

4-1-2009

"Unpatriotic" Profits: The Risks Companies Face from International Business Activities and the Need for a Heightened Duty of Oversight for Corporate Directors

Jeffrey T. Dinwoodie

Follow this and additional works at: <https://ecommons.udayton.edu/udlr>



Part of the [Law Commons](#)

Recommended Citation

Dinwoodie, Jeffrey T. (2009) ""Unpatriotic" Profits: The Risks Companies Face from International Business Activities and the Need for a Heightened Duty of Oversight for Corporate Directors," *University of Dayton Law Review*. Vol. 34: No. 3, Article 3.

Available at: <https://ecommons.udayton.edu/udlr/vol34/iss3/3>

This Article is brought to you for free and open access by the School of Law at eCommons. It has been accepted for inclusion in University of Dayton Law Review by an authorized editor of eCommons. For more information, please contact mschlangen1@udayton.edu, ecommons@udayton.edu.

“UNPATRIOTIC” PROFITS: THE RISKS COMPANIES FACE FROM INTERNATIONAL BUSINESS ACTIVITIES AND THE NEED FOR A HEIGHTENED DUTY OF OVERSIGHT FOR CORPORATE DIRECTORS

*Jeffrey T. Dinwoodie **

TABLE OF CONTENTS

I.	INTRODUCTION	378
II.	BACKGROUND	379
	A. <i>Patriotism and National Security</i>	379
	B. <i>Limitations on International Business Arrangements</i>	381
	C. <i>Corporate Law</i>	384
	1. Corporate Purpose	384
	2. Board Oversight Responsibilities	385
	3. Board Challenges	387
III.	THE CASE FOR INCREASED OVERSIGHT RESPONSIBILITIES	388
	A. <i>Potential Damages, Losses, and Costs</i>	388
	1. Damaged Relations with Customers	389
	2. Damaged Relations with Investors	390
	a. Shareholder Activism	390
	b. Institutional Investors	391
	c. Divestment	393
	3. Resources Spent to Repair Damages	394
	B. <i>Legal Support</i>	395
	1. Case Law	395
	2. The Corporate Director's Guidebook	396
IV.	MEETING THE INCREASED OVERSIGHT RESPONSIBILITIES	398
	A. <i>Red Flags</i>	398
	1. Relationship with a Government-Designated Trading Partner	398
	2. World Events	399
	3. High Profile Media Report	400
	4. Government Investigation or Inquiry	400

* Jeffrey T. Dinwoodie is a staff attorney in the Securities and Exchange Commission's Division of Trading and Markets. This article was written while Mr. Dinwoodie was in law school, and it was accepted for publication before Mr. Dinwoodie began employment at the Securities and Exchange Commission. The views expressed in the article are those of Mr. Dinwoodie and do not reflect the views of the Securities and Exchange Commission, its Commissioners, or staff.

5. Scrutiny of Another Company	401
B. Monitoring Systems	401
1. Components.....	401
a. Internet Searches	402
b. Outside Experts and Consultants	403
2. Issues	404
a. Legal and Regulatory Requirements	404
b. Public Relations Issues.....	405
c. Investor Relations	405
d. Forecasting	406
V. CONCLUSION	406

I. INTRODUCTION

Patriotism and national security have been dominant themes and points of emphasis in the United States since the September 11, 2001 terrorist attacks. Americans have become increasingly sensitive to anything that is potentially threatening or detrimental to the national security interests of the United States.¹

Operating within this environment, American corporations face a daunting challenge. They are under growing pressure to expand in an increasingly competitive global marketplace. But at the same time, they must be very careful with whom they do business. In recent years, the government and the media have scrutinized the international business practices of many well-known corporations and questioned whether they are contrary to national security interests. Several of these corporations have suffered strains in their relations with both investors and customers as the result of these allegedly unpatriotic business activities.

As the governing bodies of corporations, boards of directors ("boards") are directly confronted with the challenge of effectively managing their corporations' vulnerability to this "global security risk."² One of the primary responsibilities of a board is to provide oversight to the corporation.³ Traditional board oversight responsibilities require a board to monitor the corporation's financial performance, business operations,

¹ See *infra* Sec. III.A. for a discussion of how Americans have become increasingly aware and sensitive to anything that is perceived to be a threat to United States national security interests.

² "Global security risk" is broadly defined as "the risk to share value and corporate reputation stemming from the intersection of a publicly traded company's international business activities and security-related concerns, such as terrorism and weapons proliferation." Conflict Securities Advisory Group, *Global Security Risk, What is Global Security Risk?* <http://www.conflictsecurities.com/security/index.cfm> (accessed Apr. 28, 2008).

³ See generally ABA Sec. of Bus. L. Comm. on Corp. Laws, *Corporate Director's Guidebook, Fifth Edition*, 62 Bus. Law. 1479, 1490 (2007) [*Director's Guidebook*] (explaining that corporate directors provide leadership towards a corporation's core objectives through two primary functions, decision-making and oversight).

management performance, ethics program, and legal and regulatory compliance.⁴ This article examines board oversight responsibilities over a corporation's international business activities and relationships. It argues that boards must perform greater oversight than that which has traditionally been required.

Section II of the article provides relevant background information. It discusses the forces, factors, and events that have contributed to the elevated focus on patriotism and national security in the United States. It then reviews the pertinent legal limitations that the United States government has placed on American businesses' ability to conduct business with international partners. Section II then provides the relevant corporate law framework. It discusses the debate over corporate purpose, the corporate social responsibility movement, the evolution of board oversight duties, and the business judgment rule.

Section III argues that boards must take on enhanced oversight responsibilities over their corporations' international business activities in light of (1) the range of harms that can result from certain international business relationships and affiliations and (2) some recent legal developments.

Section IV argues that in order to exercise these enhanced oversight responsibilities, boards must (1) respond to “red flags” that come to the attention of the directors that the corporations' international business affairs could be called into question and (2) develop and implement programs to monitor and alert the directors to potentially damaging publicity stemming from their corporations' international business affairs.

Section IV provides practical recommendations on how boards could fulfill these enhanced oversight responsibilities. It describes five examples of plausible red flags that should capture a board's attention. It concludes by describing the key components of an effective monitoring system along with some of the major issues of which such a system should be vigilant

II. BACKGROUND

A. Patriotism and National Security

Patriotism and national security have been dominant themes and points of emphasis in the United States since the September 11, 2001 terrorist attacks (“9/11 attacks”). The 9/11 attacks evoked a range of feelings across the United States—including anger, fear, sadness, and

⁴ *Id.*

vulnerability.⁵ These feelings evolved into a renewed sense of national pride and patriotism⁶ along with a renewed societal focus on national security.⁷

Events that occurred after the 9/11 attacks also contributed to this societal emphasis on patriotism and national security. Shortly after the 9/11 attacks, the United States waged war in Afghanistan.⁸ Two years later, the United States invaded Iraq. These continuing conflicts have kept national security in the news and in the consciousness of Americans. In addition to the ongoing conflicts in Afghanistan and Iraq, mounting tensions with the governments of Iran⁹ and North Korea¹⁰ have also contributed to society's focus on national security.

The statements of United States government officials have also contributed to the focus on national security. President George W. Bush, for example, used extremely forceful language in discussing America's "War on Terror."¹¹ During a speech shortly after the 9/11 attacks, President Bush proclaimed that "[e]very nation, in every region, now has a decision to make. Either you are with us, or you are with the terrorists."¹²

Other government actions have also contributed to this environment

⁵ See generally David Cole, *Enemy Aliens: Double Standards and Constitutional Freedoms in the War on Terror* 17 (The New Press 2003) (commenting that nobody "who witnessed the terrorist attacks of September 11, even from the relatively safe vantage point of the television set, will ever forget them.").

⁶ See generally S. Mitra Kalita, *A Blending of Patriotism, Native Pride; In Diverse Fairfax School, Civics Start in 1st Grade*, Wash. Post B01 (June 8, 2004) (noting that after the 9/11 attacks, many elementary schools put more emphasis on civics and patriotism through the expansion of civics curriculums and by holding patriotic-themed student programs and events).

⁷ See generally Andrew Kohut, Address, *The Impact of September 11 on Public Opinion: Increased Patriotism, Unity, Support for Bush; More Interest in News* (Brookings Instn., Mar. 27, 2002) (available at <http://www.brookings.edu/events/2002/0327terrorism.aspx?p=1>) (reporting that polls taken since the 9/11 attacks show a heightened sense of national unity, patriotism, and an increased interest in politics and political news). Admittedly, the sense of national unity in the United States has decayed as a result of several polarizing issues, such as the Iraq War. However, the overall sense of patriotism, and the increased interest in politics and political news, referred to by Kohut, still generally exists in 2009.

⁸ See generally U.S. Dept. of Def., *Securing Afghanistan: Stabilization & Growth*, <http://www.defenselink.mil/home/features/2007/Afghanistan/index.html> (accessed Apr. 4, 2008) (noting that the "U.S. and its allies launched an invasion of Afghanistan to overthrow the Taliban regime and destroy the al-Qaeda terrorist network it supported.").

⁹ See generally Robin Wright, *Iran a Threat, Bush Insists: Experts Says President is Wrong and Is Escalating Tensions*, Wash. Post A14 (Mar. 21, 2008) (reporting on the escalating tensions between the Bush Administration and Iran).

¹⁰ See generally Helene Cooper, *A New Bush Tack on North Korea*, 157 N.Y. Times A1 (Dec. 7, 2007) (reporting that even though President Bush had publicly called North Korea's leader, Kim Jong-il, a tyrant, he recently wrote a letter asking Jong-il to disclose North Korea's past and present nuclear work).

¹¹ The Bush Administration made national security the primary focus of its agenda. The Bush Administration's emphasis on national security was evident in the layout of the Bush White House Internet homepage. Of the eighteen topics listed on the site's "In Focus" menu, six of them related closely to national security: "Defense," "Global Diplomacy," "Homeland Security," "Iraq," "Middle East," and "National Security." U.S. Govt., *The White House*, <http://web.archive.org/web/20080325200409/http://www.whitehouse.gov/> (accessed Apr. 5, 2008).

¹² Pres. George W. Bush, Address, *Address to a Joint Session of Congress and the American People* (D.C., Sept. 20, 2001) (available at http://www.dhs.gov/xnews/speeches/speech_0016.shtml).

in America. For example, Congress has passed laws aimed at strengthening national security, which have garnered a significant amount of attention.¹³ Another illustrative example of how the government has fed the societal focus on national security is the color-coded Homeland Security Advisory System.¹⁴ This warning system, by its very nature, brings thoughts of United States national security and fears of terrorism into the consciousness of Americans.¹⁵

This heightened sense of patriotism¹⁶ and focus on national security has created an environment where Americans have become increasingly aware and sensitive to anything perceived to be potentially threatening to American national security interests.¹⁷

B. Limitations on International Business Arrangements

The Department of the Treasury's Office of Foreign Assets Control ("OFAC") administers and enforces the American economic sanction programs ("Sanction Programs"),¹⁸ a series of legal barriers which attempt to limit the abilities of Americans to do business with certain countries and international partners.¹⁹ The sanction programs have been used periodically throughout history by the United States government to support various foreign policy and national security goals.²⁰ Not surprisingly, the sanction

¹³ The most noteworthy and controversial piece of legislation enacted after the 9/11 attacks was the United and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT Act) Act of 2001, Pub. L. No. 107-56, 115 Stat. 272 (2001). See generally Lisa Finnegan Abdolian & Harold Takooshian, *The USA Patriot Act: Civil Liberties, The Media, and Public Opinion*, 30 Fordham Urb. L.J. 1429 (2003) (examining the legal provisions of the USA PATRIOT Act, the media's coverage of the Act, and public opinion on post-9/11 civil liberties).

