies are vulnerable to sex-discrimination lawsuits and advising companies to adopt consistent procedures and established guidelines for employee advancement in order to prevent overbearing litigation).

<sup>90</sup> See Morris et al., *supra* note 9, at 66 (citing AFL-CIO survey as concluding that the critical mass of career women, now reaching their 40’s, are becoming increasingly frustrated with the disparities between men and women’s pay in corporate employment; thus increasing litigation is natural result). See generally Wade, *supra* note 8, at 225 (asserting that dramatic rise in amounts paid to settle discrimination claims has played role in bolstering shareholder activism).

that such employment lawsuits will cost corporations “billions and billions of dollars.”<sup>91</sup> Due to this trend, disturbing practices that corporations would like to keep secret (namely, methods used to reward workers, determine entry-level salaries, make promotions and layoff decisions, and divvy up merit raises) have become more readily scrutinized; thus, the need for corporate reform in terms of diversity is urgent.<sup>92</sup>

### B. *The Development of the Civil Right to Equal Employment*

In order to understand the importance of the recent success that women and minorities have been experiencing in asserting their rights to equal employment, a brief historical review is necessary. The Civil Rights Act of 1964 (the “64 Act”) made it illegal for employers to discriminate on the basis of race, creed, and sex.<sup>93</sup> Furthermore, it provided for the establishment of the Equal Employment Opportunity Commission (“EEOC”).<sup>94</sup> The ‘64 Act also required that any company with 100 employees or more file annual accounts of the number of women and minorities it had at all levels of the organization.<sup>95</sup>

<sup>91</sup> See Morris et al., *supra* note 9, at 66 (quoting a recently filed brief by U.S. Chamber of Commerce litigation center in support of Wal-Mart’s appeal of class-action certification of its lawsuit estimates damage somewhere in “billions and billions of dollars.”); see also Wade, *supra* note 8, at 225 (describing “meteoric rise in amounts paid to settle discrimination claims”).

<sup>92</sup> See Morris et al., *supra* note 9, at 66 (highlighting that traditionally such practices were kept quiet as internal complaints were inconspicuously handled by management, in contrast with today’s threat of sex discrimination cases which has been described as “one of corporate America’s worst nightmares”); see also Tristin K. Green, *Work Culture and Discrimination*, 93 CALIF. L. REV. 623, 664 (2005) (positing that, in light of discriminatory potential of work culture, there should at least be modest reform in the way courts and litigants think about traditional discrimination claims).

<sup>93</sup> 42 U.S.C. § 2000e-2(a)(1) (2005) (stating that “[i]t shall be an unlawful employment practice for an employer . . . to fail or refuse to hire or to discharge any individual, or otherwise to discriminate against any individual with respect to his compensation, terms, conditions, or privileges of employment, because of such individual’s race . . . religion [and] sex . . .”).

<sup>94</sup> See Francis Achampong, *Policy Implications of Rules Governing Harassment and Discrimination Complaints in Private and Federal Employment*, 20 HOFSTRA LAB. & EMP. L.J. 51, 54 (2002) (examining role of EEOC under Civil Rights Act of 1964); see also Marjorie A Silver, *The Uses and Abuses of Informal Procedures in Federal Civil Rights Enforcement*, 55 GEO. WASH. L. REV. 482, 485 (1987) (positing that “[t]he passage of the Civil Rights Act of 1964 (1964 Act) marked a turning point in this country’s political commitment to the eradication of discrimination against women and minorities”).

<sup>95</sup> See Michael J Zimmer, *Systematic Empathy*, 34 COLUM. HUMAN RIGHTS L. REV. 575, 603 n.124 (2003) (noting that EEO-1 Form requires that private employers with one hundred or more employees compile gender, race, and ethnicity information about their employees, as mandated by the Civil Rights Act of 1964); see also John B. Moretta, *Just Who Is An Applicant?: The Impact of Electronic Resumes and Job Search Engines on*

Although the EEOC acquired large settlements through sex discrimination claims against AT&T in the 1970's, the conservative Reagan-era courts rarely certified class-action lawsuits and made it more difficult to prove sex-discrimination.<sup>96</sup> After a significant growth in civil rights and women's' activism groups, Congress passed The Civil Rights Act of 1991 ("the '91 Act") which allowed for substantial punitive damages against companies that discriminated by gender.<sup>97</sup> The '91 Act made it easier for women to file sex discrimination charges.<sup>98</sup> Notably, not much employment litigation occurred during the economic boom of the 1990's.<sup>99</sup> However, by the end of the decade, multi-million dollar settlements were being awarded to classes of plaintiffs by major corporations.<sup>100</sup> In 1999, the SEC further enhanced the rights of employment discrimination claimants by prohibiting firms from requiring that their employees sign private contracts binding them to arbitrate civil rights claims.<sup>101</sup>

*Employment Discrimination Law*, 2 J. HIGH TECH. L. 123, 138 (2003) (highlighting that "penalties for failure to file a report or for falsifying a report are extensive and severe").

<sup>96</sup> See Morris et al., *supra* note 9, at 66 (highlighting how "[i]n the '80s the EEOC . . . became less feisty; conservative Reagan-era courts all but eliminated the class-action suit and made it much tougher to prove sex discrimination"); see also Douglas M. Staudmeister, Comment, *Grasping the Intangible: A Guide to Assessing Nonpecuniary Damages in the EEOC Administrative Process*, 46 AM. U.L. REV. 189, 195 (1996) (suggesting that the judiciary had retreated from previous advances in civil rights and EEO jurisprudence).

<sup>97</sup> See Melissa Hart, *Will Employment Discrimination Class Actions Survive?*, 37 AKRON L. REV. 813, 814 (2004) (positing that "[t]he addition of compensatory and punitive damages and a jury-trial right in the Civil Rights Act of 1991 may increase the level of scrutiny and perhaps the level of judicial involvement necessary in an employment discrimination class action"); see also Morris et al., *supra* note 9, at 71 (stating that the Civil Rights Act of 1991 allowed for substantial punitive damages against companies that discriminated by gender).

<sup>98</sup> See Achampong, *supra* note 94, at 55-72 (examining the modern formalized process of the EEOC to deal with complaints of sexual discrimination from filing to appeal); see also Staudmeister, *supra* note 96, at 201 (noting that there has been a dramatic increase of litigation in the wake of the Civil Rights Act of 1991).

<sup>99</sup> See John J. Donohue III & Peter Siegelman, *Law and Macroeconomics: Employment Discrimination Litigation Over the Business Cycle*, 66 S. CAL. L. REV. 709, 725 (1993) (analyzing the statistical relationship between the business cycle and the volume of federal employment discrimination case filings); see also Antilla, *supra* note 10, at 19 (noting that employment discrimination suits increase during low economic downturns).

<sup>100</sup> See Morris et al., *supra* note 9, at 66 (highlighting settlements of Mitsubishi for \$34 million in 1996, Home Depot for \$104.5 million in 1997, and American Express for \$42 million in 2002); see also *Boeing Gives Details of Settlement of Sex-Bias Suit*, N.Y. TIMES, Jul. 17, 2004, at C1, C4 (hereinafter *Boeing Gives Details*) (discussing the Boeing settlement of \$40.6 to \$72.5 million).

<sup>101</sup> See Antilla, *supra* note 10, at 19 (stating that in 1999 SEC changed rules to prohibit mandatory arbitration for discrimination claims); see also *Paul Revere Variable Annuity Ins. Co. v. Kirschhofer*, 226 F.3d 15, 19 n.5 (1st Cir. 2000) (stating that "NASD

Today, employment discrimination lawsuits are being certified as class actions with increased frequency and are resulting in multi-million dollar settlements. The 2004 Boeing settlement arose out of a lawsuit brought by women who contended they were mistreated because of their sex.<sup>102</sup> The case was initiated in 2000 by female employees who claimed that Boeing allowed for sexual intimidation and improper advances in the workplace and alleged that Boeing paid women less for performing the same duties as men.<sup>103</sup> The certified class could have included as many as 29,000 former employees.<sup>104</sup> Boeing resultantly agreed to pay the plaintiffs between \$40.6 million to \$72.5 million to settle the class action.<sup>105</sup> In addition, the settlement, preliminarily approved by Judge Marsha A. Pechman of United States District Court in Seattle, included changes in the way Boeing evaluates employees for raises and promotions.<sup>106</sup>

In January 2005, Boeing's troubles only increased when the same district court judge certified a class of former African American Boeing employees asserting Title VII disparate impact and disparate treatment claims.<sup>107</sup>

Rule 10201 was amended to exempt statutory employment discrimination claims from mandatory arbitration").

<sup>102</sup> See *Boeing Gives Details*, *supra* note 100, at C4 (stating that female employees who brought claim said Boeing tolerated sexual intimidation and improper advances in workplace); see also Morris et al., *supra* note 9, at 66 (describing that female employees claimed they were paid less and not promoted as quickly as their male counterparts).

<sup>103</sup> See Morris et al., *supra* note 9, at 66 (highlighting that female employees who brought claim said they were paid less and not promoted as quickly as males); see also *Boeing Gives Details*, *supra* note 100, at C4 (stating that "case was first brought in February 2000 by female employees who said that Boeing tolerated sexual intimidation and improper advances in the workplace").

<sup>104</sup> See *Boeing Gives Details*, *supra* note 100, at 4 (stating that Boeing claimed class could number "as many as 29,000"); see also Christopher P. Reynolds & Richard W. Black, *The Increasing Risk of Legal Challenges to an Employer's Compensation Policies and Practices: Considerations for Compensation Self-assessment*, JOURNAL OF INVESTMENT COMPLIANCE, March 22, 2005, at 55 (outlining Boeing's settlement with approximately 29,000 salaried and hourly female employees alleging discrimination).

<sup>105</sup> See *Boeing Gives Details*, *supra* note 100, at 4 (stating such changes); *Sex Discrimination Suit is Settled by Boeing; Employment*, NAT. L. J., July 26, 2004, at 16 (reporting that Boeing agreed to pay between \$40.6 and \$70.2 million).

<sup>106</sup> See *Boeing Gives Details*, *supra* note 100, at 4 (stating that settlement included changes in way Boeing evaluates workers for raises and promotions); see also *Sex Discrimination Suit is Settled by Boeing*, *supra* note 105, at 16 (stating that settlement required Boeing to "change the way it determines starting salaries, modify its performance-evaluation tools and monitor salaries and overtime to reduce the risk of gender discrimination").

<sup>107</sup> See *Williams v. Boeing Co.*, 225 F.R.D. 626 (W.D. Wash. Jan. 21, 2005) (certifying class-action of African American employees against Boeing).

The Wal-Mart sex discrimination class action based on huge discrepancies in pay and promotion between the corporation's male and female employees began in 1998 when a female employee realized, after finding a W-2 form lying around the Sam's Club in which she worked, that she was making \$10,000 less per year than her male counterpart.<sup>108</sup> When a federal district court judge certified the class of plaintiffs in *Dukes v. Wal-Mart*,<sup>109</sup> the largest discrimination suit in history was born, covering 1.5 million current and former employees at every Wal-Mart and Sam's Club store in the country.<sup>110</sup>

Possibly the most prominent multi-million dollar settlement of late is that which resolved the Wall Street women and EEOC's class action sex discrimination suit against Morgan Stanley in July 2004.<sup>111</sup> While denying ever having presided over any discrimination, Morgan Stanley agreed to pay the plaintiffs \$54 million.<sup>112</sup>

### III. DIVERSITY IN CORPORATE AMERICA

#### A. *In General*

Over forty years after the Civil Rights Act of 1964 made discrimination on the basis of race, creed, and sex illegal, employment discrimination is still a major issue in corporate

<sup>108</sup> See Cora Daniels, *Women vs. Wal-Mart: How Can the Retailer Reconcile Its Storied Culture With the Anger of Some of its Female Employees?*, FORTUNE, July 21, 2003, at 78 (discussing that Wal-Mart suit started after female assistant manager found W-2 of male assistant manager who was making \$10,000 more than her annually); see also Morris et al., *supra* note 9, at 66 (highlighting fact that at Wal-Mart women make up more than 72% of hourly workers but hold only about one third of management positions).

<sup>109</sup> 222 F.R.D. 137 (N.D. Cal. June 16, 2004).

<sup>110</sup> See Benedict Sheehy, *Corporations and Social Costs: The Wal-Mart Case Study*, 24 J.L. & COM. 1, 39 (stating lawsuit was on behalf of 1.5 million former female employees); see also Daniels, *supra* note 108, at 78 (stating Wal-Mart case would become largest discrimination suit in history).

<sup>111</sup> See Thomas Landon Jr., *Morgan Names Official to Regulatory and Legal Areas*, N.Y. TIMES, May 5, 2005, at A1 (mentioning "humiliating \$54 million sex discrimination settlement"); see also Antilla, *supra* note 10, at 19 (discussing the \$54 million settlement between Morgan Stanley and class of 340 former and current female employees).

<sup>112</sup> See Phyllis Furman, *Wall Street Suit Nets \$40M. Morgan Stanley Women To Share Big Settlement*, DAILY NEWS (NY), August 16, 2005, at 8 (reporting that "Morgan Stanley, which did not admit to any wrongdoing, agreed last year to pay a total of \$54 million to settle the case"); see also Antilla, *supra* note 10, at A19 (noting \$12 million went to Allison Schieffelin whose claims led to the EEOC suit, \$40 million to the 340 former and current MS employees, and \$2 million to the development of new diversity program).

America.<sup>113</sup> Particularly, the EEOC stated that in fiscal year 2004, it received 27,696 charges of race discrimination and recovered \$61.1 million in monetary benefits for charging parties and other aggrieved individuals.<sup>114</sup> Currently, women hold half of all management and professional jobs yet only 8% have achieved executive vice president level or above at Fortune 500 companies.<sup>115</sup> Moreover, both minorities and women who do reach senior executive status are paid significantly less than their white male counterparts.<sup>116</sup> Based upon these alarming statistics, it is evident that despite some companies' best efforts, American public corporations, as a whole, are not "equal opportunity employers."<sup>117</sup>

### *B. In the Context of Mergers and Acquisitions*

The employment discrimination discussion becomes both more complex and pressing in light of corporate America's current merger wave.<sup>118</sup> From November 2004 to January 2005, U.S.

