

MATERIALITY:
A BEDROCK PRINCIPLE PROTECTING
LEGITIMATE SHAREHOLDER INTERESTS
AGAINST DISGUISED POLITICAL AGENDAS

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INTRODUCTION

The Committee on the Disclosure of Political Spending recently submitted a petition (“the Petition”) to the U.S. Securities Exchange Commission (“SEC” or “the Commission”) urging the Commission to require SEC-registered companies to disclose their contributions and expenditures for political activities.¹ In support of the Petition, Professors Lucian Bebchuk and Robert Jackson (who are members of the committee that submitted the Petition) have recently published an article in the *Georgetown Law Journal* enti-

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¹ Letter from Comm. on Disclosure of Corp. Political Spending to Elizabeth M. Murphy, Sec’y, U.S. Sec. & Exch. Comm’n (Aug. 3, 2011), available at <http://www.sec.gov/rules/petitions/2011/petn4-637.pdf>. [hereinafter “Committee Petition”].

tled “Shining Light on Corporate Political Spending,”² in which they argue for not only the requirement that SEC-registered companies disclose election-related contributions and expenditures, but also for increased disclosure of activities related to government relations and public affairs.³ Bebchuk and Jackson present several arguments and respond to a range of objections to their Petition. Unfortunately, these arguments play into the hands of special-interest activists who are pursuing ends that are unrelated to the economic success of SEC-registered companies and the wellbeing of their shareholders.

While truly deserving of a lengthy rebuttal, for the purposes of this article, I shall limit my response to three major arguments. In Part I, I explain that the SEC does not have the authority to require disclosure of information on these sorts of expenditures because such information is immaterial. Part II explains why, should the Commission decide to proceed with Bebchuk and Jackson’s recommendation, which would harm rather than protect investors, the Commission would be unable to satisfy its legally mandated cost-benefit analysis because the alleged benefits are outweighed by the significant costs of mandated disclosure. Part III discusses why it would be inappropriate for the Commission to move forward with a rulemaking related to corporate public policy spending at a time when it must address myriad issues related to the financial crisis of 2008, as well as those that are central to the economically important capital-raising functions of the capital markets.

I. THE COMMISSION CANNOT REQUIRE COMPANIES TO DISCLOSE INFORMATION REGARDING PUBLIC POLICY EXPENDITURES BECAUSE SUCH EXPENDITURES ARE IN ALMOST EVERY CONCEIVABLE CASE IMMATERIAL AND IF NOT IMMATERIAL, CURRENT RULES ALREADY REQUIRE DISCLOSURE.

United States securities laws, and in particular the Securities Act of 1933, are based mostly on the principle of disclosure. This was a conscious choice of the drafters of the statutes.⁴ The SEC’s mission is to maintain fair, orderly, and efficient markets, facilitate capital formation, and to protect investors by ensuring that market participants have accurate material⁵ informa-

² Lucian A. Bebchuk & Robert J. Jackson, Jr., *Shining Light on Corporate Political Spending*, 101 GEO. L.J. 923 (2013).

³ *See id.*

⁴ *See* Troy Paredes, Comm’r, U.S. Sec. & Exch. Comm’n, Remarks at SEC Speaks in 2013 (Feb. 22, 2013), available at http://www.sec.gov/news/speech/2013/spch022213tap.htm#P22_2267.

⁵ The requirement of materiality is derived from SEC Rule 10b-5, which was promulgated pursuant to the SEC’s authority under section 10(b) of the Securities Exchange Act of 1934. Section 10(b) makes it unlawful, in connection with the purchase or sale of any security, to use or employ “any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.” 15 U.S.C. § 78j(b) (2006). Rule 10b-5 provides that, in connection with the purchase or sale of any security, it shall be unlawful “[t]o make

tion about SEC-registered securities.⁶ As the SEC stated in 1975, “[i]n administering the disclosure process under the Securities Act and the Securities Exchange Act, the Commission has generally resolved these various competing considerations by requiring disclosure only of such information as the Commission believes is important to the reasonable investor—*material information*.”⁷ The Commission further explained that the requirement that information be material is “necessary in order to insure meaningful and useful disclosure documents of benefit to most investors without unreasonable costs to registrants and their shareholders.”⁸

The courts have since expounded on what information is “material” such that disclosure is appropriate. In *TSC Industries v. Northway*, the Supreme Court set forth an objective standard of materiality that generally applies to corporate disclosure.⁹ The Court found that, for the purposes of securities fraud, an omitted fact is material only if there is “a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote.”¹⁰ Moreover,

What the standard does contemplate is a showing of a substantial likelihood that, under all the circumstances, the omitted fact would have assumed actual significance in the deliberations of the reasonable shareholder. Put another way, there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the “total mix” of information made available.¹¹

Fundamentally, it is not enough that some investors may view a fact as important; rather, it must be important to the *reasonable* investor. Not a special-interest shareholder, a shareholder with an axe to grind, a shareholder with a particular religious or political bent, or a shareholder who thinks that it would be “nice to know” some relatively insignificant fact, but

any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made . . . not misleading.” 17 C.F.R. § 240.10b-5 (2011).