¹⁴ See generally Dept. of Homeland Sec., *Homeland Security Advisory System*, http://www.dhs.gov/xinfoshare/programs/Copy_of_press_release_0046.shtm (last updated Feb. 9, 2009).

¹⁵ See generally John Mintz, *DHS Considers Alternatives to Color-Coded Warnings*, Wash. Post A06 (May 10, 2005) (reporting that officials in the Department of Homeland Security were considering changing the color-coded terrorism warning system due to wide spread criticisms of the system).

¹⁶ Society's emphasis on patriotism was evident in the 2008 Presidential election. For example, the media reported on whether candidates wore American flags on their lapels. See generally Alec MacGillis, *The Trail: A Daily Diary of Campaign 2008, Lapel Pin Politics*, http://blog.washingtonpost.com/the-trail/2007/10/05/lapel_pin_politics.html (Oct. 5, 2007) (noting that Presidential candidate Barack Obama caused a minor controversy when he stopped wearing an American flag pin on his lapel).

¹⁷ See *infra* Sec. III.A. for a discussion of how Americans have become increasingly aware and sensitive to anything that is perceived to be a threat to United States national security interests.

¹⁸ See U.S. Dept. of the Treas. Off. of For. Assets Control, <http://www.treas.gov/>; select OFAC SDN List, select Office of Foreign Assets Control, select Frequently Asked Questions, select What is OFAC and What Does It Do? (accessed Apr. 7, 2008).

¹⁹ As part of its enforcement duties, OFAC maintains a list of individuals and companies owned or controlled by, or acting for or on behalf of, targeted countries. OFAC also lists individuals, groups, and entities, such as terrorists and narcotics traffickers. Collectively, these individuals and companies are called Specially Designated Nationals ("SDNs"). U.S. persons are generally prohibited from dealing with SDNs. U.S. Dept. of the Treas. Off. of For. Assets Control, <http://www.treas.gov/>; select OFAC SDN List, select Office of Foreign Assets Control, select Frequently Asked Questions, select What is an SDN? (accessed Apr. 5, 2008).

²⁰ For a history of the Treasury Department's economic sanctions efforts see U.S. Dept. of the Treas. Off. of For. Assets Control, *Our History*, <http://www.treas.gov/offices/enforcement/ofac/mission.shtml> (accessed Apr. 7, 2008), See generally Harry Wolff, *Unilateral Economic Sanctions*:

programs have garnered significant attention and become increasingly relevant since the 9/11 attacks.²¹

The sanction programs are based primarily on the Trading with the Enemy Act of 1917 ("TWEA")²² and the International Emergency Economic Powers Act of 1977 ("IEEPA").²³ TWEA gives the President the power to freeze certain assets and to prohibit certain financial transactions during times of war.²⁴ IEEPA allows the President to prohibit American trade with nations that are deemed to pose a threat to American national security.²⁵ Acting under these two acts, presidents have issued numerous executive orders which limit business dealings between American businesses and different sorts of international parties, including nations such as Iran,²⁶ regimes such as the Taliban,²⁷ and terrorist organizations such as al-Qaeda.²⁸

Congress has passed other laws which also seek to limit business dealings between Americans and various international business partners. For example, the Cuban Assets Control Regulations prohibit a wide range of business dealings with Cuba, such as American investment and financial

Necessary Foreign Policy Tool or Ineffective Hindrance on American Businesses? 6 Hous. Bus. & Tax L.J. 329, 332-46 (2006) (providing a history of the United States government's use of economic sanctions to further its foreign policy goals).

²¹ Economic sanctions programs are subject to change based on world events, United States foreign policy goals and philosophies, and changes in relations between the United States and various nations, organizations, and individuals. For example, the sanctions limiting dealings between American businesses and North Korea are commonly changing based on negotiations between the two nations. See U.S. Dept. of the Treas. Off. of For. Assets Control, *North Korea: What You Need To Know about Sanctions, An Overview of the Foreign Assets Control Regulations as They Relate to North Korea, Title 31 Part 500 of the U.S. Code of Federal Regulations* (Aug. 19, 2008) (available at <http://www.treas.gov/offices/enforcement/ofac/programs/nkorea/nkorea.pdf> 1) (noting that on June 26, 2008, President Bush simultaneously terminated the application of the Trading with the Enemy Act of 1917 ("TWEA") with respect to North Korea and issued an executive order which continued two specific TWEA-based restrictions against North Korea). In October 2008, the United States removed North Korea from its State Sponsor of Terrorism List after agreements were reached between the two countries with regards to North Korea's nuclear weapons program. The State Sponsor of Terrorism List is maintained by the U.S. Department of State. Countries on this list are subject to restrictions on U.S. foreign assistance and a series of trade and other financial restrictions. The U.S. Dept. of St. Off. of the Coord. for Counter Terrorism, *State Sponsor of Terrorism*, <http://www.state.gov/s/ct/c14151.htm> (accessed Jan. 3, 2009). See also Glenn Kessler, *U.S. Drops North Korea from Terrorism List*, Wash. Post A01 (Oct. 12, 2008).

²² Trading with the Enemy Act of 1917, 50 U.S.C. app. §§ 1-44 (2000).

²³ See International Emergency Economic Powers Act of 1977, 50 U.S.C. §§ 1701-06 (2000 & Supp. 2005).

²⁴ 50 U.S.C. app. § 5(b)(1)(A).

²⁵ 50 U.S.C. § 1701(a); 50 U.S.C. § 1702(a)(1)(A)(i).

²⁶ Exec. Or. 12959, 60 Fed. Reg. 24757 (May 6, 1995); Exec. Or. 13059, 62 Fed. Reg. 44531 (Aug. 19, 1997). These Executive Orders prevent U.S. persons from selling, servicing, financing or supporting transactions involving Iran. They do not apply directly to subsidiaries of U.S. companies that are separately organized in foreign jurisdictions and are operating independently of U.S. persons.

²⁷ Exec. Or. 13129, 64 Fed. Reg. 36759 (July 4, 1999). This Executive Order prohibits transactions with the Taliban.

²⁸ Exec. Or. 13224, 66 Fed. Reg. 49079 (Sept. 23, 2001). This Executive Order became effective on September 24, 2001, in response to the 9/11 attacks. It prohibits U.S. transactions with twenty-seven terrorist organizations, individuals, corporations, and non-profit organizations thought to be associated with Osama bin Laden and al-Qaeda.

involvement in Cuba and the import of Cuban products.²⁹

There are holes in many of these legal barriers which create opportunities for American corporations to do business with foreign business partners, despite the aims of the United States government.³⁰ One major loophole is that the legal requirements typically apply only to “American controlled entities.”³¹ Corporations have been able to avoid the application of these legal barriers by using foreign subsidiaries and affiliates organized in foreign jurisdictions and operating independently of United States persons.³² Despite efforts to close these loopholes, corporations have still been able to maintain business relationships with disfavored nations and

²⁹ Cuban Assets Control Regulations, 31 C.F.R. §§ 515.201-515.206 (2005).

³⁰ There is speculation that the federal government has not taken more direct action to expose and stop companies from doing business in countries believed to be sponsoring terrorism because government officials fear that strong measures could be seen as blacklisting foreign countries, and it could lead to tensions with allies. See generally Marc Perelman, *An Anti-Terrorist Divestment Campaign Fires Blanks*, 155 *Fortune* 7, 24 (Apr. 16, 2007) (describing some of the reasons why the United States government has not taken stronger action in support of the anti-terror divestment movement). In 2004, Congress directed the U.S. Securities and Exchange Commission (“SEC”) to create the Office of Global Security Risk. Congress directed this office to perform duties such as ensuring that all companies sold on U.S. exchanges operating in State Department-designated terrorist-sponsoring states disclose such activities to investors and implementing enhanced disclosure requirements based on the risk to corporate share value and reputation stemming from business interests in high risk countries. H.R. Rpt. 108-221 at 151-52 (July 21, 2003) (available at http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=108_cong_reports&docid=f:hr221.108.pdf). See generally U.S. Secs. & Exch. Comm., *Office of Global Security Risk*, <http://www.sec.gov/divisions/corpfin/globalsecrisk.htm> (last modified Mar. 2, 2005). In June of 2007, the SEC’s Office of Global Security Risk launched an Internet tool to allow investors to view the pertinent portion of the annual reports of companies that disclosed business activities in countries listed on the State Department’s State Sponsors of Terrorism List. The SEC removed the tool after controversy ensued as to the accuracy and fairness of the list. See Press Release, Christopher Cox, Chairman, *Statement by Securities and Exchange Commission Concerning Companies’ Activities in Countries Known to Sponsor Terrorism* (July 20, 2007) (available at <http://www.sec.gov/news/press/2007/2007-138.htm>).

³¹ See generally Press Release, Frank R. Lautenberg, U.S. Senator, *U.S. Sen. Amendment to the FSC-ETI Bill to Close Loophole in Terror Sanctions Law* (Apr. 22, 2004) (available at <http://lautenberg.senate.gov/newsroom/record.cfm?id=254185>) (discussing a planned amendment to a bill designed to close a loophole that allows the foreign subsidiaries of American companies to do business with certain terrorist nations).