<sup>113</sup> See Morris et al., *supra* note 9, at 64 (explaining that studies have shown women in all job categories are still being paid less for doing same job as men). See generally David Wilkins, *From "Separate Is Inherently Unequal" to "Diversity is Good For Business": The Rise of Market-Based Diversity Arguments And The Fate of the Black Corporate Bar*, 117 HARV. L. REV. 1548, 1551 (2004) (commenting that Supreme Court has again had to turn its attention to race-related discrimination in matters regarding affirmative action programs at the University of Michigan and its law school).

<sup>114</sup> The U.S. Equal Employment Opportunity Commission, *Race/Color Discrimination*, March 2, 2005, <http://www.eeoc.gov/types/race.html> (reporting that the EEOC resolved 29,631 race charges in fiscal year 2004 and observed an increasing number of race discrimination charges)

<sup>115</sup> See Morris et al., *supra* note 9, at 64 (highlighting discrepancy between number of women in corporate employment and number of women in upper level management); see also Louis Uchitelle, *Gaining Ground on the Wage Front*, N.Y. TIMES, Dec. 31, 2004, at C1 (highlighting share of women in executive, administrative, and managerial occupations is more than 46% and is similar or greater in professional ranks).

<sup>116</sup> See Morris et al., *supra* note 9, at 69 (explaining study on pay gap between male and female employees that controlled factors such as women delaying promotions by taking time off from work to raise families and women willingly choosing professions that pay less or quitting high-powered jobs); see also Uchitelle, *supra* note 115, at C1 (noting that working women now earn just over 80% of what men do).

<sup>117</sup> See Anne Fisher, *How You Can Do Better on Diversity*, FORTUNE, Nov. 15, 2004, at 60 (noting only 32% of U.S. employees think their companies do a decent job of hiring and promoting people other than white males); see also Antilla, *supra* note 10, at A19 (commenting that although Merrill Lynch settled class-action sex discrimination case in 1976 and pledged that 18% of their brokers would be women by 1980, it still only has women in 15% of its stockbroker positions today).

<sup>118</sup> See *Jute v. Hamilton Sundstrand Corp.*, No. 04-3927-CV, 2005 U.S. App. LEXIS 18038, at \*3 (2d Cir. Aug. 23, 2005) (demonstrating example of how employee discrimination becomes more complex when employers have ability to use "post-merger reorganization" as reasoning behind termination); see also Tully, *supra* note 11, at 21



companies announced forty-eight deals of \$1 billion or more, totaling an “astonishing” \$357 billion.<sup>119</sup> Despite the bubbling optimism connected with the merger frenzy, the truth is that such mega-mergers “typically produce about twice as many losers as winners.”<sup>120</sup> A major factor in determining what constitutes a “loser” and a “winner” is whether the merger generates sufficient synergy.<sup>121</sup>

Adequate synergy is defined by raising earnings while integrating both the acquiring and acquired corporations' businesses cultures.<sup>122</sup> Because integration typically involves major restructuring and many job cuts, companies whose philosophies and cultures are similar benefit from this process.<sup>123</sup> In terms of promoting diversity through a merger, both sides must have a commitment to encourage diverse leadership.<sup>124</sup> However, in the overwhelming majority of deals, diversity is not considered a major factor in deciding whether to merge.<sup>125</sup> As a result, studies have shown that women and minorities are much

(noting launch of new merger wave in corporate America that “marks not a tentative comeback but what looks like the start of a swaggering, full-fledged frenzy”);

<sup>119</sup> See Tully, *supra* note 11, at 21.

<sup>120</sup> See Tully, *supra* note 11, at 21.

<sup>121</sup> See Vivian Marino, *Shafts Of Light Seen In The Merger Tunnel*, N.Y. TIMES, June 2, 2002, § 3, at 4 (highlighting that “about half the executives interviewed attributed unsuccessful deals to their own poor evaluation of the potential synergies and benefits of a merger”); see also Tully, *supra* note 11, at 21 (noting that buyer must generate sufficient synergies by cutting jobs, combining computer systems, or selling more products to same customers, in order to pay for premium over market value).

<sup>122</sup> See Tully, *supra* note 11, at 21 (explaining that buyer must raise earnings quickly enough to justify value market was already placing on the target before the deal was announced in order to have a successful merger). See generally Paddy Manning, *Mega Mergers Stretch The Envelope*, THE AUSTRALIAN, April 9, 1999, at 35 (positing that “[m]ergers are all about synergies and efficiencies, as well as about market share”).

<sup>123</sup> See Tully, *supra* note 11, at 21.

<sup>124</sup> See *Cingular Recognized for Diversity*, MEMPHIS BUS. J., Aug. 8, 2005, available at [http://memphisbizjournals.com/memphis/stories/2005/08/08/daily3.html?from\\_yf=1](http://memphisbizjournals.com/memphis/stories/2005/08/08/daily3.html?from_yf=1) (suggesting that Cingular's merger with AT&T Wireless was successful due to diversity and inclusion initiatives); see also Elisabeth Frater, *Unite and Conquer: Corporate Mergers – Tackling the Tough Issues and Creating the Best of Both Diversity Worlds*, MINORITY CORPORATE COUNSEL ASSOC. (2004), <http://www.mcca.com/site/data/magazine/2004-09/uniteconquer0904.shtml> (adding companies must not only make a commitment to diverse leadership within corporate ranks, but also among key vendors, including law firms, advertising partners, and consulting agencies).

<sup>125</sup> See Frater, *supra* note 124 (positing that corporate mergers and acquisitions are generally not driven by diversity concerns). See generally Stuart Silverstein, *Breaking The Glass; Panel Seeks To Remove Ceiling On Promotions*, L.A. TIMES, Feb. 10, 1994, at D2 (citing the U.S. Labor Department's Glass Ceiling Commission as considering new ways of promoting diversity, including requiring companies seeking antitrust clearance for mergers to meet equal employment opportunity standards).

more likely to lose their jobs or be demoted in a reorganization.<sup>126</sup> In fact, downsizing, an element of every merger, has been defined as “the greatest challenge to workplace diversity.”<sup>127</sup>

### C. Legal Theories Underlying Diversification

#### 1. The Economic Justification: Diversity as ‘Good For Business’

The ‘diversity is good for business’ rationale gained acceptance after the famous affirmative action case, *Gratz v. Bollinger*.<sup>128</sup> In *Gratz*, amicus briefs in support of the University of Michigan Law School’s affirmative action policy were signed and submitted by a “veritable who’s who of the country’s largest and most profitable corporations.”<sup>129</sup> The briefs defended affirmative action in terms of the “demands of the marketplace”.<sup>130</sup> They asserted that it was in the best interest of American businesses to develop access to a substantial group of talented minorities who have graduated from the nation’s best educational institutions if American companies wished to continue prospering and expanding in a competitive global economy.<sup>131</sup> Justice O’Connor placed substantial weight on these amicus briefs and the economic justification for diversity in her majority opinion.<sup>132</sup>

<sup>126</sup> See Faye Rice, *How To Make Diversity Pay*, FORTUNE, Aug. 8, 1994, at 79 (discussing that at many companies women and minorities are often placed in low-level, dead-end staff positions which are typically cut first during reorganization); see also *A Report on the Glass Ceiling Initiative*, U.S. Dep’t of Labor, <http://www.mith2.umd.edu/WomensStudies/GenderIssues/GlassCeiling/LaborDeptInfo/glass-ceiling-initiative> (last visited January 17, 2006) (finding that “minorities and women are less likely to obtain positions in line functions - such as sales and production- which most directly affect the corporations’ bottom line, and are considered the fast track to the executive suite”).

<sup>127</sup> Rice, *supra* note 126, at 79.

<sup>128</sup> 539 U.S. 244 (2003).

<sup>129</sup> Wilkins, *supra* note 113, at 1552.

<sup>130</sup> Wilkins, *supra* note 113, at 1553.

<sup>131</sup> See *Grutter v. Bollinger*, 539 U.S. 306, 331 (2003) (acknowledging that “major American businesses have made clear that the skills needed in today’s increasingly global marketplace can only be developed through exposure to widely diverse people, cultures, ideas and viewpoints”); see also Wilkins, *supra* note 113, at 1553 (determining that “[i]f American business is to continue to expand and prosper in a competitive global economy, the current captains of capitalism sternly warned, then these organizations must have access to a substantial pool of talented minorities who have graduated from the nation’s best educational institutions”).

<sup>132</sup> See *Grutter*, 539 U.S. at 335 (holding that “[i]n order to cultivate a set of leaders with legitimacy in the eyes of the citizenry, it is necessary that the path to leadership be visibly open to talented and qualified individuals of every race and ethnicity”); see also

Today, it is well-documented that diversity is, in fact, 'good for business.' Many corporations have signed onto this rationale and have reaped financial benefits from instituting diversity programs.<sup>133</sup> For example, the merger between Anthem and Wellpoint, two of the nation's largest health benefits companies, brought together two corporations devoted to promoting women's rights.<sup>134</sup> Wellpoint lists as one of its major reasons for diversification, the fact that "women are the decision makers nearly 60% of the time when it comes to health insurance" and "[f]rom a business standpoint, our company has to reflect that."<sup>135</sup> In fact, corporations have become so accepting of diversity as an economic factor that there is currently a market for books and software dedicated to measuring "diversity return-on-investment and performance."<sup>136</sup>

In what ways do corporations find that diversity enhances their bottom line? First, the 65 Fortune 500 companies that signed the amicus briefs argue that a diverse work force facilitates effective problem-solving.<sup>137</sup> The corporations claim

Wilkins, *supra* note 113, at 1553 (noting that these two corporate briefs were significantly cited by Justice O' Connor in *Grutter*).

<sup>133</sup> See Rice, *supra* note 126, at 79 (suggesting that diverse work forces can enhance performance and are vital to workplace success); see also Wilkins, *supra* note 113, at 1554 (commenting that frustrated diversity advocates in large law firms "have increasingly turned to the kind of 'diversity is good for business' arguments articulated in *Grutter* to put pressure on firm managers to hire and promote minority lawyers").

<sup>134</sup> See Dana Knight, *Anthem-WellPoint Deal Bodes Well For Female Managers*, INDIANAPOLIS STAR, Jan. 28, 2005, at 1C (positing that WellPoint is good at advancing women in business); see also *WellPoint Named Top Company for Women Execs*, Earnings.com, <http://fulldisclosure.com/releasetext.asp?ticker=ath&coid=82476&client=c&b&release=66223> (last visited January 17, 2006) (noting that WellPoint was named one of America's Top 25 Companies for executive women).

<sup>135</sup> See *id.*

<sup>136</sup> See J. Cunyon Gordon, *The Legal Profession, Looking Backward: Painting by Numbers: "And, Um, Let's Have a Black Lawyer Sit At Our Table,"* 71 FORDHAM L. REV. 1257, 1278 (2003) (noting mockingly that companies can "buy books like *Measuring Diversity Results* for \$34.95 and if purchased with the 'Diversity Start-up Metrics Software' the skittish CEO rates a package price of \$149.00 (a savings of over \$10!)"). See generally Dallas, *supra* note 4, at 797 (explaining study of board best practices which found consensus among working groups that there are substantial economic arguments in favor of diversity).

<sup>137</sup> See Wilkins, *supra* note 113, at 1586 (noting that 65 Fortune 500 corporations stated in their brief that "a diverse group of individuals educated in a cross-cultural environment has the ability to facilitate unique and creative approaches to problem-solving arising from the integration of different perspectives"); see also Brief of Amicus BP America Incorporated as Amicus Curiae Supporting Neither Party at 2, *Grutter v. Bollinger*, 539 U.S. 306 (2003) (Nos. 02-241, 02-516) (noting that, "[b]ecause BP strongly believes that innovation, one of its core values, can only come from encouraging true diversity of styles and ideas while leveraging multiple talents, BP has made diversity and inclusion a strategic focus of its business in the [United States] and around the world");

that heterogeneous groups of employees with different perspectives arrive at more innovative ideas.<sup>138</sup>

In addition, proponents of the 'good for business' rationale note that the world is multi-cultural and that ethnic groups have buying power; thus, it is necessary for businesses to have employers who can "talk" to these ethnic consumers and give the business credibility.<sup>139</sup> The theory is that the more diverse a company's employees are, the more adept those employees will be at understanding the wants and needs of diverse consumers.<sup>140</sup>

Further, studies have measured share price reaction to the announcement of diversity awards and to publicized settlements of discrimination lawsuits.<sup>141</sup> For example, firms who have received the Exemplary Voluntary Efforts Award given by the Department of Labor to businesses that promote diversity have shown significantly positive excess returns while firms found liable for discrimination have exhibited significantly negative excess returns.<sup>142</sup> Lastly, proponents of the 'diversity is good for

Brief of General Motors as Amicus Curiae Supporting Respondents at 24, *Grutter v. Bollinger*, 539 U.S. 306 (2003) (Nos. 02-241, 02-516) (positing that "[a]bundant evidence suggests that heterogeneous work teams create better and more innovative products and ideas than homogenous teams").

<sup>138</sup> See Roger Eglin, *Diversity Helps To Oil Progress at BP*, LONDON TIMES, Oct. 24, 2004, at 6 (explaining survey results by consulting company which found that among other things inclusive environments can foster innovation); see also Lynne A. Dallas, *Does Corporate Law Protect The Interests Of Shareholders And Other Stakeholders?*, 76 TUL. L. REV. 1363, 1391 (2002) (noting that group studies into background characteristics of management teams have found heterogeneous groups tend to make higher quality decisions in matters involving creative and judgmental decision making).

<sup>139</sup> See Gordon, *supra* note 136, at 1277 (explaining the access-and-legitimacy paradigm that diversity is good business because of need for employees who can effectively communicate with ethnic consumers); see also Steven A. Ramirez, *Diversity and the Boardroom*, 6 STAN. J.L. BUS. & FIN. 85, 91 (2000) (stating that as country becomes more diverse it will necessarily lead to more diverse marketplace of consumers).

<sup>140</sup> See Gordon, *supra* note 136, at 1284-85 (stating that demand-side diversity calls for matching communicator's race or ethnicity with that of consumer); see also Dallas, *supra* note 138, at 1402 (suggesting that having heterogeneous groups who actually include diverse perspectives and sets of values that the group is trying to assess can improve the group's decision making).

<sup>141</sup> See Dallas, *supra* note 138, at 1384 (explaining that diversity proposals have been made by shareholders and have received substantial shareholder support); Steven A. Ramirez, *A Flaw in the Sarbanes-Oxley Reform: Can Diversity in the Boardroom Quell Corporate Corruption?*, 77 ST. JOHN'S L. REV. 837, 847 (2003) (noting that institutional shareholders have long sought to encourage more diverse corporate boards).