⁶ See 15 U.S.C. § 78c(f) (2006) (setting forth the SEC’s mission statement as articulated by Congress). See also *The Investor’s Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation*, U.S. SEC. & EXCH. COMM’N, <http://www.sec.gov/about/whatwedo.shtml> (last updated Mar. 8, 2013) (“By far the best way for investors to protect the money they put into the securities markets is to do research and ask questions. The laws and rules that govern the securities industry in the United States derive from a simple and straightforward concept: all investors, whether large institutions or private individuals, should have access to certain basic facts about an investment prior to buying it, and so long as they hold it.”).

⁷ 40 Fed. Reg. 51,656 (Oct. 16, 1975).

⁸ *Id.*

⁹ 426 U.S. 438, 449 (1976).

¹⁰ *Id.*

¹¹ *Id.* Significantly, the Court in *TSC Industries* explicitly rejected the broader materiality formulation of the Seventh Circuit in the case on appeal: “material facts include ‘all facts which a reasonable shareholder might consider important.’” *Id.* (internal citation omitted).

a reasonable shareholder focusing on the total mix of information informing his investment decisionmaking.

The Supreme Court clearly understood the problem of disclosure overload. In the unanimous opinion written by Justice Thurgood Marshall, the Court observed that “[s]ome information is of such dubious significance that insistence on its disclosure may accomplish more harm than good.”¹² The potential liability for a fraud violation can be great and, as Justice Marshall explained, “[i]f the standard of materiality is unnecessarily low, not only may the corporation and its management be subjected to liability for insignificant omissions or misstatements, but also management’s fear of exposing itself to substantial liability may cause it simply to bury the shareholders in an avalanche of trivial information—a result that is hardly conducive to informed decisionmaking.”¹³

The Supreme Court continued the application of the objective materiality test established in *TSC Industries* multiple times, including in 1988 in *Basic Inc. v. Levinson*¹⁴ and again in 2011 in *Matrixx Initiatives, Inc. v. Siracusano*.¹⁵ Thus, in order for the Commission to remain consistent with Supreme Court precedent, the Commission may require the disclosure of corporate expenditures only if it finds that a “reasonable shareholder would consider it important in deciding how to vote” and that such disclosure would alter the “total mix of information made available” to the shareholder. As discussed below, in almost every conceivable case, these expenditures are immaterial and would not be important to a reasonable shareholder.

First, no amount of creative reasoning on the part of the Petition’s proponents can change the fact that the amount of undisclosed public policy expenditures by public companies is simply immaterial. One need look no further than the disclosure proponents’ own writings to understand this simple fact. For example, in “Shining Light on Corporate Political Spending,” Professors Bebchuk and Jackson attempt “to illustrate the potential magnitude of the corporate political spending that occurs through intermediaries” by pointing to the fact that the most active “intermediaries,” or as most people appropriately call them, “trade associations,” spent \$1.5 billion on lobbying and politics from 2005 through 2010, with \$814 million spent in 2009 and 2010 alone.¹⁶ Bebchuk and Jackson conclude that this evidence suggests there is a material amount of undisclosed political expenditures by public companies because “not only do intermediaries spend large sums on politics, but . . . these amounts have been increasing in recent years.”¹⁷

¹² *Id.*

¹³ *Id.*

¹⁴ 485 U.S. 224 (1988).

¹⁵ 131 S. Ct. 1309 (2011).

¹⁶ Bebchuk & Jackson, *supra* note 2, at 931.