³² Ltr. from Halliburton, to the Managers of the N.Y.C. Police Pension Fund and the N.Y.C. Fire Pension Fund, *Halliburton Business in Iran – Global Overview* (Oct. 21, 2003) (available at http://www.comptroller.nyc.gov/press/pdfs/halliburton-pr03-12-102/Oct21-03_Halliburton-report.pdf) (explaining that Halliburton’s principal business activities in Iran occurred through the use of subsidiaries operating from locations such as the Cayman Islands and the United Arab Emirates); Press Release, William C. Thompson, Jr., N.Y.C. Comptroller, *SEC Declines Halliburton Request to Block NYC Pension Fund Proposal for Review of Company’s Connection to Iran* (Mar. 20, 2003) (available at http://www.comptroller.nyc.gov/press/2003_releases/pr03-03-027.shtm) [*NYC Comptroller Mar. 20, 2003 Press Release*] (noting that GE conducted business operations with the Iranian government through its Canadian subsidiary and ConocoPhillips conducted business in Iran and Syria through its UK subsidiary). Also, many experts believe that several well-known American companies purposely avoid U.S. trade restrictions by shipping their goods to third parties for the purpose of, or knowledge that, the third parties will then sell the goods to and in prohibited nations. See generally Christopher S. Stewart, *The Axis of Commerce*, Condé Nast Portfolio (Sept. 2008) (reporting on how several prominent American companies use Dubai as a conduit to avoid U.S. restrictions in order to gain access to the Iranian market) and Farah Stockman, *HP Uses Third Party to Sell Printers in Iran: Calif. Firm’s Sales Soar in Embargo*, *Bos. Globe A1* (Dec. 29, 2008) (noting that it appears that California-based Hewlett-Packard has purposely avoided U.S. economic sanctions by using a partnership with a company in Dubai to sell its printers in Iran).

international parties.³³

C. Corporate Law

1. Corporate Purpose

For decades, experts have debated questions of corporate purpose and to whom corporate duties run.³⁴ The prevailing view is that corporations must be designed and managed with the goal of maximizing shareholder wealth.³⁵

Nonetheless, corporations often take a wide range of interests into account when making business decisions, some of which appear to not directly improve shareholder interests.³⁶ This practice of considering non-shareholder interests has generally been approved by courts under the business judgment rule³⁷ on the basis that the decisions advance the long-

³³ See Wolff, *supra* n. 20, at 351-56 (providing a detailed overview of the government initiatives to close the holes in the economic sanctions programs).

There have been other attempts to enact federal legislation to stop companies from circumventing the economic sanctions programs. For example, then-Senator Barack Obama cosponsored the Iran Sanctions Enabling Act of 2007, which would, among other things, require the government to publish a list every six months of those companies that have an investment of more than \$20 million in Iran's energy sector. The legislation would also protect fund managers who divest from those companies from investor lawsuits. Iran Sanctions Enabling Act of 2007, H.R. 2347, 110th Cong. §§ 3(a)(1), (5)(c) (July 31, 2007). See also Press Release, House Comm. on Fin. Servs., *Frank, Lantos and Obama Introduce Divestment Bill* (May 15, 2007) (available at http://www.house.gov/apps/list/press/financialsvcs_dem/press0515072.shtml).

³⁴ In the early 1930s, Professor E. Merrick Dodd, Jr. of Harvard Law School and Professor Adolf Berle of Columbia Law School engaged in a famous debate over the question of to whom corporate duties run. Professor Dodd argued that corporations' responsibilities run to shareholders, employees, customers, and the general public. Professor Berle disagreed, arguing that corporations' responsibilities were limited to the interests of shareholders. See generally ABA Comm. on Corp. Laws, *Other Constituencies Statutes: Potential for Confusion*, 45 Bus. Law. 2253, 2254-57 (1990) [*Other Constituencies Statutes*] (recounting the historical debate between Professors Dodd and Berle).

³⁵ Gary von Stange, *Corporate Social Responsibility Through Constituency Statutes: Legend or Lie?* 11 Hofstra Lab. L.J. 461, 461-62 (1994) (noting that traditionally, it has been beyond the scope of corporate directors' duties to conduct corporate activities in furtherance of non-shareholder interests). In 1968, Berle conceded defeat to Dodd, when, during a speech, he remarked, "I was not convinced as [a] matter of doctrine that social responsibility should not be left to government [rather than to directors]—but there was no doubt that the event conformed rather to his prediction than to mine." Adolf Berle, *Corporate Decision-Making and Social Control*, 24 Bus. Law. 149, 150 (1968). See also *Other Constituencies Statutes*, *supra* n. 35, at 2255 (noting that courts have consistently avowed the legal primacy of shareholder interests when management and directors make decisions). See e.g. *Dodge v. Ford Motor Co.*, 170 N.W. 668, 684 (Mich. 1919) (repudiating Henry Ford's discretionary powers to extend corporate profits to benefit employees and consumers rather than stockholders, and endorsing the principle that a corporation's primary goal is to maximize shareholder value and wealth).

³⁶ See *Other Constituencies Statutes*, *supra* n. 34, at 2257-58 (noting that corporations commonly spend resources at the expense of shareholder short-term interests — for things such as employee outings, employee benefits, and charitable and community purposes — for the sake of advancing long-term interests).

³⁷ See *infra* Sec. II.C.3. for a detailed discussion of the business judgment rule. One can imagine the internal debate that would likely occur over a corporation's decision whether to enter into a potentially controversial international business relationship. On one hand, the corporation could enter into the relationship and reap the ensuing short-term profits. On the other hand, the corporation could turn down the relationship and pass over the potential profits under the business judgment rule, on the

term interests of shareholders.³⁸

2. Board Oversight Responsibilities

A corporation's board of directors is primarily responsible for two main areas, corporate decision-making and oversight.³⁹ All directors owe a duty of care to the corporation.⁴⁰ The duty of care requires that each director exercise an objective, reasonably prudent standard of care in the discharge of his or her duties.⁴¹ A director must act with the care that a person in a like position would reasonably believe appropriate under similar circumstances.⁴² The duty of care is to be judged according to the individual director's knowledge, skills, and experience — and in light of the situation at hand.⁴³

Traditional board oversight responsibilities⁴⁴ require a board to monitor “the corporation's business and affairs including, for example, financial performance, management performance, and compliance with legal obligations and corporate policies.”⁴⁵

basis that the corporation would be better served by avoiding the long-term reputational risks that would accompany such a relationship.

³⁸ See e.g. *Shlensky v. Wrigley*, 237 N.E.2d 776, 781 (Ill. App. 3d 1968) (deferring to Wrigley's refusal to install lights in Wrigley Field, despite the evidence that Wrigley was favoring non-shareholder interests in the decision).

³⁹ *Director's Guidebook*, supra n. 3, at 1490.

⁴⁰ Additionally, each director owes a duty of loyalty to the corporation. “The duty of loyalty requires that each director act in good faith and in the best interests of the corporation.” *Director's Guidebook*, supra n. 3, at 1497. For a detailed discussion of the duty of loyalty of corporate directors, see *id.* at 1497-99; Steven M. Bainbridge, Star Lopez, & Benjamin Oklan, *The Convergence of Good Faith and Oversight*, 55 UCLA L. Rev. 559 (2008); Dennis J. Block, Michael J. Malmone & Steven B. Ross, *The Duty of Loyalty and the Evolution of the Scope of Judicial Review*, 59 Brook. L. Rev. 65 (1993).

⁴¹ For a detailed discussion of the duty of care of corporate directors, see *Director's Guidebook*, supra n. 3, at 1494-96; R. Franklin Balotti & Joseph Hinsey IV, *Director Care, Conduct, and Liability: The Model Business Corporation Act Solution*, 56 Bus. Law. 35, 39-51 (2000); Melvin Aron Eisenberg, *The Duty of Care of Corporate Directors and Officers*, 51 U. Pitt. L. Rev. 945 (1990); James M. Tobin, *The Squeeze on Directors—Inside Is Out*, 49 Bus. Law. 1707 (1994).

⁴² *Directors Guidebook*, supra n. 3, at 1494. Additionally, a director with special skills is expected to utilize those skills in the performance of his or her duties and not just limit him or her self to the person in a like position standard. See *Restatement (Second) of Agency* § 379(1) (1958).

⁴³ *Directors Guidebook*, supra n. 3, at 1494.

⁴⁴ A board's other primary function is decision-making. There are several interesting issues having to do with a board's decision-making in the context of managing a company's exposure to damaging publicity from its international business dealings.

For example, a board could take several approaches in its decision-making process as to whether it enters into potential business relationships with foreign trading partners. On one hand, a board could create a standard policy stating, that on a categorical basis, it will not have any relationships or contacts with certain nations — whether it be with that nation's government, or organizations, companies or individuals linked to that nation. Another approach that a board could take would be to create a list of issues and factors that it would use to evaluate whether it would enter into potential international business relationships. Alternatively, a board could provide itself with a lot of flexibility by purporting to evaluate each prospective relationship on a case-by-case basis, rather than having any standard policies or decision-making factors.

While board decision-making in this context is an important issue, it is outside of this paper's focus on board oversight responsibilities. Therefore, it is not discussed in further detail.

⁴⁵ *Director's Guidebook*, supra n. 3, at 1490.

Historically, a board was only required to investigate potential problems when suspicious events or red flags came to the board's attention and indicated that board oversight was necessary.⁴⁶ Recent case law, however, has suggested that a board must play a more active oversight role and actually install systems that monitor for and alert the board to potential problems requiring attention.⁴⁷

Graham v. Allis-Chalmers Manufacturing Co. set forth the old red flag test.⁴⁸ In *Graham*, a shareholder brought a derivative suit against a company's board, alleging that the company's liability for antitrust violations was attributable to the board's failure to perform its oversight responsibilities.⁴⁹ In affirming the lower court's dismissal of the claim, the Delaware Supreme Court emphasized that the board was entitled to rely on the honesty and integrity of subordinates until something occurred to make the directors suspicious that something was wrong.⁵⁰ The Court noted that it was possible for a board to be held liable for neglecting to investigate suspicious events.⁵¹ The Court, however, created a red flag test when it went on to write that "absent cause for suspicion there is no duty upon the directors to install and operate a corporate system of espionage to ferret out wrongdoing which they have no reason to suspect exists."⁵²

Courts have interpreted *Graham* as standing for the proposition that "absent grounds to suspect deception, neither corporate boards nor senior officers can be charged with wrongdoing simply for assuming the integrity of employees and the honesty of their dealings on the company's behalf."⁵³ *Graham's* red flag test remained the standard for evaluating board oversight responsibilities in Delaware for decades.⁵⁴

In 1996, *In re Caremark International Derivative Litigation*⁵⁵ came before the Delaware Court of Chancery. In *Caremark*, shareholders brought a derivative suit against a company's board, alleging that the company's losses resulting from violations of federal Anti-Referral Payment laws were attributable to the board's failure to fulfill its oversight responsibilities.⁵⁶ In approving settlement of the suit,⁵⁷ Chancellor Allen made several important observations.

⁴⁶ See *Graham v. Allis-Chalmers Mfg. Co.*, 188 A.2d 125, 130 (Del. 1963).

⁴⁷ See *In re Caremark Intl. Inc. Derivative Litig.*, 698 A.2d 959, 969 (Del. Ch. 1996).

⁴⁸ 188 A.2d at 130.

⁴⁹ *Id.* at 127.

⁵⁰ *Id.* at 130.

⁵¹ *Id.*

⁵² *Id.*

⁵³ *Caremark*, 698 A.2d at 969.

⁵⁴ See *Stone v. Ritter*, 911 A.2d 362, 367-69 (Del. 2006) (tracing the evolution of the assessment of director liability for failing to act in good faith in the discharge of oversight responsibilities and noting that *Graham* set the standard prior to *Caremark*).

⁵⁵ 698 A.2d at 959.

⁵⁶ *Id.* at 961-66.

⁵⁷ *Id.* at 972.