<sup>142</sup> See Fields & Keys, *supra* note 3, at 7 (highlighting positive excess return of sample of 34 firms at announcement of receiving Exemplary Voluntary Efforts Award for promoting diversity versus the significant negative excess return of firms found liable for discrimination); see also Roy S. Johnson, *The 50 Best Companies for Asians, Blacks & Hispanics*, FORTUNE, August 3, 1998, at 94 (finding that companies included on list for commitment to diversity continue to profit).

business' rationale also cite that cultural diversity results in organizational effectiveness.<sup>143</sup>

## 2. The Social Justice Rationale

In Justice Harlan's landmark dissent from the majority's holding (now, of course, overruled) in *Plessy v. Ferguson*,<sup>144</sup> which authorized separate but equal transportation, he emphasized that classifications in the law based on race are unconstitutional because "[o]ur Constitution is color-blind."<sup>145</sup> Notably, diversity was not justified on economic grounds here. Justice Harlan opposed racial discrimination in the law because he considered it morally wrong and socially unjust.<sup>146</sup> This justification for diversity in business is known as the social justice rationale.<sup>147</sup> According to this rationale, diversity is important because women and minorities deserve to be treated fairly and equally to their white male counterparts in corporate employment.<sup>148</sup> Moreover, this rationale suggests that when women and minorities who have a more personal understanding of discrimination are integrated into the corporate work force,

<sup>143</sup> See Deborah Ramirez and Jana Rumminger, *Civil Right in the New Decade: Race, Culture, and the New Diversity in the New Millennium*, 31 CUMB. L. REV. 481, 520 (2001/02) (noting that "[d]iversity is critical to managing a well-functioning workforce, to devising creative problems solving and solutions, to eliminating racial hostility, maximizing employee potential and to achieving institutional missions of business"); see also Ramirez, *supra* note 141, at 94 (explaining that when companies recognize the importance of fostering an environment of tolerance and sensitivity it can be a powerful way to increase organizational effectiveness).

<sup>144</sup> 163 U.S. 537 (1896), *overruled by* *Brown v. Board of Educ.*, 347 U.S. 483, 494 (1954).

<sup>145</sup> *Plessy v. Ferguson*, 163 U.S. 537, 559 (1896) (Harlan, J., dissenting) (explaining why the policy of "separate but equal" treatment of minorities should be abolished).

<sup>146</sup> See *id.* at 559 (stating all citizens are equal in eyes of law, regardless of race); see also William J. Brennan, Jr., *In Defense of Dissents*, 37 HASTINGS L.J. 427, 431 (1986) (discussing Justice Harlan's view that all citizens of United States are entitled to universal civil freedom).

<sup>147</sup> See Wilkins, *supra* note 113, at 1599–1600 (explaining that social justice rationale for diversity is based on idea that inclusion of racial and ethnic minorities in legal profession preserves integrity and fairness of our legal system); see also Carl G. Cooper, *Diversity: Denied, Deferred or Preferred*, 107 W. VA. L. REV. 685, 688–90 (2005) (outlining moral case for diversity).

<sup>148</sup> See Wilkins, *supra* note 113, at 1600 (explaining success of black lawyers in corporate law firms is a matter of social justice because it is "an integral part of ensuring that blacks have access to every aspect of American economic, social, and political life"); see also Robert Brookins, *Mixed-Motives, Title VII, and Removing Sexism from Employment: The Reality and the Rhetoric*, 59 ALB. L. REV. 1, 39–40 (1995) (theorizing gender discrimination has impeded women's professional development and thus deprived society of benefits of women's creativity and insight).

especially at the top levels of corporate employment, the promotion of social responsibility is more likely.<sup>149</sup>

Studies show that employees generally seek to experience three things in their work: equity, achievement, and a sense of camaraderie.<sup>150</sup> Of these three components, equity, the feeling of being treated justly, is most critical.<sup>151</sup> Not only do employees who are justly treated perform better for the business, they also benefit individually through psychological and emotional satisfaction.<sup>152</sup>

Anecdotal evidence supports the idea that diverse directors, executives, and employers are more likely to promote corporate diversity and social justice.<sup>153</sup> For example, Laura Liswood, a senior adviser and former managing partner at Goldman Sachs and head of the Council of Women World Leaders at Harvard's Kennedy School, states that the groups that dominate in corporate America (usually white men) "tend to think the system is meritocratic, and that it works correctly, and that if changes are needed, they're minor,"<sup>154</sup> while, in the exact same organization, women and minorities believe the opposite.<sup>155</sup> On the other hand, some of the most successful African Americans in

<sup>149</sup> See Wilkins, *supra* note 113, at 1599 (stating diversity in legal profession creates inclusive legal system that better represents and protects rights of all ethnic and racial groups in population); see also Steven Ramirez, *supra* note 14, at 119 (explaining women and minorities are much more attuned to diversity issues and can make productive changes in senior management).

<sup>150</sup> See Eglin, *supra* note 138, at 6 (citing Sirota Consulting Survey that determined these needs); see also Quentin Reade, *Diversity, PERSONNEL TODAY*, April 20, 2004, at 4 (listing these three needs that all employees seek).

<sup>151</sup> See Eglin, *supra* note 138, at 6 (stating equity is most important of three needs); see also Reade, *supra* note 150, at 6 (explaining if employees are not treated equitably, enthusiasm drops drastically).

<sup>152</sup> See Robert H. Cohen, Note, *Pay Equity: A Child of the 80s Grows Up*, 63 *FORDHAM L. REV.* 1461, 1490 (1995) (explaining major component of employee satisfaction is how fairly employees believe they are being treated in comparison with other employees); see also John Hasnas, *Ethics and the Problem of White Collar Crime*, 54 *AM. U. L. REV.* 579, 636 (2005) (citing research demonstrating that employers who are committed to goals of equity have more satisfied and dedicated employees).

<sup>153</sup> See Ramirez, *supra* note 14, at 109 (explaining how diversity in management leads to improved recruitment, retention and superior group interaction); see also Cheryl L. Wade, *Racial Discrimination and the Relationship Between the Directorial Duty of Care and Corporate Disclosure*, 63 *U. PITT. L. REV.* 389, 427 (2002) (theorizing that minority executives will improve workplace for minority workers and decrease societal racism through heightened awareness).

<sup>154</sup> See Morris et al., *supra* note 9, at 70 (suggesting a blindness to diversity issues among those with corporate control).

<sup>155</sup> See Morris et al., *supra* note 9, at 70 (explaining Liswood's theory on women and minorities); see also Wilkins, *supra* note 113, at 1595 (suggesting minority lawyers often feel trapped in certain practice areas where their race is perceived as valuable credential).

corporate America have also been among the most socially conscious and have benefited, not only their companies' bottom line, but society through diversification.<sup>156</sup> For instance, Franklin Raines, the first black CEO of a Fortune 500 company, used his status at Fannie Mae to open up new home ownership possibilities for blacks and for working-class people of all races.<sup>157</sup> Likewise, Kenneth Frazier, general counsel of Merck & Co., Inc., assisted in opening a private school for underprivileged children and was integrally involved in the pharmaceutical industry's decision to make HIV/AIDS drugs available in South Africa.<sup>158</sup>

#### IV. SPAWNING DIVERSITY INITIATIVES THROUGH MERGERS

Mergers are complex transactions that do not come accompanied with a blueprint for success.<sup>159</sup> Generally, elements of a successful merger include setting realistic goals about the companies' shared role in the marketplace (i.e., whether their products are compatible) and bringing the individual client bases together as "greater than the sum of their parts."<sup>160</sup> However, the most challenging (and most over-looked) merger-related issues are often internal. The "people" issues, specifically the combining of company cultures, workforces, and philosophies, are what most

<sup>156</sup> See Wilkins, *supra* note 113, at 1611–12 (citing examples of successful, socially conscious African Americans); see also *Mortgage Group Joins NAACP to Help Blacks Purchase Homes*, CHI. TRIB., January 22, 1999, at 6 (hereinafter *Mortgage Group*) (discussing how successful African American chairman of Fannie Mae instituted program to help minority homeowners).

<sup>157</sup> See Wilkins, *supra* note 113, at 1612 (describing social consciousness of certain successful African Americans); see also *Mortgage Group*, *supra* note 156, at 1 (describing a partnership between Fannie Mae and the NAACP spearheaded by Raines).

<sup>158</sup> See Wilkins, *supra* note 113, at 1612 (discussing Frazier's altruism); see also Vivia Chen, *Master of the Game*, MINORITY L.J., Summer 2001, at 17, 20 (describing Frazier's pro bono work and efforts in South Africa).

<sup>159</sup> See CAREY & OGDEN, *supra* note 17, at 150 (stating "[w]e advise companies involved in mergers or acquisitions to carefully assess talent on both sides before deciding on whom to place where on the new team"); see also Eleanor Fox, *The 1982 Merger Guidelines: When Economists are Kings?*, 71 CALIF. L. REV. 281, 297 (1983) (noting "[t]he attempt is not to find economic truth, which we cannot do, but to develop a consensus, which we must try to do").

<sup>160</sup> See Frater, *supra* note 124 (describing the importance of company unison in pursuit of a common goal); see also ANTHONY F. BUONO AND JAMES L. BOWDITCH, *THE HUMAN SIDE OF MERGERS AND ACQUISITIONS: MANAGING COLLISIONS BETWEEN PEOPLE, CULTURES, AND ORGANIZATIONS* 21 (Beard Books 2003) (explaining that "[a]s a way of assuring merger and acquisition compatibility, most analysts have stressed the strategic fit between the merger partners (or the acquirer and its target) and the importance of ensuring overall strategic synergy.").

times, make or break the merger.<sup>161</sup> Companies entering into mergers benefit when their philosophies and cultures are similar.<sup>162</sup>

Mergers create intense periods where teams from the two involved companies work together very closely to consider the best practices, create new policies, and restructure the workforce.<sup>163</sup> Thus, mergers present ideal opportunities for companies to start fresh with diversity initiatives.<sup>164</sup> A merger talk can be “an outstanding time to create, revamp, or refocus strategies for diversifying both corporate leadership and employees.”<sup>165</sup> On the other hand, diversity can be wholly neglected if mergers are not handled properly and progress from a diversity perspective can be placed at risk.<sup>166</sup>

#### A. *Commitment to Diversity Plus Commitment to Diversity Equals Social and Economic Success*

Reviewing the many failed and few successful mergers of the past few years shows that companies dedicated to diversity for both social and business reasons tend to leverage diversity while

<sup>161</sup> See CAREY & OGDEN, *supra* note 17, at 150 (discussing importance of having adequate personnel before effectuating merger); see also Frater, *supra* note 124 (stating that “[i]n the midst of this period of internal activity, it is critical to keep sight of people issues, including diversity, to develop a shared vision, and to convey that shared vision and commitment from the outset”).

<sup>162</sup> See CAREY & OGDEN, *supra* note 17, at 150 (noting “[i]t is important. . . to have directors whose personal backgrounds, and personal career development, have been in the key functions for this business.”); see also Frater, *supra* note 124 (discussing the benefits of having the teams from two companies involved and working close together).

<sup>163</sup> Managers and directors engage in delicate discussions about factors like business synergies, potential cost efficiencies, management compatibility, and possible management lineups, in addition to share price and stockholder reaction in the short and medium terms. The legal teams then become very active in assisting in negotiations, drafting the necessary agreements, and performing due diligence to ensure that prior to finalizing the deal. Each company understands the material risk of the other business as well as assuring that the merger will pass regulatory scrutiny with the SEC, the Federal Reserve Bank, or whatever agency has jurisdiction. See Frater, *supra* note 124. Such synergy and compatibility between two merging companies is vital for the success of the merger. See generally CAREY & OGDEN, *supra* note 17, at 47.

<sup>164</sup> See Frater, *supra* note 124 (discussing corporate restructure benefits that follow from merger or acquisition); see also CAREY & OGDEN, *supra* note 17, at 47 (supporting the idea of diversity as an important merger factor, stating “[i]f you’ve got two organizations with different cultures, you’ve got a big problem”).

<sup>165</sup> See Frater, *supra* note 124 (quoting Joan Guggenheimer, executive vice president and general counsel of Bank One Corporation before merger with JP MorganChase).

<sup>166</sup> See Frater, *supra* note 124 (noting “[t]he goal remains to have people with diverse views engaged and able to contribute toward the company’s success”); see also Buono, *supra* note 163, at 61 (stating “[t]he underlying strategic purpose of a merger or acquisition can significantly influence how the firms will be combined”).



merging, experience smooth merger negotiations regarding the cultural and philosophical aspects of the new firm, and resultantly, reap social as well as economic benefits.<sup>167</sup> By placing a strong emphasis on diversity during a merger, directors and managers send a message from the top throughout the organization that a commitment to diversity and cooperation is required from everybody.<sup>168</sup> The merger between JPMorgan Chase and Bank One represents an example of such a merger.<sup>169</sup>

When JPMorgan Chase and Bank One united in July 2004, they consciously used their merger to further their mutual commitment to diversity.<sup>170</sup> Both companies even go so far as to

<sup>167</sup> See Frater, *supra* note 124 (quoting Joan Guggenheimer on her experience with McDavid, who was also committed to diversity throughout the process, stating "Bill and I have been through many mergers before this, but in my experience this one has been extremely smooth from a people and culture standpoint"); see also CAREY & OGDEN, *supra* note 17, at 29 (emphasizing that "[c]ompanies that have achieved success in meshing cultures make it look like a systematic, easy process").

<sup>168</sup> See Frater, *supra* note 124 (discussing how company CEOs set the tone for cooperation); see also CAREY & OGDEN, *supra* note 17, at 49 (explaining the importance of having "extremely resourceful and creative leadership by the CEO of the combined organizations").

<sup>169</sup> See Frater, *supra* note 124 (stating the rationale for this particular merger was diversification). See generally Press Release, Bank One, JPMorgan Chase, Bank One Commit To Investing \$800 Billion In Communities (April 15, 2004), <http://investor.shareholder.com/jpmorganchase/press/releaseDetail.cfm?releaseid=132883> (noting both companies believe in strong corporate citizenship).

