

A LESSON IN INSTITUTIONAL ACTIVISM: THE TEXACO DISCRIMINATION LAWSUIT

By Steven B. Singer

Leo Durocher, the famously pugnacious baseball manager, was once asked by a sportswriter why he remained so combative throughout his entire career. Leo peered up at the scribe who had dared to ask him such a question and sneered in response, “because nice guys finish last.” In the world of sports, this behavior is accepted because it is supposedly what you need to do to compete and win. But does Leo Durocher’s famous axiom ring true in other fields and endeavors as well? When it comes to matters of corporate governance, the answer is a resounding “no.” In fact, when companies do the “right thing,” the evidence demonstrates that *everyone* -- management, employees and shareholders -- ultimately benefits.

A prime example is the class action race discrimination litigation that was brought against Texaco Inc. by its African-American employees in 1994. In that lawsuit, six African-Americans who worked at Texaco facilities across the country came forward to challenge what they claimed were racially discriminatory employment practices and policies utilized by Texaco. The gravamen of plaintiffs’ allegations was that Texaco discriminated against African-Americans in terms of promotion and compensation. Simply stated, African-Americans were not promoted at the same rate as similarly qualified Caucasian employees, and African-Americans were not paid the same as their Caucasian counterparts for similar work and responsibilities.

For nearly three full years, the litigation was hotly contested. Texaco denied each and every allegation made by the plaintiffs. Thirty additional Texaco employees -- African-American and Caucasian -- came forward to attest to discrimination they had either experienced or

witnessed while at Texaco. Texaco still denied that there was any problem with its employment practices. After more than one year of intense and hard-fought discovery, plaintiffs moved for class certification. Judge Charles L. Brieant, the Federal judge overseeing the litigation, asked the U.S. Equal Employment Opportunity Commission to conduct an investigation into plaintiffs' class-wide charges of discrimination. Once again, Texaco took the position, now before the EEOC, that African-Americans were not subject to any discrimination. As plaintiffs had, the EEOC determined that Texaco's performance appraisal process -- the system which it used to evaluate all of its employees nationwide -- had a "disparate impact" on African-Americans who, as a group, did not receive the high ratings that Caucasian employees did. The EEOC determined that there was "reasonable cause" to believe that Texaco had discriminated against African-Americans "on a class-wide basis," and issued plaintiffs a "right to sue" notice in connection with their class-wide allegations. Nevertheless, Texaco still refused to acknowledge that plaintiffs' case had any merit, instead arguing that the EEOC had considered the wrong evidence and was simply incorrect.

Plaintiffs, meanwhile, had obtained further compelling evidence that supported their claims -- audiotapes made by a former Texaco employee on which senior Texaco officers could be heard making disparaging remarks about Texaco's African-American employees and discussing the withholding and destruction of documents which plaintiffs had requested and sought during discovery. When the "Texaco Tapes" surfaced in early November 1996, a national furor erupted immediately. The litigation, which had languished in relative obscurity for the previous three years, suddenly became the biggest story in the country. The Texaco case became a national referendum on employment discrimination. The tapes were played before a national audience on

“NightLine.” The United States Attorney commenced a criminal investigation and eventually indicted certain Texaco employees on charges of obstruction of justice. Civil rights organizations called for a nationwide boycott of Texaco gasoline.

Significantly, the reports about the tapes and the litigation had a dramatic impact on the price of Texaco stock. Within two days after the story broke, Texaco stock had dropped more than \$5 per share -- a loss which, as numerous financial publications noted, wiped out more than \$1 billion in market value. With institutional investors owning a significant percentage of Texaco stock, the financial and social implications of the tapes galvanized a number of the country’s largest institutional investors. At the forefront was H. Carl McCall, the New York State Comptroller and trustee of the New York State Common Retirement Fund, which at the time owned more than 1.2 million shares of Texaco common stock, with an estimated value of \$114 million. Shortly after the story broke, Mr. McCall wrote a letter to Peter I. Bijur, Texaco’s new Chairman and Chief Executive Officer, stating that he was “profoundly dismayed” by the reports and correctly noting that the attitudes evinced by these employees were not only “grossly offensive,” but had “put shareholders at risk.” Mr. McCall called on Mr. Bijur to condemn the remarks and “take steps to strengthen Texaco’s commitment to tolerance and inclusion in the workplace.”

Other institutional investors quickly followed suit. New York City Comptroller Alan Hevesi also called upon Texaco to address the situation. State lawmakers in Texas introduced legislation requiring public employee retirement funds to sell their \$250 million in Texaco holdings. The City of Philadelphia’s public pension funds actually did vote to divest. Numerous other large pension funds and institutions -- both public and private -- called upon Texaco’s

Board of Directors to take action.

Within weeks of the initial disclosures about the tapes, Texaco agreed to settle the litigation for \$176 million -- the largest settlement of a race discrimination case in history. Equally important, the settlement resulted in the creation of an unprecedented "Equality and Fairness Task Force," an independent body comprised of civic, business and civil rights leaders, which was charged with evaluating and improving Texaco's employment systems and practices, and ensuring that Texaco became a bastion for equal opportunity.

Contrary to what old Leo Durocher preached, the actions that Texaco was forced to take after the tapes surfaced has benefited everyone, including the Company and its shareholders. Within days after the settlement was announced, Texaco stock rebounded to close higher than the price it had been trading at immediately prior to the tapes. Texaco has since implemented a company-wide mentoring program for its employees, revised its performance appraisal process, created an ombudsman program designed to address employee grievances, and made managers' bonuses dependent upon their EEO and diversity compliance efforts. The end result of these dramatic efforts: in 1997, 25% of promotions were earned by minorities, nearly 39% of all new hires were minorities, and Texaco spent more than \$400 million with minority- and women-owned business enterprises. In December 1998, Texaco named Deval L. Patrick, an African-American appointed by the Court to serve as the Chair of the Task Force and the former chief of the Civil Rights Division of the Department of Justice under President Clinton, to be its General Counsel.

Obviously, the changes at Texaco occurred in large part because institutions and other large investors -- those with the greatest stake and largest financial interest in the company -- spoke up and urged Texaco to do the "right thing." Indeed, Texaco is a lesson in what

shareholder activism can help to accomplish, and how that activism can translate into results that benefit everyone. In fact, one can argue that when difficulties arise at a company, it is incumbent upon institutions to ensure that the problems are addressed and that solutions are found -- either through shareholder resolutions, putting pressure on directors and management, or through litigation. The Texaco case certainly proved that to be true.

As for Leo Durocher, well, in 24 years of managing four different teams, he won exactly one World Series.

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