First, Chancellor Allen rebuffed *Graham's* red flag test.⁵⁸ *Graham's* test, according to Chancellor Allen, did not require rigorous enough oversight obligations.⁵⁹ Chancellor Allen noted that director oversight responsibilities include a “duty to attempt in good faith to assure that a corporate information and reporting system, which the board concludes is adequate, exists”⁶⁰ Chancellor Allen went on to write “that failure to do so [establish a corporate information and reporting system] under some circumstances may, in theory at least, render a director liable for losses caused by non-compliance with applicable legal standards.”⁶¹ The duty of a board to establish corporate information and reporting systems was later affirmed by the Delaware Supreme Court in *Stone v. Ritter*.⁶²

3. Board Challenges

Directors are subject to personal liability if they breach any of their duties or fail to satisfy any of their obligations.⁶³ Generally, judicial review of a challenge to board action is subject to the business judgment rule.⁶⁴ The business judgment rule creates a presumption that, in making a business decision, directors have acted on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the corporation.⁶⁵ The party challenging the board has the burden of establishing facts to rebut the business judgment rule's presumption.⁶⁶

⁵⁸ *Id.* at 970.

⁵⁹ *Id.* (“it would, in my opinion, be a mistake to conclude that our Supreme Court’s statement in *Graham* concerning espionage means that corporate boards may satisfy their obligation to be reasonably informed concerning the corporation, without assuring themselves that information and reporting systems exist in the organization that are reasonably designed to provide to senior management and to 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.”).

⁶⁰ *Id.*

⁶¹ *Id.*

⁶² 911 A.2d at 370.

⁶³ See generally Lisa M. Fairfax, *Spare the Rod, Spoil the Director? Revitalizing Directors’ Fiduciary Duty through Legal Liability*, 42 Hous. L. Rev. 393, 410–414 (2005) (providing an overview of the potential liability facing directors and the mechanisms, such as insurance and indemnification clauses, that can be used to protect directors).

⁶⁴ For a detailed discussion of the business judgment rule, see Kenneth B. Davis, Jr., *Once More, The Business Judgment Rule*, 2000 Wis. L. Rev. 573 (2000).

⁶⁵ See Fairfax, *supra* n. 63, at 410 (noting that the business judgment rule protects directors from liability by sanctioning all decisions made in good faith, even if courts disagree with the decisions). *Smith v. Van Gorkom* was an important exception to the business judgment rule. 488 A.2d 858 (Del. 1985). In *Van Gorkom*, the Delaware Supreme Court found a board liable for the breach of its duty of care when the board approved a cash-out merger of its company without undergoing what the court deemed to be a proper decision-making process. *Id.* at 864. For a detailed discussion of *Van Gorkom* and the business judgment rule, see Leo Herzl & Leo Katz, *Smith v. Van Gorkom: The Business of Judging Business Judgment*, 41 Bus. Law. 1187 (1986).

⁶⁶ See Darren C. Skinner, *Director Responsibilities and Liability Exposure in the Era of Sarbanes-Oxley*, 52 Prac. Law. 29, 30 (2006) (noting that under the business judgment rule, the burden is placed on the party challenging a board’s decision to establish facts which rebut the presumption that the board

The business judgment rule's presumption applies to protect directors when a board's *action* is under attack.⁶⁷ The rule does not apply the same way in the case of director *inaction*. In cases of nonfeasance, the business judgment rule's protective presumption applies when a board has made the decision not to take action.⁶⁸ The rule does not provide protection when a board fails to take action and the nonfeasance is not the product of a conscientious decision.⁶⁹

III. THE CASE FOR INCREASED OVERSIGHT RESPONSIBILITIES

This article argues two points.⁷⁰ First, it argues that the boards of companies that are involved in or aspiring to commence international business relations must take on enhanced oversight responsibilities.

Second, this article argues that in order to fulfill these heightened oversight responsibilities, boards have two specific obligations. Boards must respond to red flags that indicate that their companies' international business activities may be susceptible to damaging publicity. Additionally, boards must implement systems that actively monitor for and alert the directors to potentially negative publicity arising from the companies' international business activities.

The need for these heightened oversight responsibilities stems from the losses and problems that companies can incur as the direct result of engaging in certain unpopular international business activities. In addition, recent legal developments support the need for boards to take on greater oversight responsibilities within this realm.

A. Potential Damages, Losses, and Costs

As described in Section II.A, there has been a surge in patriotism and an increased societal focus on national security in the United States since 2001. This trend has created an environment where companies can suffer massive damages and losses as the result

acted on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the corporation).

⁶⁷ See *id.* at 30-31 ((citing *In re Walt Disney Co. Derivative Litig.*, 825 A.2d 275, 278 (Del. Ch. 2003), and observing that the business judgment rule is properly invoked only when a particular action of the board is under attack. The business judgment rule does not provide protection from claims that do not involve directorial decision-making, such as when the directors are charged with failing to exercise proper oversight through inaction).

⁶⁸ Gavin Clarkson, *The Y2K Tsunami: Directors & Officers Should Prepare to Be Deluged*, 5 B.U. J. Sci. & Tech. L. 3, 11 (1999) (discussing, within the context of the Y2K crisis, how the business judgment rule would not protect directors who either abdicated their oversight functions or failed to act without making a conscious decision not to do so).

⁶⁹ *Id.* at 11-12.

⁷⁰ The legal requirements discussed in Sec. II.B were intended to provide background information. My discussion focuses on the case where a company, in its international dealings, is operating inside the technical requirements of the law.

of their international business dealings. A company with international dealings that appear to be damaging to American national security interests is vulnerable to negative publicity and could foreseeably suffer in several ways. First, a company's reputation and brand image could be damaged, causing the company to lose customers. Second, a company may have troubles in its relationships with both institutional and individual investors. Third, a company may have to spend significant resources to try to stop the publicity and repair the damage. An in-depth examination of these potential problems supports the conclusion that a board must take on enhanced oversight responsibilities over its company's international business dealings.

1. Damaged Relations with Customers

Consumers have become increasingly aware and concerned about the companies behind the products and services they are buying.⁷¹ A product of the post 9/11 surge in patriotism and the increased attention on national security in America is the growing trend where many Americans avoid providing financial support to any source that is perceived to be a threat to American national interests.⁷²

Accordingly, publicity linking a company to an international business activity that is perceived to be against American national security

⁷¹ There is a growing trend that more and more consumers are becoming socially conscious. For example, the fair-trade movement, which advocates improved trading, social, and environmental standards and conditions for disadvantaged producers and workers, has become increasingly popular. See generally Jane Black, *Fair Trade Hits Home*, Wash. Post F01 (July 18, 2007) (noting how the fair-trade concept, which initially focused on helping overseas farmers, is becoming a marketing phenomenon for products coming from small farms inside the United States).

The trend of socially responsible consumerism is also illustrated by companies' efforts to divorce themselves from controversial celebrity endorsers. For example, Nike suspended its endorsement deal with football star Michael Vick after reports emerged that Vick was involved in a dog fighting ring. Paul Newberry, *Nike, Reebok Give Vick the Boot*, Wash. Post (July 28, 2007) (available at <http://www.washingtonpost.com/wp-dyn/content/article/2007/07/27/AR2007072701789.html>). Similarly, Reebok, the company which produced Michael Vick's jersey, stopped selling the jerseys shortly after the story broke. *Id.*

⁷² For example, in 2003, there was an American consumer backlash against French goods after the French government opposed international action against the Saddam Hussein-run government in Iraq, a position that many Americans viewed as being against American national interests. Parija Bhatnagar, *French Goods Face U.S. Backlash*, CNNMoney (Mar. 13, 2003) (available at Lexis News & Business library, CNNMoney.com file). Some restaurants, in an effort to avoid being linked to anything French, changed their menus so that their French fries were called "freedom fries." The French-owned Sofitel Hotel stopped flying the French flag outside of its Manhattan hotel as a precautionary measure against consumer backlash. *Id.*

In a different story, 7-Eleven made a major move to avoid being linked to an unpopular foreign business partner. 7-Eleven ended its relationship with Venezuelan-controlled Citgo Petroleum Corp. after Venezuelan President Hugo Chavez made derogatory comments about President Bush during a 2006 visit to the United Nations Headquarters in New York City. In connection with the move, 7-Eleven released the following statement, "Regardless of politics, we sympathize with many Americans' concerns over derogatory comments about our country and its leadership recently made." The Associated Press, *7-Eleven to End Relationship with Venezuela-Backed Citgo*, <http://www.foxnews.com/story/0,2933,216079,00.html> (Sept. 27, 2006).

interests can severely damage a company's reputation and brand image⁷³—and may ultimately hinder the company's ability to successfully sell its products and services.⁷⁴ Further, a company tied to an unpopular international business activity may foreseeably become the subject of a customer boycott.⁷⁵

2. Damaged Relations with Investors

Publicity linking a company to a business relationship with a controversial foreign nation, regime, organization, or individual may create problems for that company in its relations with investors.

Many investors, similar to consumers, have become increasingly interested in the companies and causes their dollars are supporting.⁷⁶ "Social investing" focuses on a range of different causes, such as companies' perceived levels of patriotism, their environmental practices, their treatment of their employees, and their stances on human-rights issues.⁷⁷

Publicity linking a company to a business association that may be viewed as damaging to American national security interests may lead to the following harmful effects on a company's relationships with investors: costly and embarrassing forms of shareholder activism; strained relationships with institutional investors; and the divestment, or selling off, of shares.

a. Shareholder Activism

Corporations with controversial international business relationships and dealings are commonly vulnerable to various forms of costly and

⁷³ The fate of musicians, actors, and celebrities who have made unpatriotic statements is relevant in this discussion. For example, in 2003, Natalie Maines, the lead singer of the Dixie Chicks, told a London audience, "Just so you know, we're ashamed the President of the United States is from Texas." Warren St. John, *The Backlash Grows Against Celebrity Activists*, 152 N.Y. Times § 9 (Mar. 23, 2003). After reports of the comment spread, there was a strong backlash against the Dixie Chicks. *Id.* There was a drop in radio airplay of the band's music, and there were public burnings of Dixie Chicks CDs. *Id.*

⁷⁴ See e.g. St. John, *supra* n. 73 (noting that after Natalie Maines' controversial remark, the Dixie Chicks were the subject of radio boycotts that contributed to a twenty percent drop in airplay of the band's music).

⁷⁵ In a suburban Chicago newspaper's "Speak Out" editorial section, there was a call for a boycott of GE on the basis that "GE is doing business with Iran and is helping Iran kill Americans in the war." Reader Editorial, *Viewpoint: Speak Out: Boycott GE*, *Courier News* A4 (May 23, 2008).

⁷⁶ See Carolyn Cui, *Social Investing Soars Amid More Options*, 251 Wall St. J. C5 (Mar. 6, 2008) (reporting on the growth of socially responsible investing). See also e.g. Trillium Asset Management, *About Us*, <http://trilliuminvest.com/about> (accessed Feb. 16, 2009) (explaining that they are one of several investment firms in existence devoted to socially responsible investing).