<sup>170</sup> A company with a history of valuing diversity in mergers is most likely to emphasize diversity in future mergers. See Frater, *supra* note 124. Thus, it is in the best interest of directors embarking on a merger who are committed to diversity to review its merging partner's past deals to infer compatibility on this issue. See *id.* JPMorgan Chase is an example of a company with such a history. See *id.* at 2. The company presently known as JPMorgan Chase & Co. was formed in December 2000 through a merger of JPMorgan and Chase Manhattan Corporation. See JPMorgan Chase & Co.: 2001 Catalyst Award Winner, CATALYSTWOMEN.ORG, <http://www.catalystwomen.org/award/files/winners/jpmorgan20chase.pdf> (last visited Nov. 13, 2005). From the get-go both JPMorgan and Chase Manhattan were dedicated to forging a company devoted to diversification and approached their merger "as an opportunity to create a more inclusive environment in which diversity was the key integration strategy." See *id.* The company is quoted as stating, "diversity was the cornerstone of the company's success." *Id.* Prior to its merger with JPMorgan, 20% of Chase's corporate officers were women and 3 of its 17-member board of directors were women. Now the representation has increased across all levels. See *id.*

Chase approached the merger with the "merger of equals" philosophy. See *id.* The JPMorgan Chase merger is especially notable for the procedures it undertook to ensure that both company's cultures would be integrated successfully. See *id.* Chase utilized its Central Merger Office (created during its 1996 merger with Chemical), which was responsible for coordinating hundreds of merger related task teams. See *id.* The task teams offered employees from both companies the opportunity to participate in the merger process. See *id.* To ensure a clear and open process in people selection, competency-based criteria were selected and communicated to all managers and employees. See *id.* Chase also created a corporate diversity council made up of members of Chase' senior management team which establishes the diversity agenda for the company. See *id.*

state that a “large part of the rationale for [their] particular merger . . . was diversification.”<sup>171</sup>

After realizing that they were compatible business-wise during early merger talks, both teams realized they shared a common focus on “people issues” and, most importantly, diversity.<sup>172</sup> Throughout the merger process, both companies took advantage of the time they spent working together.<sup>173</sup> JPMorgan Chase leveraged its prior practice of leadership training in order to ensure that the culture of the new firm was aligned with its mission to “value and promote diversity”<sup>174</sup> and both firms strengthened their already deeply-rooted supplier diversity practices.<sup>175</sup>

JPMorgan Chase and Bank One emphasize that communication of their shared vision with employees was integral to their merger’s success.<sup>176</sup> They put the diversity initiatives on the agenda of their first global staff meeting, enlisted support of attorneys in furthering supplier diversity goals, urged the entire staff to become active on their merged Diversity Council, and communicated the importance they placed on diversity to outside law firms.<sup>177</sup> While JPMorgan Chase and

<sup>171</sup> See Frater, *supra* note 124 (emphasizing the companies strong commitment to diversity).

<sup>172</sup> See Frater, *supra* note 124 (admitting both companies had previously had diversity on their respective agendas). See generally Press Release, J.P. Morgan Chase & Co. and Bank One Corporation to Merge (Jan. 14, 2004), <http://www.jpmorganchase.com/cm/cs?pagename=Chase/Href&urlname=jpmc/about/press/2004-01-14merger> (hereinafter *JPMorgan Chase Merger*) (stating the merger makes tremendous sense operationally).

<sup>173</sup> See Frater, *supra* note 124 (stating working together gives companies an opportunity to get to know each other). See generally *JPMorgan Chase Merger*, *supra* note 172, at 2 (emphasizing looking forward to working with each other to bring unique benefits to the constituents).

<sup>174</sup> See Frater, *supra* note 124 (articulating several operating principals in order to ensure the companies were culturally aligned). See generally *JPMorgan Chase Merger*, *supra* note 174, at 2 (noting both companies’ strong commitment to community development and philanthropy).

<sup>175</sup> See Frater, *supra* note 124 (expanding diversity programs to vendors such as law firms). See generally April W. Klimley, *To Compete During Economic Uncertainty, Minority Suppliers Must Network, Form Alliances and Conquer the Internet*, BLACK ENTERPRISE, June 2001, at 291 (noting that JPMorgan Chase has sought to increase supplier diversity at all levels).

<sup>176</sup> See Frater, *supra* note 124 (suggesting a notice sent to employees about the company’s commitment to diversity was the first communication of the merger). See generally *JPMorgan Chase Merger*, *supra* note 174, at 2 (noting the intense focus on management).

<sup>177</sup> See Frater, *supra* note 124 (noting importance of diversity to outside law firms). See generally Press Release, Bank One, Bank One Names Joan Guggenheimer Chief Legal Officer (April 9, 2003), <http://investor.shareholder.com/jpmorganchase/press/>

Bank One both admit to initially instituting diversity programs to address employee needs expressed in polls and surveys, they now realize that their commitment to diversity has turned out to be beneficial for general good management.<sup>178</sup>

Making diversity a key issue in a merger is more difficult when the companies have philosophical and managerial differences.<sup>179</sup> For instance, when Time-Warner merged with AOL, both companies had diversity as a goal from the outset; yet, management needed to adapt to the concept.<sup>180</sup> Each of Time Warner's many divisions had different traditions toward diversity and all lacked sustained focus.<sup>181</sup> However, the companies used the restructuring that flowed from the merger as an opportunity to implement diversity initiatives and involve all participants, management, employees and outside vendors in the process.<sup>182</sup>

The new firm garnered ideas and developed practices from a group of senior corporate managers, outside executives, and diversity consultants.<sup>183</sup> It created a diversity council to

releasedetail.cfm?releaseid=106029 (commenting Guggenheimer was head of Diversity for Smith Barney).

<sup>178</sup> See Frater, *supra* note 124 (suggesting promotion of diversity actually makes for better management). See generally *JPMorgan Chase Merger*, *supra* note 174, at 2 (stating firms' will select the best practices from each institution and implement them).

<sup>179</sup> See Frater, *supra* note 124 (noting "it was very clear from the outset that diversity would not get lost in the shuffle as a priority in the new company"). See generally Press Release, Tom Baxter, President of Time Warner Cable; Steve White, SVP of AT&T Broadband (Atlanta Region); and Art Torres, President of the Walter Kaith Foundation Testify During the FCC's En Banc Hearing on Equal Employment Opportunity (EEO) Rules (June 24, 2002), <http://www.ncta.com/press/press.cfm?PRid=277&showArticles=ok> (hereinafter *FCC En Banc Hearing*) (commenting that the Diversity Counsel was set up to share in experiences and learn how to diversify the employee base).

<sup>180</sup> See Frater, *supra* note 124 (noting new executive vice president faced managerial differences first day of work). See generally *FCC En Banc Hearing*, *supra* note 179, at 1 (noting diverse workforce is not just social goal).

<sup>181</sup> See Frater, *supra* note 124 (discussing how Time Warner possessed a "strong decentralized management structure, which came from a different tradition, making the merger with American Online increasingly difficult). See generally Sallie Hofmeister, *Consensus-Building Skills Help Parsons Land Top Job*, L.A. TIMES, Dec. 7, 2001, § 3, at 1 (noting how, after AOL-Time Warner merger, it became even more important to focus on issues of diversity).

<sup>182</sup> See Frater, *supra* note 124 (explaining how internally, companies like Time Warner "benefit when their philosophies and cultures are similar" and that "legal issues associated with a merger are significant, and present a real challenge for corporate legal teams"); see also Hofmeister, *supra* note 183, at 1 (noting Time Warner will become a "model for diversity in corporate America").

<sup>183</sup> See Frater, *supra* note 124 (stating how object of the plan was not only to "garner new ideas from each division," but to implement a companywide policy "proven to work"); see also Mike Robuck, *SCTE in Step with Diversity Week*, CT PIPELINE, Sept. 20, 2005, at

specifically formalize and advance diversity plans.<sup>184</sup> Time Warner mandated that executives interview diverse candidates and undergo performance reviews.<sup>185</sup> In terms of the bottom-line, Time Warner held each of its CEO's accountable for diversity in their annual goals, tying a portion of their bonuses to that success.<sup>186</sup> The newly merged firm now also requires supplier diversity ensuring that a percentage of vendors are women and minority-owned enterprises.<sup>187</sup>

### *B. Ignoring Diversity in Mergers Compounds Problems for Women and Minorities*

When diversity is not valued by merging companies and is not emphasized as an important issue during the merger process, the end result can be disastrous for women and minorities. In 2002, a federal district judge approved a \$35 million settlement to be paid by Rent-a-Center to resolve a class action sex discrimination lawsuit.<sup>188</sup> The settlement covered over 5,300 women.<sup>189</sup> The

40 (noting that CEO of Time Warner, Glenn Britt, said that diversity "isn't a short term initiative; it's a long-term process and we support that").

<sup>184</sup> See Frater, *supra* note 124 (discussing that diversity council's goal was "to formalize and advance diversity and an action plan with metrics that were unique to [each] division"); see also Tom Baxter, Opening Comments, En Bank Hearing on Broadcast and Cable Equal Employment Opportunity Rules (June 24, 2002), <http://www.fcc.gov/realaudio/tr062402.txt> (noting that diversity council was created so that each division of the parent company could "share experiences and success stories in terms of seeking greater diversity in our employee base, management, and third-party business relationships").

<sup>185</sup> See Frater, *supra* note 124 (highlighting Time Warner's mandatory requirements that other companies did not have including, but not limited to, performance reviews); see also Baxter, *supra* note 184 (discussing Time Warner's active recruitment at local colleges and universities, to look for new talent and develop "people of color and women as part of that group").

<sup>186</sup> See Frater, *supra* note 124 (noting that Time Warner looked to "attack diversity on a comprehensive strategy: supplier, work force, target markets, content, philanthropy, and targeted investments"). See generally Baxter, *supra* note 184 (discussing how Time Warner has tried to diversify their employee base by providing internships, community outreach programs, and specialized training programs for minorities and women).

<sup>187</sup> See Frater, *supra* note 124 (noting that "tracking dollars and compensating people for keeping diversity goals on the front burner can only go so far" and that management must understand and believe in the benefits of diversity in order to see a continued improvement); see also Baxter, *supra* note 184 (discussing how Time Warner stresses importance of diversity with regard to its suppliers and business partners and how company has managed to contract with minority-owned contractors and suppliers over 10% of the time).

<sup>188</sup> See Carrie Mason-Draffen, *Sex Discrimination Settlements*, NEWSDAY, Jul. 13, 2004, at A5. There have been a number of class action sex discrimination lawsuits over last ten years against notable companies including Morgan Stanley, Pacific Bell/Nevada Bell, and Mitsubishi Motors Corp. See Lynn Y. Bruner, *Court Gives Final Approval to \$47*

plaintiffs' major claim was that, in 1998, when Rent-a-Center was acquired by Renter's Choice<sup>190</sup>, a notoriously sexist and male-dominated organization, Rent-a-Center's female employees were rapidly purged from the new firm, job requirements were made more stringent to prevent women from being hired, and remaining female employees were grossly mistreated.<sup>191</sup>

Before the acquisition, Renter's Choice had a "systematic, top-down corporate culture that drove away female employees."<sup>192</sup> Its CEO, Ernie Talley, had been overheard stating that "women belonged in the kitchen, not in the rent-to-own business."<sup>193</sup> This attitude was reflected at every level of the company.<sup>194</sup> To name but a few of Rent-a-Center's discriminatory practices, women were subjected to sexual and derisive comments, work requirements were changed in an effort to induce female

*Million Settlement in Sex Discrimination Suits Against Rent-A-Center By EEOC and Private Plaintiffs*, Oct. 4, 2002, <http://www.eeoc.gov/press/10-4-02.html>.

<sup>189</sup> See Geri L. Dreiling, *Past Due: A Federal Judge Forces the Boys of Rent-A-Center to Clean Up Their Bad Behavior*, KANSAS CITY PITCH WEEKLY, May 9, 2002, at Cover (describing how, as per settlement agreement, Rent-A-Center agreed to fill ten percent of job vacancies during the first fifteen months following settlement with women who had been fired and agreed to create a human resources department); see also Bruner, *supra* note 188 (noting soon after Judge David Herndon approved initial settlement offer, 26,728 claim forms were sent to women who were currently employed by Rent-A-Center, or worked there in past, and also to women who were known to have applied for work but were rejected for hire).

<sup>190</sup> See Dreiling, *supra* note 189 (stating acquisition of Rent-a-Center by Renter's Choice created largest rent-to-own company in America); see also Bruner, *supra* note 188 (noting Rent-A-Center was given a December 2, 2002 deadline to transfer settlement funds that would be disbursed to women who claimed they were fired or forced out of the company after the company was acquired by Renter's Choice, four years prior).

<sup>191</sup> See Dreiling, *supra* note 189, at 1 (noting women were forced to clean bathrooms, forced to lift 75 pounds as a prerequisite to employment, and women's employment applications were destroyed by management); see also Robert Grossman, *Events at Rent-A-Center Prove That When Employers Don't Respect HR Today, They'll Pay Tomorrow*, SOCIETY FOR HUMAN RESOURCE MANAGEMENT ONLINE (2002), <http://www.shrm.org/hr/magazine/articles/0802/0802covstory.asp> (describing company as being unprofessional in a number of ways, such as the "good old boys" drinking and having go-go dancers perform on stage for entertainment purposes).

<sup>192</sup> See Dreiling, *supra* note 189 (stating attitude of discrimination proved costly for Rent-A-Center as large class action discrimination suits were brought against them, similar to other companies such as Mitsubishi, Shoney's, State Farm, and Home Depot); see also Grossman, *supra* note 191 (describing how district managers would often go to stores in their district operated by males and tell them how to improve their business, but did not offer the same advice to female managers).

<sup>193</sup> See Dreiling, *supra* note 189 (describing details of Rent-a-Center class-action settlement).

<sup>194</sup> See *Wilfong v. Rent-a-Center*, No. 00-CV-0680-DRH, 2001 U.S. Dist. LEXIS 22718, at \*8, 17 (S.D.Ill. Dec. 27, 2001) (commenting on enforcement of company-wide policy of intentional sexual discrimination that is spelled-out by company's top executives and followed at every level of the company); see also Dreiling, *supra* note 189 (noting such).

employees to quit and to keep women from applying, women who complained about boorish or offensive behavior were ignored or punished, and pregnant employees were fired.<sup>195</sup>

On the other hand, the pre-acquisition Rent-a-Center was considered a “good place to work” by female employees.<sup>196</sup> In their class action sex discrimination suit, female employees of Rent-a-Center emphasized that the company’s culture drastically changed after it was purchased by Renter’s Choice.<sup>197</sup>

Renter’s Choice’s management grabbed the reigns of the new firm; they immediately increased the lifting requirement for store employees from 50 pounds to 75 pounds so to disadvantage potential female applicants and encourage female employees to quit,<sup>198</sup> male higher-ups sexually harassed the female employees, managers were criticized for sending female candidates to take management tests, pregnant women were fired on the spot, and male coworkers engaged in “base, crude, and abusive” behavior.<sup>199</sup> Before the acquisition, Rent-a-Center’s workforce was 20.9 percent female, whereas only 1.8 percent of Renter’s Choice’s employees were women.<sup>200</sup> In only two years after Rent-a-Center was acquired by Renter’s Choice, the proportion of

<sup>195</sup> See *Wilfong*, 2001 U.S. Dist. LEXIS 22718, at \*24 (discussing the various claims by the plaintiffs of sexual harassment, pregnancy discrimination, demotion and unequal working conditions); see also Dreiling, *supra* note 189 (describing some of the ways in which atmosphere of Rent-a-Center spawned harassing environment).