⁷⁷ See Jeff Brown, *Save the Earth Sacrifice Your Returns?* Wash. Post F01 (May 13, 2007) (noting that a growing number of investors are considering issues such as the environment and the Darfur conflict when making their investment decisions, and pointing out that socially responsible funds generally earn lower returns compared to other funds).

embarrassing shareholder activism.⁷⁸

For example, in 2003, Halliburton dealt with a disruptive form of shareholder activism when the New York City Pension Fund submitted a resolution for a shareholder vote for the establishment of a board committee to review Halliburton's business dealings with Iran.⁷⁹ In 2002, Conoco-Phillips and General Electric (“GE”) dealt with similar shareholder resolutions when the New York City Police and Fire Department Pension Funds filed similar resolutions seeking review of Conoco-Phillips' operations in Iran and Syria and GE's operations in Iran.⁸⁰

Investment companies with holdings in companies that have controversial international ties can also be the targets of disruptive shareholder activism. In 2007, shareholder activists sent approximately 170,000 e-mails to Fidelity Management & Research LLC (“Fidelity”) in an effort to get the fund to divest its holdings in companies with ties to Sudan.⁸¹ In April 2007, hundreds of activists demonstrated outside of Fidelity's Boston headquarters, a spectacle that created embarrassing publicity for Fidelity.⁸²

b. Institutional Investors

Corporations with controversial international business relationships also face strains in their relationships with large institutional investors.

ii. *Pressure from Institutional Investors*

Many institutional investors have raised objections to companies with ties to certain countries. For example, the New York City Pension Funds recently convinced the Aon Corporation to sever its ties to several nations after the pension funds raised concern over those countries' terrorist-

⁷⁸ While shareholder activism has some positive effects, it can be costly and damaging to corporations when it involves or causes negative publicity, investor complaints and protests, disruptions at annual meetings, and controversial shareholder proposals.

⁷⁹ *NYC Comptroller Mar. 20, 2003 Press Release*, *supra* n. 32 (noting that the SEC refused to state that it would take no action against Halliburton if Halliburton omitted a New York City Pension fund proposal from Halliburton's 2003 proxy materials).

⁸⁰ *Id.* See also General Electric, *General Electric Proxy Statement 2003, Shareholder Proposal No. 13* (Mar. 10, 2003) (available at <http://www.ge.com/jsp/investor/proxy/proposal13.jsp>) (requesting that the board establish a committee to review the company's relationships with Iran with an eye toward the potential damage that the relationships could cause to GE's reputation).

⁸¹ Jennifer Levitz, *Darfur Outrage Spreads to Mutual Funds: Shareholders Get a Say On Ruling Out Investments With Sudan-Linked Stakes*, 251 *Wall St. J.* C15 (Mar. 12, 2008).

⁸² *Id.* The shareholder activism that Fidelity experienced raises some important points. First, it shows that investment companies which do not themselves directly deal with controversial foreign nations can be subjected to negative publicity for their investment in companies that do have such direct foreign relationships. Second, the Fidelity case illustrates the potential for damaged relations between institutional investors and companies with ties to unfavorable foreign countries. For example, the article noted that several mutual funds sold off their shares of PetroChina stock in protest of PetroChina's activities in Sudan. *Id.*

sponsoring activities.⁸³ The California State Teachers' Retirement System recently asked thirteen international energy companies with which it invests to take immediate steps to assess the risks to their business operations in Iran.⁸⁴

Similarly, one of the largest and most powerful unions in the country, the Teamsters, has pressured companies to cut ties to Iran.⁸⁵ James P. Hoffa, the President of the Teamsters, recently sent a letter calling on pension fund managers to screen their funds for companies that do business in Iran.⁸⁶ Hoffa's call to divest from companies doing business in Iran was based on several reasons. Some of these reasons directly relate to American national security interests, such as his objections to Iran's supplying of weapons to insurgent groups in Iraq, its alleged attempts to enrich uranium, and its funding of terrorist groups.⁸⁷

ii. State Laws Limiting Investment

California and Florida are amongst several states that have recently passed laws which limit their state-run pension funds' abilities to invest in companies that have certain international ties.⁸⁸ California's bill divests billions of dollars from the state pension fund from energy and defense companies doing business with Iran.⁸⁹

⁸³ Press Release, William C. Thompson, N.Y.C. Comptroller, *City Pension Funds Prompt Aon to Sever Ties to Iran* (Jan. 23, 2006) (available at http://www.comptroller.nyc.gov/press/2006_releases/pr06-01-008.shtm).

⁸⁴ Cal. St. Teachers' Ret. Sys., *CalSTRS Board Urges Energy Companies to Review Growing Risk of Business in Iran* (June 7, 2007) (available at <http://www.calstrs.com/Newsroom/2007/news060707.aspx>).

⁸⁵ Intl. Bhd. of Teamsters, *Hoffa Calls on Pension Funds to Divest in Companies Conducting Business in Iran* (Aug. 22, 2007) (available at http://www.teamster.org/07news/nr_070822_1.asp) (announcing that Teamsters General President James P. Hoffa wrote to Teamster pension fund managers asking them to divest shares in companies that do business in Iran).

⁸⁶ Ltr. from James P. Hoffa, General President of the Intl. Bhd. of Teamsters, to Pension Fund Managers, *Divesting Pension Funds of Investments in Companies that Do Business with Iran* ¶1 (Aug. 23, 2007) (available at <http://online.wsj.com/public/resources/documents/HoffaIran.pdf?mod=WSJBlog>) (calling on pension fund managers to consider screening their funds for investments in companies doing business in Iran).

⁸⁷ *Id.*

⁸⁸ See generally *Not With My Money; Divestment*, Economist (Oct. 20, 2007) [*Not With My Money*] (noting that the "boomlet in state laws requiring divestment from Iran," which was started by California and Missouri, has inspired other states to consider similar laws). Most state-run funds have actively complied with these state laws. A few, however, have opposed them. Compare Press Release, Teachers' Retirement System of the State of Illinois, *TRS Complies with Divestment Laws* (undated) (available at <http://trs.illinois.gov/subsections/press/trscomplieswithdivestmentlaws.html>) (announcing that the Teachers' Retirement System is in compliance with an Illinois state law prohibiting it from investing in companies that do business in Sudan or Iran) with Press Release, California Public Employees' Retirement System, *CalPERS Opposes Iran Divestment Legislation* (May 14, 2007) (available at <http://www.calpers.ca.gov/index.jsp?bc=/about/press/pr-2007/may/oppose-iran-divestment.xml>) (reporting that CalPERS voted to oppose California legislation prohibiting investment in Iran because it would limit the decision-making authority of CalPERS' board).

⁸⁹ Jonathan Alter, *Before We Bomb Iran...*, Newsweek 45 (Oct. 22, 2007) (noting that in California, Governor Schwarzenegger signed a state bill that divested close to \$24 billion in pension fund assets from energy and defense companies doing business with Iran).

Florida's bill screens its state pension funds for holdings in companies with ties to Iran's oil sector.⁹⁰ Missouri has taken a slightly different approach and has created an investment fund which screens out companies with ties to terror nations.⁹¹

c. Divestment

Another risk facing companies with controversial international dealings is the risk that investors will divest, or sell off, their shares in protest of the international ties. Sometimes, a company with controversial foreign ties can become the subject of a large scale divestment campaign.⁹²

One of the most well-known divestment campaigns encourages investors to sell their shares in companies that have ties to nations linked to terrorism.⁹³ This “Divest Terror” campaign has had mixed results in terms of reaching its goal of forcing companies to cut ties with terror-linked nations and causing nations to change their policies.⁹⁴

Nonetheless, the Divest Terror campaign has contributed to some noticeable changes in the private investment industry. For example, the Conflict Securities Advisory Group (“CSAG”), a research and consulting

⁹⁰ Hilary Leila Krieger, *Florida Becomes First US State to Pass Iran Divestment Bill*, Jerusalem Post (May 4, 2007), <http://www.jpost.com/servlet/Satellite?cid=1178198609606&pagename=JPost%2FJPArticle%2FShowFull>.

⁹¹ Sarah Steelman, *Terror-Free Investing*, 268 Wall St. J. A21 (Dec. 14, 2006) (describing how, under the leadership of its state treasurer (the article's author), Missouri has created the Missouri Investment Trust, a terror-free investment fund).

⁹² “Divestment campaigns” are public relations efforts carried on by individuals and organizations for the purpose of persuading individual and institutional investors to divest their holdings in companies that engage in practices or maintain relationships considered objectionable by the particular individuals or organizations. For example, during the 1970s and 1980s, there was a large scale divestment campaign levied against companies doing business in South Africa to protest the South African apartheid government. See generally Nora Boustany, *Sudan Divestment Effort Gains Momentum at State Level*, Wash. Post A12 (Oct. 7, 2006) (describing the efforts to bring change in Sudan through a divestment campaign, and noting that the South African divestment campaign helped end apartheid).

⁹³ See e.g. The Ctr. for Sec. Policy, *Divest Iran*, <http://www.centerforsecuritypolicy.org/p11717.xml> (May 30, 2006) (discussing how a task force led by the Treasury Department sought to convince allies to avoid doing business with Iran and other entities with connections to terrorism. Also stating that the Louisiana Sheriffs' public pension fund agreed not to invest in companies that engage in commercial activities with countries like Iran). See generally Alter, *supra* n. 89 (reporting on the anti-terror divestment campaign).

⁹⁴ Compare Perelman, *supra* n. 30 (describing the anti-terror divestment movement as having only limited success so far); *Not With My Money*, *supra* n. 88 (describing how one expert feels that divestment is unlikely to change Iranian policy because any economic pain caused by companies cutting ties with Iran will be mitigated by Chinese and Russian companies filling the gap), with Ltr. from Patrick G. Ryan, Exec. Chairman, Aon Corp., to William C. Thompson, Jr., Comptroller, The City of N.Y., (Jan. 19, 2006) (copy on file with *Dayton Law Review*) (communicating to a group of New York City pension funds that the Aon Corporation suspended its business activities with Iran because of the financial and reputational risks which the pension funds were concerned would be incurred by Aon); Henry Goldman, *Halliburton Won't Seek Iran Work*, Wash. Post E02 (Mar. 25, 2005) (reporting that Halliburton's pledge not to seek new work in Iran was based in part on the pressure put on the company by several New York City pension funds).

firm based in Washington, D.C., was recently created.⁹⁵ CSAG advises asset management firms, corporations, public pension systems and others on how to assess and manage global security risk issues.⁹⁶ In addition, the Roosevelt Anti-Terror Multi-Cap Fund was recently created.⁹⁷ This fund purported to provide investors with the first mutual fund comprised entirely of investments in companies without any ties to terror-linked nations.⁹⁸

Stopping companies from maintaining international business ties with countries and partners that are against United States national security interests is a topic that was addressed by several candidates in the 2008 presidential election. For example, Barack Obama and John McCain both voiced support for divestment from companies doing business in Iran.⁹⁹

3. Resources Spent to Repair Damages

In addition to the initial damages incurred with regards to customer and investor relations, a company could be forced to spend vast resources on projects and programs to restore their damaged reputations.¹⁰⁰

The case of the Ford Motor Company and its ties to the Nazi government in Germany demonstrates the costs that a company can incur to restore its image after being linked to an unpopular foreign partner.