<sup>196</sup> See Dreiling, *supra* note 189 (describing conditions at Rent-a-Center before acquisition).

<sup>197</sup> See *Wilfong*, 2001 U.S. Dist. LEXIS 22718, at \*4 (noting that post-acquisition Rent-a-Center discriminated against female employees at various stages of their employment including hiring process); Dreiling, *supra* note 189 (referring to the management of Renter’s Choice as the “good ol’ boys from Texas”).

<sup>198</sup> See Dreiling, *supra* note 189 (discussing how managers were ordered to send female employees out to make deliveries and pickups alone so that they would inevitably perform poorly according to new requirements); see also Robert Goodrich, *Federal Judge Approves Rent-a-Center’s \$47 Million Settlement of Sex Bias Suit*, ST. LOUIS POST-DISPATCH, October 5, 2002, at 10 (noting that women were asked to lift furniture and appliances weighing up to 75 pounds).

<sup>199</sup> See *Wilfong*, 2001 U.S. Dist. LEXIS 22718, at \*10, n.4 (delineating several offensive statements made by officers and directors of Rent-a-Center to female employees, such as “[y]ou were fired because you’re a woman.”); see also Dreiling, *supra* note 189 (citing an example of such behavior where male assistant manager grabbed female assistant manager’s buttocks).

<sup>200</sup> See *Wilfong v. Rent-a-Center*, No. 00-CV-0680-DRH, 2001 U.S. Dist. LEXIS 22718, at \*11 (S.D.Ill. Dec. 27, 2001) (comparing almost 50% decrease in female employment with the continual increase in male employment in years immediately following acquisition); see also Dreiling, *supra* note 189 (referring to Talley’s companies as an “empire”).

women in the combined workforce had dropped to 8.5 percent.<sup>201</sup> About half the women who had been working for Renter's Choice were gone.<sup>202</sup> The disparity between male and female employees was similar at the company's top levels. All seven vice presidents were men, all 45 regional directors were men, 265 men and 7 women held the position of market manager, and 30 men and just 2 women were service managers.<sup>203</sup> In addition, the new firm had an all-male board of directors.<sup>204</sup>

While corporate culture clashes typically follow when businesses merge, the female ex-Rent-a-Center employees who filed the class action defined the attitude of the new regime as "shocking."<sup>205</sup> Just five months after the acquisition, employees of the new company called it a "downright hostile place for women."<sup>206</sup> Women who had devoted decades to Rent-a-Center were forced to leave or were fired, regardless of job performance.<sup>207</sup> Female employees were sexually harassed on a daily basis, and because the new company, at the behest of

<sup>201</sup> See *Wilfong*, 2001 U.S. Dist. LEXIS 22718, at \*11 (noting that within two years after acquisition, number of female employees had decreased from 2,092 to 1,151); see also Dreiling, *supra* note 189 (highlighting that many women were fired while others felt they had to quit to escape offensive work environment).

<sup>202</sup> See *Wilfong*, 2001 U.S. Dist. LEXIS 22718, at \*11 (citing Talley's directive to "get rid of" women in any way possible as plausible explanation for the drop in female employment); see also Dreiling, *supra* note 189 (stating that as female population was drastically declining, "one regional manager urged his store managers in a memo to continue to hire gents").

<sup>203</sup> See *Wilfong*, 2001 US Dist. Lexis 22718, at \*13 (emphasizing fact that women were denied promotions at significantly higher rates than similarly situated male employees); see also Dreiling, *supra* note 189 (quoting company newsletter, *Rental Times*, the cover of which featured a group photo of Rent-a-Center's regional directors, all of whom were men, and the headline of the article read "Meet the 'Suits' Who Try to Motivate Us").

<sup>204</sup> See *Gender Bias Dispute Settled*, ST. PETERSBURG TIMES (Fla.), March 8, 2002, at 5E (explaining that, as part of settlement, Rent-A-Center must create human resources department and seek women for company's all-male board of directors); see also Dreiling, *supra* note 189 (noting that Rent-a-Center was required to find women for its board of directors).

<sup>205</sup> See Dreiling, *supra* note 189 (describing offensive post-merger conditions); Michael Selmi, *Sex Discrimination in the Nineties, Seventies Style: Case Studies in the Preservation of Male Workplace Norms*, 9 EMPL. RTS. & EMPLOY. POL'Y J. 1, 40 (2005) (characterizing discriminatory behavior at Rent-A-Center as "extreme").

<sup>206</sup> See Dreiling, *supra* note 189 (noting employee feelings post-merger); see also Selmi, *supra* note 205, at 40 (quoting Rent-A-Center regional director who stated, "women should be home taking care of their husbands and children, chained to the stove, not working in my store").

<sup>207</sup> See Dreiling, *supra* note 189 (summarizing lead plaintiff Wilfong's story); *Sex Discrimination Victims' Counsel Achieve Changes In Company's Personnel Policies*, LAW REPORTER, Dec. 2002, [http://www.findarticles.com/p/articles/mi\\_qa3898/is200212/ain9153610](http://www.findarticles.com/p/articles/mi_qa3898/is200212/ain9153610) (detailing Wilfong's post-merger ordeal).

Renter's Choice, axed Rent-a-Center's human resource department, the women had virtually nowhere to voice their complaints.<sup>208</sup> One Rent-a-Center tradition the new management did keep was their annual convention for top managers, held in Las Vegas, complete with entertainment including scantily clad cheerleaders and outings to strip clubs.<sup>209</sup>

The plaintiffs in the class action sex discrimination suit against Rent-a-Center highlight that the discrimination and harassment they endured did not occur until after Rent-a-Center was acquired by Renter's Choice.<sup>210</sup> The suit also alleged that the discrimination "emanate[d] from top management."<sup>211</sup>

As part of the settlement agreement, the new Rent-a-Center, in addition to paying out \$47 million, was forced to institute human resource and diversity programs.<sup>212</sup> It agreed to fill 10 percent of job vacancies during the first fifteen months following the settlement with women who had been fired, to create a human resource department, and to file quarterly reports for the following four years describing the company's steps to end discrimination, detailing complaints and providing statistical information.<sup>213</sup> Any discrimination complaints will now be decided by a court-appointed special master.<sup>214</sup> While it vowed at

<sup>208</sup> The new firm dismantled the human resources department. See *Wilfong v. Rent-A-Center, Inc.*, No. 00-CV-0680-DRH, 2001 U.S. Dist. LEXIS 22718, at \*14, n.6 (S.D.Ill. Dec. 27, 2001). It created a "manager of coworker relations" to handle employee complaints, but the position was held by a male who consistently sided with the male managers when female employees brought complaints. See Dreiling, *supra* note 189.

<sup>209</sup> See Dreiling, *supra* note 189 (describing Rent-A-Center's annual convention); Geri L. Dreiling, *Nasty Boys: The Women Screwed by Rent-A-Center are Threatening to Take the Company to the Cleaners. But Ernie Talley and the Rest of his Texas Bubbas are Trying to Have the Last Laugh*, RIVERFRONT TIMES (Mo.), Feb. 27, 2002 (comparing Rent-A-Center's annual convention to fraternity parties).

<sup>210</sup> See Dreiling, *supra* note 189 (noting harassment of female employees began after Talley's purchase of Rent-A-Center); see also *Wilfong*, 2001 U.S. Dist. LEXIS 22718, at \*11 (noting drops in employment of women after Talley's acquisition).

<sup>211</sup> Dreiling, *supra* note 189 (describing details of suit); see *Wilfong*, 2001 U.S. Dist. LEXIS 22718, at \*9-10 (noting statements like "women don't belong in rent-to-own" and "get rid of women any way you can" reflect company policy when made by top executive, as they were at Rent-A-Center).

<sup>212</sup> See *Wilfong & EEOC v. Rent-a-Center, Inc., WAGE - WOMEN ARE GETTING EVEN*, <http://www.wageproject.org/sexdiscDB/sexdiscDB.php?mode=full&id=310> (last visited Oct. 11, 2005) (hereinafter *Wilfong & EEOC*) (summarizing terms of settlement); Dreiling, *supra* note 189 (describing pending settlement which has now been finalized).

<sup>213</sup> See *Wilfong & EEOC*, *supra* note 212 (detailing agreed to settlement); Dreiling, *supra* note 189 (describing conditions of settlement).

<sup>214</sup> See Dreiling, *supra* note 189 (noting settlement clause requiring discrimination complaints to be decided "by a court-appointed special master"); Geri L. Dreiling, *Hell Hath No Fury: The Good Ol' Boys at Rent-A-Center Raise a White Flag-They're Licked*,



the time of the settlement to increase the number of women on its board, as of 2005, only one out of Rent-a-Center's eight board members is female.<sup>215</sup>

### C. Using Mergers to Change Face and Build Diversity

The union of BP and Amoco provides an example of a merger which brought about positive reform in BP's commitment to diversity.<sup>216</sup> Historically, BP, a worldwide petroleum empire, has been known as a "long bastion of Anglo-Saxon males."<sup>217</sup> Until recently, BP had never employed a women or foreigner in a senior position and diversity was an issue left relatively undiscussed.<sup>218</sup> While BP's world-wide expansion<sup>219</sup> resulted in male and female employees of almost every nationality joining BP's work force,<sup>220</sup> the company did not develop a commitment to diversification or inclusion of female and minority employees. Diversity was merely forced upon it and "left to chance."<sup>221</sup>

DALLAS OBSERVER, Mar. 14, 2002, [http://www.dallasobserver.com/Issues/2002-03-14/news/news2\\_print.html](http://www.dallasobserver.com/Issues/2002-03-14/news/news2_print.html) (noting court-appointed special master clause).

<sup>215</sup> See *Corporate Governance*, RENT-A-CENTER, <http://www.corporate-ir.net/ireye/irsite.zhtml?ticker=rcii&script=2260> (last visited Nov. 13, 2005) (listing Mary Elizabeth Burton as Rent-A-Center's only female board member); see also *Executive Bios*, RENT-A-CENTER, <http://www6.rentacenter.com/site/page/pg4301.html> (last visited January 17, 2006) (listing five male and zero female Rent-A-Center executives).

<sup>216</sup> See Eglin, *supra* note 138, at 6 (noting that BP took more proactive approach to diversity following merger with Amoco); see also *Diversity*, BP GLOBAL, <http://www.bp.com/sectiongenericarticle.do?categoryId=9002292&contentId=3072071> (last visited January 17, 2006) (noting that seventy percent of BP's employees find their work environment one where people from different backgrounds can succeed and seventy-six percent feel protected against harassment).

<sup>217</sup> Eglin, *supra* note 138, at 6 (describing history of BP).

<sup>218</sup> See Eglin, *supra* note 138, at 6 (asserting that, in the past, any mention of concepts of diversity or inclusion to white, male Anglo-Saxon management would lead invariably to looks of incomprehension); cf. *Long Road Into Top Posts for Women*, ENERGY DAY, Apr. 25, 2002, at 5 (hereinafter *Long Road*) (noting that BP is one of three major oil companies that are members of Opportunity Now, a pan-industry organization which campaigns to increase women's participation in workforce at all levels).

<sup>219</sup> See Eglin, *supra* note 138, at 6 (discussing BP's current status as biggest single energy investor in Russia and China); Alan F. White, *Organizational Transformation at BP: An Interview with Chairman and CEO Robert Horton*; *British Petroleum*, HUM. RESOURCE PLAN., Feb. 1992, at 3 (quoting former BP Chairman as saying that BP's organizational goal is to be "Most Successful Oil Company in the World").

<sup>220</sup> See Eglin, *supra* note 138, at 6 (positing that BP's 110,000 employee workforce includes members from almost every nationality, culture, ethnic background, and religion); *Long Road*, *supra* note 218, at 5 (reporting that BP increased the number of female executives in its senior leadership group by 40% from 2000 to 2002).

<sup>221</sup> Eglin, *supra* note 138, at 6 (noting historical lack of import placed on diversity by BP).

BP soon learned, however, that if the company was going to have a productive workforce and be successful in the marketplace, diversity and inclusion would have to be managed.<sup>222</sup> BP used its merger with Amoco, a company already taking diversity seriously, to reevaluate its attitude and commitment toward diversity.

The merger with Amoco led BP to the creation of a new executive position at the company: Vice President of Diversity and Inclusion.<sup>223</sup> Notably, BP hired a woman to fill this job. BP recognized that its approach of hiring a diverse group of people and letting diversity matters sort themselves out was ineffective and barriers to female and minority advancement remained.<sup>224</sup> As a result, BP has initiated a new policy that not only emphasizes diversity, but inclusion as well. Patti Berringer, BP's Vice President of Diversity and Inclusion, lists many reasons for BP's new commitment to diversity that include the economic, social, and ethical justifications.<sup>225</sup> By creating a "depth of understanding" and "willingness to come to terms with [the diversity] issue" throughout its merger with Amoco, BP has been

<sup>222</sup> See Eglin, *supra* note 138, at 6 (positing that, although BP had originally rested on erroneous ideology that employing diverse group of people would naturally lead to inclusive environment, it has now recognized need for managing its diversity and inclusion affairs); Judith S. Lederman, *In Business; Managing Company Morale*, N.Y. TIMES, Mar. 31, 2002, § 14WC, at 3 (reporting that BP commissioned workplace study soon after its merger with Amoco, revealing that employees had fewer accidents on job when there was better employee satisfaction, and forcing recognition that management had to get closer to its employees).

<sup>223</sup> See Eglin, *supra* note 138, at 6 (noting that, in many years of reporting on BP's affairs, the author had never interviewed a woman because none was ever employed in senior position); see also Ross Wigham, *BP Puts Diversity on Global Agenda*, PERSONNEL TODAY, Aug. 6, 2002, at 7 (stating presence of women in BP's senior management team is minimal, with only five females in four hundred).

<sup>224</sup> See Eglin, *supra* note 138, at 6 (discussing BP's recognition that their multinational employees would need to feel they were being treated with dignity and respect, before diversity would appear on top rungs of corporate ladder); Sarah Murray, *Case Study: BP: Different Strokes for Different Folks*, FIN. TIMES (London), May 10, 2004, at 5 (quoting Patti Berringer as saying that "[i]t isn't enough to put people together. It's about creating mutual understanding, and one of the keys is to look for macro interventions that create micro understanding").

<sup>225</sup> Sirota Consulting was hired by BP soon after its merger with Amoco to conduct a survey of employee attitudes. Sirota has suggested that BP will benefit from its new dedication to diversity and inclusion because (1) heterogeneous teams of employees produce optimum results, (2) diversity adds value to the organization in terms of diverse ideas, viewpoints, talent and experiences; (3) diversity fosters innovation; and (4) diversity and inclusion creates a safer work environment, encourages employee engagement, increases commitment and pride, boosts customer satisfaction, and drives financial performance. See Eglin, *supra* note 138, at 6; Lederman, *supra* note 222, at 3.

able to change its face.<sup>226</sup> While it is still a male-dominated organization, more women and people of color are now being recruited and promoted to senior jobs.<sup>227</sup>

In consideration of its global employees and consumers, BP felt a need to change its image. However, some corporations find establishing a commitment to diversity a more urgent matter. An example of this is R.R. Donnelley & Sons Co., a printing company challenged, over the years, by numerous age and race discrimination suits.<sup>228</sup> While most of the suits were, typically, settled without admission of wrongdoing, the company's reputation was severely tarnished.<sup>229</sup> Donnelley used its merger with Moore Wallace Inc., which created the largest printing company in North America, to revitalize the company's diversity initiatives.<sup>230</sup> Moore's CEO, Mark Angelson, who took over Donnelley, strongly stressed diversity as a "fundamental precept" to which he was "deeply committed."<sup>231</sup> Since the merger it has made an effort to recruit women and minorities for upper level positions.<sup>232</sup> Currently, it has 2 women and 2 African-Americans

<sup>226</sup> Eglin, *supra* note 138, at 6 (quoting Patti Bellinger, Vice President of Diversity and Inclusion for BP).

<sup>227</sup> See Eglin, *supra* note 138, at 6 (reporting that BP's Vice President of Diversity and Inclusion, Patti Bellinger, was excited about depth of BP's understanding and willingness to come to terms with its diversity issue); see also *Top Women in Energy Sector Honored for Trailblazing, Industry Achievements*, BUS. WIRE, Apr. 30, 2004 (compiling a list of female executives in the energy industry, including several senior officers at BP and Amoco).

<sup>228</sup> See Barbara Rose, *Donnelly's New Chief Emphasizes Diversity*, CHI. TRIB., Dec. 6, 2003, at 1 (noting suits due to 1993 plant closings); see also Francine Knowles, *What Ruling Means to Workers, Employers*, CHI. SUN-TIMES, Mar. 31, 2005, at 55 (identifying race discrimination suits brought against R.R. Donnelly & Sons Co. in the 1990s as "high profile").

<sup>229</sup> See Rose, *supra* note 228, at 1 (mentioning how Donnelly "was plagued for years by age-and race-discrimination suits), see also Ronald E. Yates, *Donnelley Takes to a Challenge Like Ink to Paper*, CHI. TRIB., Dec. 22, 1996, at 1 (discussing \$500 million class action racial discrimination suit against R.R. Donnelley & Sons Co. which alleged "intentional and outrageous race discrimination").

<sup>230</sup> See Eric Herman, *Donnelley Names Exec to Improve Minority Hiring*, CHI. SUN-TIMES, Mar. 9, 2004, at 55 (discussing creation of executive position at Donnelley aimed at "improving minority hiring an outreach"); Rose, *supra* note 228, at 1 (reporting comments by new CEO which pledged to emphasize diversity).

<sup>231</sup> See Barbara Rose, *Diversity Labeled Priority by New Chief at Donnelley*, CHI. TRIB., Mar. 9, 2004, at 1 (noting suits due to 1993 plant closings); see also Rose, *supra* note 228, at 1 (commenting on new CEO's views that it is no longer good business to be represented solely by middle-age white males at executive meetings).

<sup>232</sup> See Rose, *supra* note 231, at 1 (reporting that new vice president of diversity, Damayanti Vasudevan, will promote diversity with "strategies for the workplace and marketplace"); Rose, *supra* note 228, at 1 (noting that in recent years Donnelley has made efforts to recruit women and minorities to stop spots).

on its 11 member board, while 7 of its 25 top executives are women and 2 are African-American.<sup>233</sup>

#### V. THE LACK OF DIRECTIONAL INCENTIVES TO PROMOTE DIVERSITY WHEN MERGING

The serious consideration and intense decision-making undertaken by boards preceding merger approval provides a valuable opportunity for directors to develop diversity efforts and implement effective diversification programs.<sup>234</sup> By emphasizing diversity during mergers, directors can strategically prevent future or potential employment discrimination lawsuits and costly settlements,<sup>235</sup> bolster their company's bottom line through more successful consumer relations and effective employee production, and further the social and moral good of employment equity. However, mergers are typically entered into by companies hoping only to expand their markets and increase their share value.<sup>236</sup> Thus, most of the merger negotiation is spent toiling over financial considerations. Due to the predominance of bottom-line issues during mergers, coupled with corporate law that fails to obligate directors to seriously consider diversity, diversity issues are typically pushed to the back-burner or left completely undiscussed.<sup>237</sup>

<sup>233</sup> See Rose, *supra* note 228, at 1 (describing current ethnic conditions at Donnelley). See generally R.R. Donnelley, *Board of Directors*, at <http://www.rrd.com/wwwRRD/Investors/CorporateGovernance/BoardofDirectors.asp> (last visited January 17, 2006) (naming all eleven directors on Donnelley's board).

<sup>234</sup> See Frater, *supra* note 124 (explaining how mergers create excellent opportunity for companies to create, revamp, or refocus strategies for diversity issues). See generally Wade, *supra* note 8, at 223 (noting that several commentators regard the American workplace as "locus for improved race relations").

<sup>235</sup> See Wade, *supra* note 153 (explaining how Texaco's and Coca-Cola's multi-million dollar racial discrimination settlements resulted in temporary losses for shareholders and potential significant harm to overall share value); see also Michelle McCann, Note, *Shareholder Proposal Rule: Cracker Barrel in Light of Texaco*, 39 B.C. L. REV. 965, 967 (1998) (noting that companies suffer pecuniary losses from actual settlements).

<sup>236</sup> See Fanto, *supra* note 49, at 273 (noting mergers are often entered into on presumption that "constituent companies can create more value together than separate"); see also Nicole Duke, Comment, *Hospital Mergers Versus Consumers: An Antitrust Analysis*, 30 U. BALT. L. REV. 75, 110 (2000) (indicating that expanding market share is one of top five reasons hospitals merge).

<sup>237</sup> See Fanto, *supra* note 49, at 333. This was also the problem during the enactment of Sarbanes-Oxley. While Sarbanes provoked serious discussion of corporate governance and would have been an ideal time to establish more ethical practices in terms of diversity, the major focus of the Act remained on financial disclosures. See Watson, *supra* note 3, at 25-29.

While this Note asserts that it is in the best interest of corporations, women, minorities, and society in general for directors to leverage diversity during mergers, it recognizes that directors are not entirely to blame for their inattention to this important issue. It is suggested that neither state corporate law nor federal securities regulations provide adequate incentives for directors to emphasize diversity in mergers.

### A. *Fundamental Flaws in Corporate Law That Prevent Adequate Diversification*

#### 1. Directors Can Satisfy Their Duty to Monitor Without Compliance Systems

As discussed above, corporate governance principles urge boards of directors to monitor their companies' compliance with law, including employment discrimination law. However, U.S. companies continue to discriminate against women and minorities.<sup>238</sup> It is asserted that this discrepancy results, in part, because the director's fiduciary duty of care does not obligate directors to prioritize diversity.

Currently, directors are not legally obligated to install compliance systems to monitor executive and employee adherence to employment discrimination law.<sup>239</sup> It appears directors are protected from personal liability so long as they can prove that they underwent a process of reasonable investigation and due deliberation before deciding whether to implement a compliance system.<sup>240</sup> This means that directors seemingly can

<sup>238</sup> See Wade, *supra* note 8, at 224 (elaborating on ineffectiveness of directorial duty to monitor); see also Alan Cowell, *Brewmaster Breaks One Tradition but Upholds Another*, N.Y. TIMES, Dec. 24, 2004, at A4 (highlighting that in response to continued discrimination in Norway the government has told companies "if women do not constitute at least 40 percent of corporate boards by July 2005, they will be required by law to hire more women as executives").

<sup>239</sup> See *In Re Caremark Int'l. Derivative Litig.*, 698 A.2d 959, 968 (Del. Ch. 1996) (finding corporate officers currently have no duty to establish monitoring systems to insure compliance with all applicable statutes and regulations). See generally Naomi Ono, *Boards Of Directors Under Fire: An Examination of Nonprofit Board Duties in the Health Care Environment*, 7 ANN. HEALTH L. 107, 124-126 (1998) (analyzing the *Caremark* case and its effect on director liability with respect to corporate compliance systems).

<sup>240</sup> See *Smith v. Van Gorkom*, 488 A.2d 858, 872 (Del. 1985) (emphasizing encouragement of protecting and promoting full and free exercise of managerial power granted to the board of directors); see also *Caremark*, 698 A.2d at 968 (stating that where director exercises good faith effort to be informed and to exercise appropriate judgment, he or she should be deemed to satisfy the duty of attention).

decide against implementing a compliance or diversity program to ensure that their workplace is discrimination-free if they find, after performing due diligence, that it would be more costly to the corporation, and therefore more detrimental to shareholder profit maximization, to install such a program than to suffer the consequences of violations of the law.

## 2. Directors Are Under No Obligation To Consider Non-Shareholder Interests

Additionally, the shareholder primacy paradigm to maximize shareholder profits, a “fundamental tenet of U.S. state corporate law,” does not mandate that directors act in the best interests of employees or of the community.<sup>241</sup> Under the current shareholder primacy model, directors are only required to consider the maximization of shareholder wealth during decision-making processes.<sup>242</sup> Thus, under current state corporate law, directors can satisfy their duty of care without considering the moral or social implications of sex or race discrimination.

## 3. Ineffectiveness of Shareholder Derivative Actions

Diversity efforts are currently viewed as providing economic benefits. Moreover, recent employment discrimination settlements have been extremely costly to companies. Thus, theoretically, courts should allow shareholders to bring derivative actions<sup>243</sup> against directors who do not implement compliance or diversity programs based on a breach their duty of

<sup>241</sup> See Gabaldon, *supra* note 4, at 835–37 (describing the share-holder primacy model as demonstration of the idea that the interests of shareholders are preferred over those of others with interests in the firm); see also Lynn A. Stout, *Bad and Not-So-Bad Arguments for Shareholder Primacy*, 75 S. CAL. L. REV. 1189, 1189 (2002) (citing Adolphe A. Berle’s belief that all powers granted to any group within corporation are at all times exercisable only for benefit of the shareholders).

<sup>242</sup> See Gabaldon, *supra* note 4, at 835–37 (defining board of directors as brain of the corporation, whose responsibilities only include the making or supervising of decisions necessary for the management of its affairs); see also Stout, *supra* note 241, at 1189 (explaining Berle’s argument for shareholder primacy and belief that corporation exists only to make money for its shareholders).

<sup>243</sup> Shareholder derivative suits provide equitable relief to shareholders who, without such judicial intervention, would lack standing because they lack direct harm. Wade, *supra* note 8, at 227; see, e.g., *Cohen v. Beneficial Indus. Loan Corp.*, 337 U.S. 541, 547–48 (1949). In such suits, shareholders’ injuries derive from harm to the corporation. Wade, *supra* note 8, at 227; see, e.g., *Eisenberg v. Flying Tiger Line, Inc.*, 451 F.2d 267, 269 (2d Cir. 1971).

care. However, courts have not ruled in favor of any plaintiffs asserting such claims to date.<sup>244</sup>

The general failure of shareholder derivative actions alleging breach of duty of care can be attributed to the procedural prerequisites of such suits embodied in state corporate codes.<sup>245</sup> First, shareholders must make a demand, in a letter to the board, that directors take corrective action or, alternatively, initiate or continue the litigation seeking to hold the corporation and wrongdoers within the company liable for misconduct.<sup>246</sup> Shareholder derivative claims seeking compensation for corporate losses resulting from board-approved settlements of several sexual harassment suits have been dismissed in the past because shareholder plaintiffs failed to make demand on the board before initiating their action.<sup>247</sup> Second, corporate boards are entitled to appoint a special litigation committee to determine whether a derivative action would be in the corporation's best interest. As such, the decision of whether or

<sup>244</sup> See Wade, *supra* note 8, at 227 (noting that “[d]erivative actions are likely to be unsuccessful when they allege duty of care breaches that cause corporate losses as a result of noncompliance with the laws that prohibit discrimination”); see, e.g. *White v. Panic*, 793 A.2d 356, 359 (Del. Ch. 2000) (noting that, in granting motion to dismiss, plaintiffs had not stated a claim on which to grant relief).

<sup>245</sup> Such corporate policies were created to limit the number of derivative suits. See Wade, *supra* note 8, at 227. One such policy is the demand requirement. See, e.g., *White*, 793 A.2d at 364.

<sup>246</sup> See *White*, 793 A.2d at 364 (explaining purpose for demand requirement is to distinguish between strike suits motivated by hope of creating leverage through prospect of expensive and time-consuming litigation and suits reflecting reasonable apprehension of director malfeasance that board cannot objectively pursue on corporation's behalf); see also Wade, *supra* note 8, at 227–28 (stating that demand requirement's purpose is to avoid waste of judicial resources by encouraging resolution of matter at issue without litigation).

<sup>247</sup> It is important to note that when the demanding corrective action from the board, or litigation, would be futile, the procedural prerequisite of demand is considered excused. *White*, 793 A.2d at 364. Demand is considered futile when directors have conflicts of interests regarding the litigation. *Id.* Many times plaintiffs will fail to make demand on the board under a mistaken belief that demand is excused if it seems that the directors cannot exercise independent discretion in deciding whether to initiate the lawsuit. *Id.* at 365.