In 1998, reports surfaced that Ford maintained business

⁹⁵ Conflict Securities Advisory Group, *Home*, <http://www.conflictsecurities.com> (accessed Apr. 11, 2008).

⁹⁶ *Id.*

⁹⁷ Roosevelt Multi-Cap Fund, *Homepage*, <http://rooseveltmcf.com> (accessed Feb. 16, 2009). On July 10, 2008, the Roosevelt Anti-Terror Multi-Cap Fund changed its name to the Roosevelt Multi-Cap Fund. Roosevelt Multi-Cap Fund, *Welcome*, <http://www.anti-terrorfund.com> (accessed March 30, 2009).

⁹⁸ Roosevelt Anti-Terror Multi-Cap Fund, *Prospectus 1* (Mar. 31, 2008).

⁹⁹ See Jay Solomon & Elizabeth Holmes, *Iran Emerges as Key Issue in Jewish Vote*, 251 Wall St. J. A8 (June 3, 2008) (noting that McCain voiced support for an international divestment campaign from companies doing business in Iran and that Obama sponsored legislation aimed at forcing divestment from Iran).

Divestment in companies with international ties that are opposed to United States national security interests was a topic that was addressed in several other capacities during the 2008 Presidential election. Mitt Romney arranged a meeting between a former Israeli prime minister and the Massachusetts State Treasurer so that the former prime minister could ask the State Treasurer to divest Massachusetts' pension fund investments from companies that do business in Iran. Thanassis Cambanis & Scott Helman, *Romney Talks Tough on Iran in Israel, Courts US Jewish Vote*, Bost. Globe B3 (Jan. 24, 2007). Cindy McCain, the wife of John McCain, divested her mutual fund holdings in companies with ties to Sudan, a country maligned for its genocide and ties to international terrorism. Jim Kuhnhehn, *McCain's Wife Sells Funds with Holdings in Sudan*, Wash. Post A08 (May 15, 2008).

¹⁰⁰ An interesting example of corporations having to spend significant resources to restore their damaged reputations occurred recently when it came to light that several prominent American banks had ties to the American slave trade. In 2005, Wachovia, J.P. Morgan Chase & Co., and several other major banks acknowledged that their predecessor banks used slaves as collateral for loans. The banks went to great lengths to stop the bad publicity and restore their reputations. Wachovia hired an expert to search its historical records and compile a 111-page report on its involvement in the slave trade. J.P. Morgan Chase created a \$5 million dollar college scholarship for African-American Students in Louisiana. Nick Godt, *J.P. Morgan & Co. Sued for Profiting From Slavery*, N.Y. Sun, Sept. 26, 2006 (available at <http://www2.nysun.com/article/40357>); Darryl Fears, *Seeking More Than Apologies for Slavery: Activists Hope Firms' Disclosure of Ties Will Lead to Reparations*, Wash. Post A01 (June 20, 2005).

relationships with the Nazi government during the 1930s and 1940s.¹⁰¹ The reports stated that Ford's German subsidiary, Ford-Werke, used slave laborers at its Cologne, Germany plant.¹⁰²

To halt the negative publicity and restore its damaged image, Ford spent a significant amount of money to investigate its past. Ford hired an accounting firm to investigate its old financial records; it commissioned a college professor to produce a comprehensive research report documenting the history of its German subsidiary during the Nazi era; and it even hired a third-party researcher to independently assess the validity of the research report.¹⁰³ In addition, Ford made large contributions towards human-rights research¹⁰⁴ and to a fund to aid the victims of World War II.¹⁰⁵ The Ford case demonstrates that companies are sometimes forced to spend huge amounts of time, money, and energy to fix the damage that arises from controversial international business dealings.

B. Legal Support

1. Case Law

The *Caremark* case is widely acknowledged as standing for the proposition that directors have elevated oversight responsibilities.¹⁰⁶ The *Caremark* court emphasized that a board's oversight and monitoring responsibilities are no longer only triggered when red flags capture a board's attention.¹⁰⁷ The court prescribed a more active role which boards must perform in order to satisfy their oversight responsibilities.¹⁰⁸ A board must create and maintain information and reporting systems that provide accurate information to allow both the board and management to reach informed judgments about a company's legal compliance and its business performances.¹⁰⁹

¹⁰¹ Michael Dobbs, *Ford and GM Scrutinized for Alleged Nazi Collaboration*, Wash. Post A01 (Nov. 30, 1998).

¹⁰² Keith Bradsher, *Suit Charges Ford Profited by Nazi-Era Forced Labor*, 167 N.Y. Times D5 (Mar. 5, 1998).

¹⁰³ See Ford Motor Company, *Ford Issues Report on Ford-Werke Under the Nazi Regime* (Dec. 6, 2001) (available at http://media.ford.com/article_display.cfm?article_id=10374#rel).

¹⁰⁴ Ford Motor Company, *Ford Contributes \$4 Million toward Forced and Slave Labor Studies and Humanitarian Relief* (Dec. 6, 2001) (available at http://media.ford.com/article_display.cfm?article_id=10375).

¹⁰⁵ Press Release, Ford Motor Company, *Ford-Werke AG Joins German Fund to Aid WWII Victims* (Sept. 2007) (copy on file with Dayton Law Review).

¹⁰⁶ See generally Geoffrey Christopher Rapp, *A New Direction for Shareholder Environmental Activism: The Aftermath of Caremark*, 31 Wm. & Mary Envtl. L. & Pol'y Rev. 163, 174 (2006) (noting that the *Caremark* decision influenced other courts' understandings of the duty of care); Regina F. Burch, *Director Oversight and Monitoring: The Standard of Care and the Standard of Liability Post-Enron*, 6 Wyo. L. Rev. 481, 492 (2006) (noting that *Caremark* rejected the common interpretation that directors "needn't put in place" information systems to comply with their oversight duties).

¹⁰⁷ *Caremark*, 698 A.2d at 970.

¹⁰⁸ *Id.*

¹⁰⁹ *Id.*

In *Caremark*, a company sustained losses as the result of its violation of Anti-Referral Payment Laws.¹¹⁰ There is, however, little reason to limit *Caremark*'s premise of increasing oversight responsibilities to the narrow context of a company's compliance with legal requirements. The *Caremark* court's emphasis was to force boards to become more active in their oversight and monitoring duties.¹¹¹ The court sought to expand the scope of board oversight responsibilities so that directors could no longer sit back and satisfy their duties "without assuring themselves that information and reporting systems exist" to alert them to potential issues requiring their attention.¹¹²

The *Caremark* approach can logically be extended such that boards must play a more active role in overseeing their companies' international business dealings.¹¹³ The losses and damage that a company can sustain from publicity stemming from its international business activities is one of the numerous examples where corporate losses could have been prevented by greater board oversight. Accordingly, boards must monitor their companies' international business affairs for indications that their companies could be exposed to negative publicity.¹¹⁴

2. The Corporate Director's Guidebook

The *Director's Guidebook* alludes to the conclusion that directors must take on elevated oversight responsibilities over their corporations' international business dealings.¹¹⁵ The following examples illustrate the *Director's Guidebook*'s support for such increased board oversight responsibilities:

- The *Director's Guidebook* notes specific risk and compliance oversight programs, which it suggests that directors consider implementing.¹¹⁶ Listed within this section are issues that relate to corporations' reputations amongst socially conscious consumers and investors, such as political activities and environmental issues.¹¹⁷ The *Director's Guidebook* recommends that boards consider establishing risk and compliance oversight programs that relate to corporations' reputations amongst socially conscious consumers and

¹¹⁰ *Id.* at 961-62.

¹¹¹ *Id.* at 970.

¹¹² *Id.*

¹¹³ *Id.*

¹¹⁴ An interesting example of this concept is found in the context of how boards prepared for the Y2K crisis. See Clarkson, *supra* n. 68, for a discussion of how the *Caremark* case and the duty of reasonable inquiry indicated that directors and officers were required to take an active role in their companies' assessments of Y2K risks.

¹¹⁵ *Director's Guidebook*, *supra* n. 3, at 1489-90.

¹¹⁶ *Id.* at 1501-03.

¹¹⁷ *Id.*

investors.¹¹⁸ This recommendation extends to this Article’s focus on international business dealings, which could be seen as relevant to United States national security interests. As described in Sections III.A.1 and III.A.2., consumers and investors commonly take into account whether the products and investments they support contribute to causes that are considered unpatriotic or a threat to American national security interests. Accordingly, this section of the *Director’s Guidebook* supports this Article’s argument that boards must take on greater oversight responsibilities over their companies’ international business dealings.¹¹⁹

- The *Director’s Guidebook* alludes to the *Caremark* case’s requirement of increased director oversight responsibilities in its discussion of necessary director inquiry.¹²⁰ The *Director’s Guidebook* states that even where “there are no red flags, directors should satisfy themselves periodically that the corporation maintains procedures that are appropriately designed to identify and manage business risks and are reasonably effective in maintaining compliance with laws and corporate policies and procedures.”¹²¹ The discussion in Section III of how companies can lose customers and investors, necessitating the use of vast resources to repair the damage, closely relates to the *Director’s Guidebook’s* suggestion that directors maintain procedures to identify and manage “business risks.”
- The *Director’s Guidebook* lists the following tasks as amongst those which a board and its committees must perform under a board’s oversight function: “understanding the corporation’s risk profile and reviewing and overseeing risk management programs”¹²² and “establishing and monitoring effective compliance systems and policies for ethical conduct.”¹²³ Again, as discussed in Section III, a company’s international business affairs can expose it to various risks. Therefore, the *Director’s Guidebook’s* assertion that the board understand its corporation’s risk profile supports this Article’s argument.
- The *Director’s Guidebook* states that the “material risk and liability contingencies, including industry risk, litigation, and regulatory matters” are amongst the areas in which a director must have an understanding in order to be effective in his or her oversight

¹¹⁸ See *id.*

¹¹⁹ See *id.*

¹²⁰ *Id.* at 1496.

¹²¹ *Id.*

¹²² *Id.* at 1491.

¹²³ *Id.*

functions.¹²⁴ This section of the *Director's Guidebook* is relevant to this Article in the sense that in fulfilling their enhanced oversight responsibilities over their companies' international business affairs, directors should be aware of the various legal restrictions on international business dealings.¹²⁵

IV. MEETING THE INCREASED OVERSIGHT RESPONSIBILITIES

To fulfill the increased oversight responsibilities, a board should both (1) respond to events brought to its attention that indicate that the company could be subject to negative publicity due to its international business dealings and (2) put into place programs and systems ("monitoring systems") to monitor for and alert the board to indications that the company's international business activities could lead to negative publicity.¹²⁶

This Section of the Article will provide practical recommendations on how a board can fulfill these responsibilities. As to the first requirement, the duty to respond to red flags, this Section describes five events that should capture a board's attention and cause it to closely monitor its company's international activities and relationships.