This was the case in *White*, where the accused harasser was the CEO and Chairman of the Board. *Id.* at 358. Although there was only one inside director (who happened to be a subordinate of the CEO), each outside director on the board also owed his position to the accused harasser. Moreover, all board members were male. Despite this alarming scenario, the court ruled that demand was not excused for futility and dismissed the plaintiffs claim for failure to make demand. *Id.* at 366. The holding of this case is particularly shocking considering that the accused harasser was responsible for securing all director positions and paying each director annual retainer of \$30,000 plus a fee of \$1,000 per board meeting. *Id.*

not to initiate a lawsuit against the board of directors is, effectively, placed in the hands of actual board members.<sup>248</sup>

#### 4. Due Diligence Does Not Include Deliberation of Diversity Issues

In the context of mergers, the directors duty of care becomes even more elusive. While in *Van Gorkom*, directors were held liable for making a grossly negligent decision, the court primarily based its decision on the directors' lack of procedural due deliberation in approving the merger and the directors' failure to disclose the actual monetary value of the corporation's shares to shareholders when they submitted the merger for shareholder approval.<sup>249</sup> Thus, it seems unlikely that directors will be held liable for a breach of their duty of care when approving a merger if they perform due diligence (investigate and deliberate financial matters) and make all necessary disclosure regarding the corporation's market value to shareholders. It does not appear that directors are under any special duty to inform shareholders about the corporation's diversity efforts or lack thereof or whether the company with which it is merging values diversity.<sup>250</sup> It also does not seem that a failure on the director's part to inform shareholders about whether they plan to implement a compliance or diversity program once the corporation is merged will amount to a breach of the duty of care. So long as the shareholders have correct material financial

<sup>248</sup> See VIII DEL. CODE. ANN. § 141(c) (2005) (stating that "[t]he board of directors may, by resolution passed by a majority of the whole board, designate one or more committees, each committee to consist of one or more of the directors of the corporation."); see also Wade, *supra* note 8, at 228 (listing second requirement to shareholder derivative litigation allows board to appoint committee to determine whether such litigation would be in the corporation's best interests).

<sup>249</sup> *Smith v. Van Gorkom*, 488 A.2d 858, 874 (Del. 1985) (concluding Board of Directors did not reach informed business judgment); see Alexander Khutorsky, Note, *Coming in from the Cold: Reforming Shareholders' Appraisal Rights in Freeze-Out Transactions*, 1997 COLUM. BUS. L. REV. 133, 153-54 (1997) (describing bases for holding in *Van Gorkom*).

<sup>250</sup> See, e.g., *Van Gorkom*, 488 A.2d at 872 (emphasizing encouragement of protecting and promoting the full and free exercise of managerial power granted to the board of directors and the business judgment rule itself presumed the directors will act on informed basis and in good faith); In *Re Caremark Int'l. Derivative Litig.*, 698 A.2d 959, 968 (Del. Ch. 1996) (stating that where director exercises a good faith effort to be informed and to exercise appropriate judgment, he or she should be deemed to satisfy the duty of attention).



information, it seems directors satisfy their fiduciary duty of care in recommending a merger.<sup>251</sup>

*B. When Corporate Employment Discrimination Practices are Kept Secret, Change is Unlikely*

Like shareholder derivative actions, employment discrimination lawsuits are unlikely to put pressure on boards to consider diversity in mergers because such cases are generally extremely difficult to prove and, even when successful, are unlikely to cause the public to pressure corporations into changing their ways.<sup>252</sup> The courts that decided to certify the class-action lawsuits brought by plaintiffs against Boeing and Morgan Stanley enumerated a standard: if data on pay or job levels indicates a pattern that is “two deviations from the norm,” then there is “legal inference” that discrimination is present and a suit can proceed.<sup>253</sup> This standard is generally difficult to meet.

Furthermore, while the threat of race or sex discrimination has become one of corporate America’s worst nightmares, companies faced with such lawsuits have a strong weapon on their side. In most (multi-million dollar) settlements that resolve class-action employment discrimination lawsuits, the defendant company not only fails to admit to the discrimination but requires the plaintiffs to agree to confidentiality pacts.<sup>254</sup> These

<sup>251</sup> See VIII DEL. CODE. ANN. § 141(e) (2005) (stating that member of board is fully protected in relying in good faith on the accounts or reports made to corporation by any of its officers); see also *Van Gorkom*, 488 A.2d at 874–75 (holding that directors only had duty to inquire into suspicious and deficient financial material put forth by one of the directors in regards to possible merger).

<sup>252</sup> See Selmi, *supra* note 205, at 15 (discussing how recent securities lawsuits “describe an industry that remains resistant to change and hostile to women”); see also Antilla, *supra* note 10, at A19 (stating that “[i]ngrained cultural misconduct changes only when customers, colleagues and the public get wind of the nasty facts and companies are embarrassed”).

<sup>253</sup> Boeing’s own studies showed that its salary practices “adversely impacted women,” and “demonstrated statistically significant differences (i.e., standard deviations in excess of negative two) in pay between men and women.” See *Beck v. Boeing Co.*, No. C00-301P, 2004 U.S. Dist. LEXIS 27622, at \*13 (W.D. Wash. April 9, 2004). “The norm is generally defined as what might be expected, say, given the number of women [or people of color in the company’s] workforce.” See *Morris et al.*, *supra* note 9, at 64. *Morris* also notes that while in some cases such as Wal-Mart and Costco the discrimination is blatant, most times calculating the standard deviation can be “devilishly complex.” See *id.*

<sup>254</sup> See Jennifer Gordon, *We Make the Road by Walking: Immigrant Workers, the Workplace Project, and the Struggle for Social Change*, 30 HARV. C.R.-C.L. L. REV. 407, 440 (1995) (determining that “[e]ven when employers settle a matter with a small group of workers, they frequently require the workers to sign a binding confidentiality agreement.”); see also Antilla, *supra* note 10, at A19 (noting that Morgan Stanley’s

confidentiality pacts prohibit the plaintiffs from discussing the corporate practices of discrimination which led to the lawsuit.<sup>255</sup> Because the companies are under no duty to disclose the practices themselves, the public remains unaware of how and to what extent the large public company was discriminating (and in many cases, continues to discriminate) against its female and/or minority employees.<sup>256</sup> While the sheer volume of discrimination cases brought by employees and great expense attached to discrimination settlements hint at the seriousness of the employer's offenses, the lawsuits will lack long lasting impact on society. Likewise, investors are likely to quickly forget about the short-lived controversy unless the details of the specific acts of discrimination are allowed to penetrate the public.<sup>257</sup>

## VI. RECOMMENDATIONS FOR PROMOTING DIVERSITY THROUGH MERGERS

It is suggested that as corporate law now stands, boards of directors lack the incentives necessary to consider diversity as a major factor when deciding whether to merge with another company. It is asserted that shareholder activism, corporate governance reforms mandated by the federal government and the SEC, and the restructuring of corporate boards to include more women and minorities will facilitate the necessary analysis and attention due to diversity issues in corporate employment.

settlement included confidentiality pacts where shared documents will remain confidential to ensure that no one learns how women were treated at work).

<sup>255</sup> See Antilla, *supra* note 10, at A19 (explaining that confidentiality pacts prohibit women from disclosing discrimination statistics to anyone and that any copies of documents involving settlement were to be destroyed or returned); see also Gordon, *supra* note 254, at 440 (finding that confidentiality pacts "enable the employer to avoid correcting the underlying problem" because other workers and public are prevented from knowing about it).

<sup>256</sup> See Antilla, *supra* note 10, at A19 (suggesting that "[t]here's a long history of securities firms fighting the ensure that the public does not learn how women are treated on the job."); see also Morris et al., *supra* note 9, at 64 (concluding that traditionally, corporate America has kept secret "the way it rewards its workers, determines entry-level salaries, makes promotion decisions, and divvies up merit raises").

<sup>257</sup> While the practices are currently occurring with more frequency, the public is still not becoming aware of them because they are kept secret and, without public pressure to change, corporations probably will not act. See Antilla, *supra* note 10, at A19. Practically, "[o]ne simple solution would be for the EEOC to make public the reams of employment data that companies are required to file every year." See Morris et al., *supra* note 9, at 64.

### A. *Internal and External Corporate Governance Reforms*

It is suggested that the goals of the corporation and duties of the board of directors must be expanded to encompass notions of social responsibility in general and diversity in particular.<sup>258</sup> Directors' fiduciary duties should not only run to shareholders but also to employees and the community or society.<sup>259</sup>

While this Note proposes a progressive approach to corporate governance where directors should be obligated to consider the interests of non-shareholder stakeholders, it is also emphasized that shareholders are harmed as a result of employment discrimination lawsuits stemming from inattention to workplace diversity; stock value falls as a result of the negative publicity and large settlements paid to affected workers. While directors do not have an obligation to maximize employee wealth or social justice under the shareholder primacy paradigm, they must act in the shareholders' financial interest. Thus, while the following recommendations serve to benefit non-shareholder constituencies, it is asserted that they are also consistent with the shareholder primacy model.

#### 1. Mandate Monitoring of Discriminatory Practices

The director's duty to monitor does not presently encourage director activism in eliminating workplace discrimination. Currently, state corporate law defers to the directors' decision to install or not install compliance programs so long as directors reasonably investigate and duly deliberate before making the

<sup>258</sup> See Wai Shun Wilson Leung, *The Inadequacy of Shareholder Primacy: A Proposed Corporate Regime That Recognizes Non-Shareholder Interests*, 30 COLUM. J.L. & SOC. PROBS. 587, 591 (1997) (arguing that "[a corporation] is a series of relationships, or, more precisely, an aggregation of explicit contracts and implicit agreements among shareholders, managers and stakeholders."); see also Gabaldon, *supra* note 4, at 836 (specifying that this approach is typically affiliated with neoclassical economic and progressive corporate analysis).

<sup>259</sup> See Gabaldon, *supra* note 4, at 836 (positing that "[c]orporate progressives generally attempt to devise methods of setting more places at the table—for expanding the goals of the corporation and the duties of management (most notably the board of directors) to encompass notions of responsibility to other constituents, including broad-based society"); see also Marlene O'Connor, *Restructuring the Corporation's Nexus of Contracts: Recognizing a Fiduciary Duty to Protect Displaced Workers*, 69 N.C. L. REV. 1189, 1194 (1991) (analyzing stakeholder model of corporate social responsibility in which directors' fiduciary duties are expanded to include not only obligations to maximize shareholder wealth, but also actions that shield employees from disruptions such as corporate changes).

choice.<sup>260</sup> However, it is asserted that boards must not leave diversity to chance.<sup>261</sup> It is suggested that the director's duty to monitor should include an obligation to install an extensive monitoring system to ensure that executives and employees comply with employment discrimination law and promote diversity initiatives.<sup>262</sup>

## 2. Require Attention to Diversity Under Duty of Care

In the context of mergers and acquisitions, directors are required to reasonably investigate and duly deliberate the pros and cons of a merger before recommending it for shareholder approval.<sup>263</sup> Studies show that the most common reason for recommending a merger cited by directors in disclosures mandated by the SEC is "to compete with global markets" and mostly all material disclosures involve financial considerations.<sup>264</sup> It is asserted that the director's fiduciary duty of care to not make a grossly negligent decision to enter into a

<sup>260</sup> See Gabaldon, *supra* note 4, at 858 (proposing that deferring to directors to oversee corporate matters "establishes a process that . . . will produce the same result as an integrity-seeking conscience, and it allocates to specific individuals responsibility for seeing that the process is carried out"); see also Wade, *supra* note 8, at 225 (concluding that "[w]orkplace discrimination is a corporate governance issue because shareholders rely on boards to monitor managers in a way that encourages compliance with the laws prohibiting discrimination. Corporate boards that inadequately monitor compliance with anti-discrimination law reduce, rather than maximize, shareholder wealth").

<sup>261</sup> See Eglin, *supra* note 138, at 6 (noting ineffectiveness of BP's initial plan to hire diverse employees by instituting diversity/integration programs); see also Wade, *supra* note 8, at 226 (determining that "[b]oards cannot simply assume that their executives and employees comply with the law").

<sup>262</sup> See Eglin, *supra* note 138, at 6 (highlighting that "diversity and inclusion could not be let to chance - they had to be managed"); see also Gabaldon, *supra* note 4, at 866 (finding that "an individually focused approach requiring compliance by rank-and-file employees would be the most likely to assure that issues were identified as an initial matter," and is appealing because penalties avoid punishing shareholders).

<sup>263</sup> The purpose of a board of directors is to promote stockholder interests and retain a form of corporation oversight that involves the board in such issues as mergers and acquisitions. See *Board of Directors*, WIKIPEDIA.COM, Nov. 12, 2005, [http://www.en.wikipedia.org/wiki/Board\\_of\\_directors](http://www.en.wikipedia.org/wiki/Board_of_directors). Some commentators recommend boards set up conscience committees akin to auditing committees instituted after the corporate accounting scandals of the early 2000's made up of a diverse group of directors. See Gabaldon, *supra* note 4, at 866.

<sup>264</sup> See Troy A. Paredes, *Blinded by the Light: Information Overload and Its Consequences for Securities Regulation*, 81 WASH. U. L. Q. 417, 425 (2003) (noting that one of corporation's most textual disclosures mandated by the SEC requires reporting company to discuss its liquidity, capital resources, results of operations, and any other information the registrant believes is necessary to understand its financial conditions); see also Sharon Hannes, *Comparisons Among Firms: (When) Do They Justify Mandatory Disclosure?*, 29 IOWA J. CORP. L. 699, 702 (2004) (explaining that comparisons of financial information lies at core of all securities analyses).

merger should require the director to investigate and deliberate diversity issues, including the other company's diversity initiatives, its history of discrimination, and its dedication to implementing a program to ensure compliance with discrimination law.

In the takeover context, it is suggested that a board's decision to implement takeover defense mechanisms, in response to a bidder that presents a threat to its corporate culture and diversity efforts, should satisfy *Unocal* duties, even if the acquisition would produce short-term shareholder profit maximization. It is also asserted that when the sale and break-up of the corporation becomes inevitable, directors should be entitled to consider non-shareholder stakeholder interests.