This Section also provides recommendations on how a board can fulfill the second requirement, the creation of an effective monitoring system. This Section suggests several strategies and tactics which boards could use in the creation of an effective monitoring system. It concludes by identifying some of the major areas and issues of which a monitoring system should be vigilant.

A. Red Flags

The following are five examples of events and circumstances that would serve as red flags to alert a board that it should closely monitor the international business dealings of its company.

1. Relationship with a Government-Designated Trading Partner

The board of any company with any relationship, direct or indirect,¹²⁷ to a nation, organization, or individual named in the Treasury

¹²⁴ *Id.* at 1492.

¹²⁵ See Sec. III.B. for a discussion of the U.S. legal limitations on business dealings with certain countries and international partners.

¹²⁶ *Caremark*, 698 A.2d at 970. To fulfill their oversight responsibilities, boards must still respond to red flags that come to their attention, even with the *Caremark*-prescribed monitoring systems in place.

¹²⁷ Included within this category would be a company whose relationship with a designated trading partner was through the use of a subsidiary, affiliate, or any other director or indirect arrangement. See *supra* n. 32 and accompanying text.

Department's Specially Designated National's List¹²⁸ or the State Department's State Sponsors of Terrorism List,¹²⁹ should be on alert that the company's dealings in that country or with that trading partner require monitoring. Any relationship, even one within the technical requirements of the law, with a country or a trading partner named in one of the government watch lists is subject to government, media, consumer, and investor scrutiny and concern.¹³⁰ Accordingly, the board of a company that has any tie to an entity named in one of these lists should be alerted that it must exercise its oversight responsibilities and monitor the company's dealings with that nation or partner.

2. World Events

The occurrence of certain world events should alert a board that its company's international business relationships could expose the company to negative publicity.¹³¹

A hypothetical is helpful to illustrate this red flag. If, for example, DefenseTech¹³² sold military technology to the Greek government, the DefenseTech board would have no reason to actively monitor DefenseTech's dealings with the Greek government. No special oversight would be necessary since Greece is an ally of the United States, and Greece does not have any major ties to terrorism, anti-Americanism, human-rights violations, or any other controversial issue.

However, certain major world events may lead the DefenseTech board to have to specifically monitor DefenseTech's sale of military technology to the Greek government. For example, if the Greek government became involved in a war or conflict, then DefenseTech's sale of military technology to the Greek government would be susceptible to increased government, media, and public scrutiny. In this hypothetical situation, the events leading to Greece's involvement in the conflict should act as red flags to alert DefenseTech's board that DefenseTech's relationship with the

¹²⁸ See U.S. Dept. of the Treas. Off. of For. Assets Control, *Specially Designated Nationals List*, <http://www.ustreas.gov/offices/enforcement/ofac/sdn/index.shtml> (accessed Apr. 5, 2008).

¹²⁹ See U.S. Dept. of St., *State Sponsor of Terrorism List*, <http://www.state.gov/s/ct/c14151.htm> (accessed Jan. 3, 2009).

¹³⁰ For example, GE was scrutinized by the media and the government for its dealings with Iran. See *The O'Reilly Factor*, "Is NBC's Parent Company Doing Business with Iran?" (Fox News Network Jan. 11, 2001) (TV broad., transcr. available at <http://www.foxnews.com/story/0,2933,321987,00.html>); *The O'Reilly Factor*: "Iran, General Electric and The New York Times" (Fox News Network Apr. 15, 2008) (TV broad., transcr. available at <http://www.foxnews.com/story/0,2933,351332,00.html>); Ltr. from Michael McAlevy, Chief Corp. and Secs. Counsel, Gen. Elec. Co., to Cecelia D. Blye, Chief, Off. Global Sec. Risk, U.S. Sec. and Exch. Comm., *Form 10-K for Fiscal Year Ended December 13, 2005* 1 (July 14, 2006) (available at <http://ir.10kwizard.com/download.php?format=PDF&ipage=5098923&source=329>) (providing GE's official response to the SEC's comment letter that asked about GE's business relationships with and activities in Iran and Syria).

¹³¹ The following are examples of such world events: terrorist attacks, large scale civil uprisings, mounting tensions, conflicts, and large scale anti-American sentiment.

¹³² "DefenseTech" is a fictitious company.

Greek government could attract scrutiny and may result in negative publicity. Accordingly, the DefenseTech board would have to exercise heightened oversight responsibilities and actively monitor DefenseTech's relationship with the Greek government.

The existence of these red flags would vary on a case-by-case basis according to (1) the country or international partner involved; (2) the nature of the partner, whether it be a government or a private party; and (3) the nature of the products or services that the company was selling.¹³³

3. High Profile Media Report

A high profile media report tying a company to an objectionable international business relationship should act as a red flag to trigger a company's oversight responsibilities.

For example, in 2004, *60 Minutes* aired a program investigating the business relations between American companies such as Halliburton, Conoco-Phillips, and "rogue nations" like Iran.¹³⁴ In 2008, *The O'Reilly Factor* aired several stories covering GE's allegedly unpatriotic business ties to Iran.¹³⁵ The January 11, 2008 edition of *The O'Reilly Factor* story aired footage of a reporter approaching GE's Chief Executive and Chairman of the Board, Jeffrey Immelt.¹³⁶ The footage showed the reporter asking Immelt if GE was still trading with Iran despite the fact that "Iranians are killing Americans in Iraq."¹³⁷

These media reports should have alerted the boards of Halliburton, Conoco-Phillips, and GE that their companies' international business ties were exposing their companies to scrutiny and harmful publicity. Accordingly, those boards should have been put on notice that special oversight was necessary over their companies' international affairs.¹³⁸

4. Government Investigation or Inquiry

A government investigation or inquiry into a company's international business activities should alert that company's board that its

¹³³ There would be a different degree of concern or level of publicity based on the nature and use of the product or service involved. For example, if the company were selling humanitarian supplies to an unpopular foreign government, the company would likely be exposed to less negative publicity than if it were selling military parts.

¹³⁴ *60 Minutes: Doing Business with the Enemy* (CBS Aug. 29, 2004) (TV broad.).

¹³⁵ *Is NBC's Parent Company Doing Business with Iran?*, *supra* n. 130; *Iran, General Electric and The New York Times*, *supra* n. 130.

¹³⁶ *Is NBC's Parent Company Doing Business with Iran?*, *supra* n. 130.

¹³⁷ *Id.*

¹³⁸ In the case where a company was already operating in a country known to have terror ties, the mere fact that the company is operating in that country should put that company's board on alert to exercise its oversight responsibilities. If a high profile media report were to then come forth, the media report would act as an additional red flag triggering an even closer level of board oversight over the company's activities in that country.

international activities are raising questions and special oversight is necessary. For example, in 2006, the SEC's Office of Global Security sent a letter to GE inquiring into the company's business dealings in Iran and Syria.¹³⁹ This inquiry should have served as a red flag to put the GE board on notice that its international business dealings were under scrutiny and that it should exercise greater oversight over GE's international business activities.¹⁴⁰

5. Scrutiny of Another Company

A high profile media report tying another company to an objectionable international business relationship should capture the attention of boards of other companies that maintain similar international business ties.¹⁴¹ Similarly, a high profile government investigation into another company's international business relations should also capture the attention of boards of other companies with similar international business ties.¹⁴² After learning that another company has become the subject of a high profile media report or government investigation relating to its international business dealings, a conscientious and attentive board should understand that its company's own foreign relationships could expose that company to the same sort of bad publicity and that it should exercise greater oversight responsibilities.¹⁴³

B. Monitoring Systems

1. Components

The *Caremark* court indicated that a board must put into place monitoring systems designed to monitor and alert it to issues requiring board

¹³⁹ Ltr. from Michael McAlevey, Chief Corp. and Secs. Counsel, Gen. Elec. Co., to Cecelia D. Blye, Chief, Off. Global Sec. Risk, U.S. Sec. and Exch. Comm., *Form 10-K for Fiscal Year Ended December 13, 2005* 1 (July 14, 2006) (available at <http://ir.10kwizard.com/download.php?format=PDF&ipage=5098923&source=329>) (providing GE's official response to the SEC's comment letter that asked about GE's business relationships with and activities in Iran and Syria).

¹⁴⁰ *Id.*

¹⁴¹ See Daniel R. Roach, *The Board of Directors' Role in Compliance and Ethics*, 9 No. 6 J. Health Care Compl. 49, 50 (Nov.-Dec. 2007). Roach suggested that one approach a board could take to effectively exercise its oversight responsibilities over its organization's compliance program would be to simply "read the newspaper and ask questions." *Id.* at 50. Roach advised directors who have read about another company's compliance problems to question their own companies' management about the prevention of a similar occurrence. *Id.* at 52.

¹⁴² *Id.* at 50. A critical distinction must be made between this red flag and the red flag described in Section IV.A.4. Section IV.A.4 stated that any government investigation into a company's foreign business relationships should trigger the oversight responsibilities of that company's board. In contrast, this Section states that any *high profile* government investigation into a company's foreign business relationship should trigger the oversight responsibilities of the boards of other companies with similar foreign business relationships. This section mandates that the government investigation be high profile because otherwise, there is a possibility that the boards of the other companies would not learn of the investigation of the company.

¹⁴³ See *supra* Sec. IV.A.4.

oversight and attention.¹⁴⁴ In order to fulfill this requirement, the *Caremark* court wrote that a board must make a good faith effort to ensure that the monitoring system “is in concept and design adequate to assure the board that appropriate information will come to its attention in a timely manner as a matter of ordinary operations”¹⁴⁵ Therefore, there is no single, uniform monitoring system that all companies must put into place.¹⁴⁶ Different companies’ systems can have different components, characteristics, functions, and degrees of complexity, based on the individual circumstances and needs of each company.¹⁴⁷

There are, however, several strategies and tactics which most boards could utilize in the creation of a monitoring system that would effectively monitor and alert directors to potential problems and issues relating to the company’s international business activities.

a. Internet Searches

First, the use of simple Internet search engines can give directors and management an idea as to whether a company’s international activities are raising objections or questions.¹⁴⁸ Simple Internet searches can be performed quickly and regularly and can provide fairly comprehensive information.¹⁴⁹ Internet searches can comb for mentions of the company’s international relationships and activities in news reports, investor reports, and watchdog sites.¹⁵⁰ Additionally, there are several prominent blogs¹⁵¹ that report on corporate news and could be searched on a regular basis with minimal expense or trouble.¹⁵² The sites of shareholder activists also can be searched for indications of objections to a company’s international business activities.¹⁵³

¹⁴⁴ *Caremark*, 698 A.2d at 970.