### 3. Disclosure of Diversity Findings in Disclosures Mandated by Federal Securities Laws

Presently, federal securities laws require directors to disclose material information regarding a merger recommendation. However, studies show that the information disclosed by directors in satisfaction of the securities regulations is generally financial in nature and rarely involves human or cultural issues.<sup>265</sup> Determining whether information is material is largely left to the discretion of directors. It is asserted that federal corporate governance reforms are necessary in response to the increase in employment discrimination lawsuits as such reforms were necessary after the corporate accounting scandals. As Sarbanes-Oxley requires heightened disclosure of financial information and scrutiny of boards of directors, new federal reforms that require disclosure of compliance with employment discrimination laws and of board composition should be enacted. In addition, information regarding corporate diversity efforts and compliance with employment discrimination law should also be deemed "material" by the SEC and required in pre-merger

<sup>265</sup> See Paredes, *supra* note 264, at 425 (explaining that the starting point for appreciating disclosure requirements is the Regulation S-K form requiring information regarding registrant's business development and prospects, legal proceedings, properties, financial performance, directors and officers, and securities); Cynthia A. Williams, *The Securities and Exchange Commission and Corporate Social Transparency*, 112 HARV. L. REV. 1197, 1200-01, n.2 (1999) (noting that federal securities law requires disclosure of vast array of financial data and arguing that SEC has power to require social as well as financial disclosure).

disclosures. Further, federal regulations requiring the auditing of female and minority representation on boards of directors and in top levels of management should be implemented. Lastly, the SEC should prohibit corporations from including confidentiality pacts in settlement offers.

### B. Shareholder Activism

Shareholder activism is one way in which boards of directors may be forced to rethink their ambivalence toward diversity in the merger context and in the workplace in general. Shareholders can submit proposals that bring the board's attention to monitoring problems and the possible negative consequences of ignoring diversity issues in a merger.<sup>266</sup>

Federal securities law provides the guidelines for shareholder activists. Rule 14a-8<sup>267</sup> requires corporate managers to include any proposal that satisfies the procedural and substantive prerequisites, enumerated by the SEC under the rule, in shareholder proposals contained within the proxy materials sent to shareholders.<sup>268</sup> Once these proposals are distributed, shareholders have an opportunity to vote on the proposal.<sup>269</sup>

<sup>266</sup> In the racial discrimination context, activists have purchased corporate stock as a way to gain access to corporate managers and influence their employment practices. The Rainbow/PUSH Coalition created the Wall Street Project which has purchased shares in U.S. corporations in order to influence the decisions of corporate managers and directors. See Joseph Kahn, *Jackson Challenges Capital of Capital*, N.Y. TIMES, Jan. 16, 1999, at 3. There are many steps shareholders can take in order to change racial discrimination in the workplace. They can educate other investors about the potential dangers of companies who have racially discriminatory practices, they can expose the conduct thereby making it financially material, and they can also bring derivative actions alleging duty of care breaches when managers fail to investigate and monitor race discrimination allegations. See Wade *supra* note 8, at 392, 400–01. After Texaco settled a large race discrimination case, two shareholder proposals regarding diversity were submitted that received strong support from other shareholders. See Rye Brook, *Investors Focus on Diversity at Texaco Annual Meeting; Company Faces 94 Discrimination Filings*, WASHINGTON POST, May 14, 1997, at D9.

<sup>267</sup> SEC Rule 14a-8, 17 CFR 240.14a-8 (2005).

<sup>268</sup> Rule 14(a) governs management's solicitation of shareholder proxies and provides a process by which shareholders may communicate with management and other shareholders on issues relating to corporate governance and was promulgated by the SEC pursuant to authority granted to it under the Securities Exchange Act of 1934. See SEC Rule 14a-8, 17 CFR 240.14a-8 (2005). Rule 14a-8 provides an opportunity for a shareholder who owns a small amount of shares to have his or her proposal placed alongside the company's proxy materials to be voted on at an annual or special meeting of shareholders. See SEC Div. of Corp. Fin., *Staff Legal Bulletin No. 14, Shareholder Proposals*, U.S. Securities and Exchange Commission, July 13, 2001, <http://www.sec.gov/interp/legal/cfs14.htm>.

<sup>269</sup> See MATTHEW BENDER & CO., 1-3 CORPORATE GOVERNANCE: LAW AND PRACTICE § 3.05 [4] [b] [ii] (explaining that Rule 14a-8 allows shareholders to submit one proposal for

Such proposals can suggest changes in corporate policy related to significant social issues, including discriminatory conduct in the workplace.<sup>270</sup> Proposals regarding traditional corporate governance issues are clearly appropriate.

It is suggested that shareholder activists submit proposals that prompt boards to reexamine corporate diversity initiatives and compliance with employment discrimination law during the merger process and strongly emphasize diversity as a factor affecting synergy. Such proposals should encourage boards to focus on their duty of care to reasonably investigate and duly deliberate before recommending a merger to shareholders and on their duty of care to monitor corporate compliance with discrimination law during the merger process.

### *C. Enhance the Director's Relational Role and Include Women and Minorities on Boards*

Traditionally, boards were elected by shareholders for the sole purpose of monitoring corporate managers to protect shareholder interests. Today, institutional investors are putting pressure on directors to explain how their decisions benefit shareholders.<sup>271</sup> As a result, the board's relational role has become of primary importance.<sup>272</sup> As opposed to manager monitoring, relational

a shareholder vote); *SEC Div. of Corp. Fin., Staff Legal Bulletin No. 14A, Shareholder Proposals*, U.S. Securities and Exchange Commission, July 12, 2002, <http://www.sec.gov/interp/legal/cfslb14a.htm> (noting that Rule 14a-8 allows shareholders to have their proposals voted on at special or annual meetings of shareholders).

<sup>270</sup> Proposals that relate to the "ordinary business operations" of a company will be excluded, however. The SEC determines whether a proposal relates to a significant social issue or an ordinary business operation. See *Amendments to Rules on Stockholders*, Exchange Act Release No. 34-40018, 67 S.E.C. Docket 373, \*3-4, 1998 WL 254809 (May 21, 1998). Proposals that might have social implications can still be deemed "ordinary business operations" of a company. For example T. Rowe Price Group, Inc. was able to exclude a proposal that required the Company to not sponsor or contribute to non-profit organizations which undermined the American war on terrorism as dealing with ordinary business operations. See T. Rowe Price Group, Inc., SEC No-Action Letter, 2002 WL 31890967, \*1-2 (December 27, 2002).

<sup>271</sup> See Dallas, *supra* note 4, at 795 (explaining that institutional investors are using legal doctrine of shareholder primacy to pressure directors to specify how their decisions serve interest of shareholders); Troy A. Paredes, *Too Much Pay, Too Much Deference: Behavioral Corporate Finance, CEOs, and Corporate Governance*, 32 FLA. ST. U. L. REV. 673, 732 (2005) (noting that institutional shareholders are putting more pressure on boards and CEO's).

<sup>272</sup> See Dallas, *supra* note 4, at 795 (noting the managerialism is the predominant mode of governance of U.S. public corporations); Jill E. Fisch, *Corporate Governance: Taking Boards Seriously*, 19 CARDOZO L. REV. 265, 285 (1997) (stating that increased business complexity demands companies involve directors in strategic planning and other management decisions).

monitoring is the process by which board members exchange information and ideas with the corporation's stakeholders, its shareholders, consumers, and the legal and financial communities to stay abreast of current issues in the outside environment and ensure the continued support of the stakeholders.<sup>273</sup> While the shareholder primacy model of the corporation is still predominant, the idea that directors, when making decisions on behalf of the corporation, may consider the interests of not only the corporation's shareholders but also its stakeholders is becoming readily accepted.<sup>274</sup>

The board's relational role is particularly crucial when a corporation is contemplating a merger; yet, it is frequently not taken seriously or considered only in the 11<sup>th</sup> hour.<sup>275</sup> However, because boards are responsible for recommending mergers to shareholders<sup>276</sup> and smooth integration is a key component in

<sup>273</sup> See Dallas, *supra* note 4, at 782 (defining relational role of a company); see also Timothy L. Fort, *The Corporation as Mediating Institution: An Efficacious Synthesis of Stakeholder Theory and Corporate Constituency Statutes*, 73 NOTRE DAME L. REV. 173, 174 (1997) (discussing stakeholder theory, which similar to relational monitoring involves corporation's duties towards employees, suppliers, local communities and other stakeholders).

<sup>274</sup> There are competing approaches regarding the role the corporation plays in society. One view, put forth by Adolph Berle and E. Merrick Dodd in the 1930's, suggests that the corporation is "not only a profit-making entity, but also an institution with social responsibilities." Dallas, *supra* note 4, at 796. This approach is supported by case law that upholds the fiduciary duties of directors, not only to shareholders, but also to the corporation, as an independent entity. *Id.* The recognition of fiduciary duties that run from directors to the corporation itself reflects the idea that directors are trustees for the corporation and for its many stakeholders, including the community and consumers. This view has also been codified in several constituency statutes in over half of the states which permit directors to take the interests of stakeholders into account in their decision making. *Id.* at 797. Even in Delaware, a state without such a constituency statute, the Delaware Supreme Court has stated that directors may consider the interests of employees, consumers, and other stakeholders when making decisions as long as these decisions have a rational relationship to furthering a shareholder interest. *Id.* at 796-97. Even leading proponents of shareholder primacy model have acknowledged that in order to maximize financial value corporate managers must not only satisfy but enlist the support of all corporate stakeholders. See Margaret M. Blair, *Director's Duties in a Post Enron World: Why Language Matters*, 38 WAKE FOREST L. REV. 885, 894-95 (2003). There is also the argument that corporate social responsibility has been a factor in moving corporate governance theory in the direction of stakeholders. See Cynthia A. Williams and John M. Conley, *An Emerging Third Way? The Erosion of the Anglo-American Shareholder Value Construct*, 38 CORNELL INT'L L.J. 493, 495 (2005).

<sup>275</sup> See CAREY & OGDEN, *supra* note 17, at 142 (noting crucial decisions regarding board structure are often not given sufficient thought or deliberation and are usually made in period of pressure near end of merger negotiation).

<sup>276</sup> See e.g., VIII DEL. CODE ANN. § 141(a) (2005) (stating business and affairs of every corporation shall be managed by or under direction of board of directors); see also MATTHEW BENDER & CO., 1-4 CORPORATE GOVERNANCE: LAW AND PRACTICE § 4.01 (2000) (noting broad powers granted to board which include power to choose merger partner for



successful mergers, it is integral that boards consider the social implications of M&A, including attitudes toward diversity.<sup>277</sup> It is asserted that the enhancement of the director's relational role will facilitate closer examination of a merger's effect on the company's employees and other non-shareholder stakeholders and, in turn, increase the likelihood of pre-merger synergy.

It is suggested that a diverse board made up of not only white males but also women and minorities is better equipped to effectively perform a relational role. First, as has been discussed, a diverse board will bolster the new firm's product marketing, consumer relations, and employee production because it will more easily relate to diverse employees and consumers.<sup>278</sup>

Second, adding female and minority directors will also change the psychological dynamic of the board and, in turn, the culture of the entire company. Critical race theorists have argued that today's discriminatory practices frequently result from unconscious racism.<sup>279</sup> For example, Patricia Williams asserts that by blindly enforcing so-called "neutral" legal standards that do not take account for racial or gender differences, society and, in this particular context, directors, perpetuate underlying biases and prejudices.<sup>280</sup> For instance, a board composed entirely of white males might not attach importance to the fact that a company with which it is about to merge has historically discriminated against women and minorities. By failing to emphasize the moral, social, and economic implications of such discrimination, this board will perpetuate racism or sexism within its corporation.<sup>281</sup> On the other hand, anecdotal evidence

company though stockholders have ultimate discretion to approve or veto recommendation).

<sup>277</sup> See CAREY & OGDEN, *supra* note 17, at 150 (reiterating necessity of choosing capable board members); see also Brian Allen Warwick, *Reinventing the Wheel: Firestone and the Role of Ethics in the Corporation*, 54 ALA. L. REV. 1455, 1456 (noting heightened importance on role of board of directors since *Caremark*).

<sup>278</sup> See *supra* Part C.I.

<sup>279</sup> See Wade, *supra* note 8, at 226 (stating argument of critical race theorists); see also Charles Lawrence III, *The Id, the Ego, and Equal Protection: Reckoning with Unconscious Racism*, 39 STAN. L. REV. 317, 322 (1987) (stating that many people in American society are unaware their own racist ideas).

<sup>280</sup> See Williams, *supra* note 2, at 103 (noting necessity of looking behind accepted standards in order to find "hidden" prejudice); see also Lawrence, *supra* note 279, at 356 (noting that racist attitudes are repressed and continue to be part of culture).

<sup>281</sup> See Williams, *supra* note 2, at 103 (highlighting importance of minimizing prejudice in corporate setting). See generally Lawrence, *supra* note 279, at 322 (explaining that most people are unaware of their own racist attitudes).

shows that because female and minority board members can empathize with diversity issues, they are more likely to emphasize diversity in mergers.<sup>282</sup> Importantly, a merger can also provide an opportunity to create such a diverse board and align it with “progressive and productive” corporate governance guidelines.<sup>283</sup>

*D. Recognize the Importance of the Human Issues in Mergers and Acquisitions*

Finally, all businesses stress the importance of the business or economic issues when deciding whether to merge. However, commentators have defined the “key variable” separating the successful mergers from the failures as “the human factor: before, during, and after the deal.”<sup>284</sup> Merging companies that are “hopelessly at odds with each other culturally” tend to fail. It is, thus, of the utmost importance for the board of directors of the new firm to define the company’s vision, personality, and behavior and clearly communicate the goals to all levels of the new organization.<sup>285</sup> It is asserted that mergers must be regarded as ideal opportunities to build new boards, implement best business and governance practices, and make fresh starts in terms of diversification.

<sup>282</sup> See Knight, *supra* note 134, at 1C (noting women executives emphasize diversity in merger decision and continue to promote diversity). See generally *Healthcare Leads Other Industries In Female Board Representation Dual Gender Mix Strengthens Community Trust*, HEALTHCARE PR AND MARKETING NEWS, Feb. 18, 1999, at 4 (stating that board diversity in hospital mergers strengthens public confidence).

<sup>283</sup> See CAREY & OGDEN, *supra* note 17, at 142 (emphasizing need for directors to be involved with diversity issues).

<sup>284</sup> See Carey, *supra* note 17, at 159 (noting importance of dealing with “human issues” is constant and will be present at any stage of corporate endeavor).

<sup>285</sup> CAREY & OGDEN, *supra* note 17, at 167 (stating mergers will remain prevalent, albeit in “definable waves”).