¹⁴⁵ *Id.*

¹⁴⁶ *See id.*

¹⁴⁷ *See Rapp, supra* n. 106, at 173 (stating that “the exact mechanics of such systems are left to the board’s business judgment”).

¹⁴⁸ *E.g.* Google, <http://www.google.com>.

¹⁴⁹ *Id.*

¹⁵⁰ *Id.*

¹⁵¹ *See generally e.g.* Instigator Blog, Entrepreneurship, Business, Social Media & Marketing, <http://www.instigatorblog.com> (accessed Apr. 5, 2008); Prudent Investor, <http://prudentinvestor.blogspot.com> (accessed Apr. 5, 2008); Credo Advisors, Corporate Social Responsibility, <http://credoadvisors.com/blog/category/corporate-social-responsibility> (accessed Apr. 5, 2008).

¹⁵² One popular tool for monitoring blogs is Technorati. Technorati is an Internet tool that purports to track “112.8 million blogs and over 250 million pieces of tagged social media.” Technorati, *Welcome to Technorati, About Us*, http://web.archive.org/web/20071226003737rn_1/technorati.com/about (accessed Dec. 26, 2007).

¹⁵³ For example, SocialFunds, a website devoted to socially responsible investing, features information on socially responsible mutual funds, community investments, corporate research, shareowner actions, and daily social investment news. SRI World Group, Inc., *SocialFunds.com: The Largest Personal Finance Site Devoted to Socially Responsible Investing*, <http://www.socialfunds.com> (accessed Apr. 28, 2008).

In addition, there are several free services which provide up-to-the-minute alerts when certain words or phrases appear on the Internet.¹⁵⁴ A board could use such alert services to stay current on what is being written or said about its company.¹⁵⁵

b. Outside Experts and Consultants

There are various experts and consultants that could be hired by a board to help build an effective monitoring system:

- There are several companies specializing in the field of “competitive intelligence,” that could provide valuable publicity tracking services.¹⁵⁶ These competitive intelligence providers would be helpful in quickly identifying reports, accusations, and rumors of objectionable international business relationships and activities.¹⁵⁷
- There are experts who evaluate and help manage the investor relations issues that arise from a company’s international business activities.¹⁵⁸ In addition, these experts could evaluate the international business relationships that a company is considering entering.¹⁵⁹
- There are international risk consultants who offer analysis of geopolitical conditions and provide advice on future events that could expose a company to negative publicity.¹⁶⁰ Such forward-looking information would be valuable to assist a company in evaluating, analyzing, and managing its exposure to risk in countries and regions in which it currently has business ties, but which do not presently pose a risk of bad publicity.¹⁶¹ These international risk consultants could evaluate the international business relationships that a company is considering entering.¹⁶²

¹⁵⁴ E.g. Google, *Google Alert*, <http://www.google.com/alerts> (accessed Feb. 18, 2009).

¹⁵⁵ *Id.* See generally Dennis Kennedy, *Really Simple Competitive Intelligence, Alerts to Keep You on Top of What Is Client Needs*, ABA J., (Mar. 2008), http://www.abajournal.com/magazine/really_simple_competitive_intelligence. (providing practical tips for gathering competitive intelligence).

¹⁵⁶ For example, Fuld & Company offers competitive intelligence gathering services and tools such as the Internet Intelligence Index, a tool that provides users with links to over 600 intelligence-related websites. Fuld & Co., *Internet Intelligence Index, CI Reference Center, CI Toolbox*, <http://www.fuld.com/Tindex/HomePage.html> (accessed Apr. 5, 2008).

¹⁵⁷ *Id.*

¹⁵⁸ For example, the Conflict Securities Advisory Group specializes in the assessment and management of global security risks. Conflict Securities Advisory Group, *Home*, <http://www.conflictsecurities.com> (accessed Apr. 5, 2008).

¹⁵⁹ *Id.*

¹⁶⁰ For example, Aon is a consulting firm which offers a range of crisis consulting services including the evaluation and management of international political risk. Aon, *Aon Corporation, Aon Advantage*, <http://www.aon.com/about-aon/company-overview.jsp> (accessed Apr. 5, 2008).

¹⁶¹ *Id.*

¹⁶² *Id.*

- Several companies and law firms offer internal and external investigation services.¹⁶³ These investigators could provide a host of valuable information to help a board identify potential risk areas in the realm of its company's international business affairs.¹⁶⁴ These investigators could assist a company in several ways: (1) scrutinizing the company's existing international activities to ensure that the company is in compliance with domestic and international laws and regulations; (2) monitoring the company's foreign business partners and their affiliations; and (3) investigating the ultimate end uses of the company's products and services to determine if the end uses could expose that company to controversy.¹⁶⁵

2. Issues

Similar to how the components of an effective monitoring system differ, the specific issues that the systems should be designed to monitor and identify would also vary on a case-by-case basis.¹⁶⁶ Nonetheless, there are several specific areas all monitoring systems should constantly be evaluating.

a. Legal and Regulatory Requirements

Monitoring systems should be designed to monitor the company's compliance with all relevant legal and regulatory requirements, such as the following:¹⁶⁷

- Compliance with the requirements of the federal economic sanction programs.¹⁶⁸
- Compliance with applicable federal and state securities laws and exchange requirements.¹⁶⁹

¹⁶³ For example, the law firm of Akin Gump Strauss Hauer & Feld LLP has a prominent Export Controls and Economic Sanctions practice that provides a wide range of services dealing with the administrative, public policy, regulatory, and litigation issues of conducting international business. Akin Gump Strauss Hauer & Feld LLP, *Practices & Services Export Controls and Economic Sanctions*, <http://www.akingump.com/services/ServiceDetail.aspx?service=300> (accessed Jan. 3, 2009).

¹⁶⁴ *Id.*

¹⁶⁵ *Id.*

¹⁶⁶ See *Caremark*, 698 A.2d at 970.

¹⁶⁷ This Article focuses on the case where a company is operating within the technical requirements of the law. For the sake of completeness Section IV.B.2.a. is included, indicating that a monitoring system should be mindful of potential areas where a company is not in compliance with legal and regulatory requirements.

¹⁶⁸ See *supra* Sec. II.B.

¹⁶⁹ A monitoring system designed to monitor a company's compliance with legal obligations would follow the precise guidance of the *Caremark* case, where the court specifically dealt with a situation where applicable legal requirements were not met. *Caremark*, 698 A.2d at 970.

b. Public Relations Issues

Monitoring systems should be designed to monitor a wide range of media for mentions of a company's international dealings and relationships. Some forms of media that these sweeps should focus on are:

- Book, newspaper, magazine, and television pieces raising issues with the company's international business dealings and relationships.¹⁷⁰
- The Internet for questions or complaints relating to the company's international business dealings and relationships. These Internet searches should include numerous websites and blogs devoted to general business industry news,¹⁷¹ investing,¹⁷² and corporate social responsibility.¹⁷³
- The activities, websites, and press releases of watchdog groups for indications of questions or complaints about a company's international business dealings and relationships.¹⁷⁴
- The questions asked or concerns raised to the company or its representatives about the company's international business dealings and relationships.¹⁷⁵

c. Investor Relations

Monitoring systems should be designed to search for indications of institutional and individual investor concern relating to a company's international business dealings.¹⁷⁶ Specifically, a monitoring system should focus on the following:

- Institutional investors' policies, communications, and attitudes with respect to business relationships involving certain countries or international partners;¹⁷⁷
- Indications of damaging shareholder activism relating to the company's international relationships or dealings;¹⁷⁸
- Federal and state laws limiting investment in companies with certain international practices or relationships.¹⁷⁹

¹⁷⁰ See e.g. *Is NBC's Parent Company Doing Business with Iran?*, *supra* n. 130; *Iran, General Electric and The New York Times*, *supra* n. 130.

¹⁷¹ For example, the Instigator Blog tracks "startup, entrepreneurship & social media insight." Instigator Blog, *supra* n. 151.

¹⁷² For example, The Prudent Investor analyzes financial and political news with a particular focus on international and globalization issues. The Prudent Investor, *supra* n. 152.

¹⁷³ For example, Credo Advisors is a website with a blog that specifically tracks corporate social responsibility. Credo Advisors, *supra* n. 151.

¹⁷⁴ See e.g. Ctr. for Sec. Policy, *Center for Security Policy*, <http://www.centerforsecuritypolicy.org/index.xml> (accessed Feb. 18, 2009).

¹⁷⁵ For example, when a reporter questioned GE's CEO about GE's business dealings with Iran. See *Is NBC's Parent Company Doing Business with Iran?* *supra* n. 130.

¹⁷⁶ See *supra* Sec. III.A.2.

¹⁷⁷ See *supra* Sec. II.A.2.b.

¹⁷⁸ See *supra* Sec. III.A.1-2.

d. Forecasting

Monitoring systems should also be designed to attempt to forecast potential problems.¹⁸⁰ The following are some of the key issues that companies should attempt to predict:

- The consideration of and promulgation of federal and state laws and private rules that limit or affect investment in companies with certain international business practices or relationships;¹⁸¹
- The consideration of and promulgation of federal economic restriction laws and securities laws relevant to the company's foreign operations;¹⁸² and
- Emerging world and geopolitical events that could affect the company's relationships with foreign business partners and potentially expose the company to scrutiny and negative publicity.¹⁸³

V. CONCLUSION

Corporations competing in today's global market are exposed to a rising number of risks to their reputations from their international business activities and relationships. In light of these increasing risks and some recent legal developments, boards should exercise greater oversight over their corporations' international dealings. To exercise these increased oversight responsibilities, directors must respond to events that come to their attention indicating that board oversight is necessary. In addition, directors must put into place monitoring systems to alert them to the risks arising from their corporations' international dealings.

¹⁷⁹ For example, state laws which limit where state pension funds can be invested. See discussion *supra* Sec. III.A.2.b.ii.

¹⁸⁰ I acknowledge that there is no direct reference in the case law that a monitoring system must have forecasting capabilities. Nonetheless, in light of the wide-ranging damage that a company can sustain as the result of its international business activities, boards should attempt to predict the future risks to which their companies could be exposed.

¹⁸¹ For example, state laws that limit where state pension funds can be invested. See *supra* Sec. III.A.2.a.

¹⁸² See *supra* Sec. II.B. Again, outside experts can provide specialized assistance. For example, the Washington, DC-based law firm, Wiley Rein LLP, can provide analysis of legislative announcements and legislative proposals that are being considered by Congress. See John B. Reynolds, III, Christopher B. Weld, & Matthew Fogarty, *Bills Introduced to Further Restrict Investment in Iran and Sudan*, http://wileyrein.com/publication.cfm?publication_id=13019 (Mar. 23, 2007) (providing an overview of legislative proposals which would authorize state sanctions against Sudan and penalize third-party investment in Iran).

¹⁸³ See Aon, *supra* n. 160 (discussing that Aon is a company providing services to help organizations manage the uncertainties of international business and trade).