¹⁷ *Id.*

A detailed analysis of such spending supports the opposite conclusion. Figures released by the Center for Responsive Politics¹⁸ show that approximately \$383 million was spent by groups that did not disclose their donors in 2012, which is 25% less than was spent by those groups in 2010.¹⁹ Professors Bebchuk and Jackson presume, based on “anecdotal evidence,” that public companies donate substantial amounts to intermediaries.²⁰ They, however, also acknowledge that “there is no systematic evidence that the intermediaries’ funding comes directly from public companies.”²¹ In fact, the \$383 million at issue includes contributions from numerous groups that would be unaffected by the proposed rulemaking, including individuals, labor unions, and private companies. Moreover, even if for argument’s sake one assumes that the entire \$383 million came exclusively from public companies, this amount is only 0.0026% of the revenue of U.S. public companies in 2012.²² Thus, while we may not know the precise amount of public company expenditures to intermediaries, we know enough to know that such expenditures in the aggregate are immaterial when compared to the revenue of public companies in the aggregate. Furthermore, on an individual company basis, if such expenditures were material to a company, then current SEC regulations already provide for disclosure by that company.²³

Alternatively, Bebchuk and Jackson argue that “even assuming that the amounts spent on political spending do not significantly affect financial results, a finding that political spending is financially significant is not a necessary condition to SEC rules mandating disclosure of that spending.”²⁴ They argue that regardless of the effect on financial results, this information is material because of significant investor interest in the information.²⁵

¹⁸ The Center for Responsive Politics is a not-for-profit research group, the stated goal of which is to track the effects of money and lobbying on elections and public policy. See *Our Mission: Inform, Empower & Advocate*, CTR. FOR RESPONSIVE POL., <http://www.opensecrets.org/about/index.php> (last visited May 20, 2013).

¹⁹ *Current Issues in Campaign Finance Law Enforcement: Hearing Before the Senate Judiciary Committee Subcommittee on Crime and Terrorism*, 113th Cong. (statement of Bradley A. Smith, Chairman, Ctr. for Responsive Politics) (final Senate transcript unavailable), available at <http://www.judiciary.senate.gov/pdf/4-09-13SmithTestimony.pdf>.

²⁰ Bebchuk & Jackson, *supra* note 2, at 932.

²¹ *Id.* at 932.

²² See *US national debt is more than all public revenue*, QUANT ADVISOR (Jan. 27, 2013), available at <http://quantadvisor.com/fun-fact-us-national-debt-is-164-trillion-19t-more-than-the-total-gross-revenue-of-a>.

²³ See generally 17 C.F.R. § 210.5-03 (2001) (provides for disclosure of public company costs and expenses on income statements, including operating costs and expenses; selling, general, and administrative expenses; and other general expenses not included elsewhere). The provision requires that filers “[s]tate separately any material amounts” not included under operating costs as well as “any material item” not included under other captions required by the rule. *Id.*

²⁴ Bebchuk & Jackson, *supra* note 2, at 956.

²⁵ Professor Jackson has asserted that the SEC has “plenary” authority to require such disclosure, regardless of its materiality. See *PBS NewsHour: SEC Considering New Rule for Political Contributions by Public Companies* (PBS television broadcast May 6, 2013), available at http://www.pbs.org/newshour/bb/politics/jan-june13/sec_05-06.html. This assertion does not comport with the letter and spirit of the securities laws and the law as articulated by the

Although materiality, the predicate for disclosure, is not determined by shareholder interest, the vast majority of shareholders in fact have not demonstrated an interest in this information—contrary to petitioners’ assertions. The primary argument that Bebchuk and Jackson make to demonstrate shareholder interest is that there were more shareholder proposals on this topic than any other topic in 2012. While this is true, the high number of proposals does not demonstrate broad shareholder interest but rather significant interest from a minority of special-interest shareholders. In fact, more than 75% of the corporate public policy spending proposals in 2012 were proposed by a coalition of special-interest investors coordinated by the Center for Political Accountability, Walden Asset Management, and the American Federation of State, County and Municipal Employees.²⁶ More importantly, the greatest indicator of shareholder interest is the actual shareholder vote. In fact, shareholders have not “increasingly expressed strong interest in receiving information on political spending from companies they own.”²⁷ The 2012 proxy season shows that, among Fortune 200 companies, 83% of shareholder votes—up from 78% in 2011—refused to support ac-

Supreme Court, beginning with its decision in *TSC Industries*, and as implemented by the SEC. See, e.g., Mary L. Schapiro, Chairman, U.S. Sec. & Exch. Comm’n, Statement Before the Open Commission Meeting on Disclosure Related to Business or Legislative Events on the Issue of Climate Change (Jan. 27, 2010) (“These principles of materiality form the bedrock of our disclosure framework.”), available at <http://www.sec.gov/news/speech/2010/spch012710mls-climate.htm>. As precedent for an SEC-mandated expenditure rule, many proponents cite the SEC’s 1992 rule and subsequent 2006 revisions regarding disclosure of executive compensation. See Executive Compensation Disclosure, 57 Fed. Reg. 48,126 (Oct. 16, 1992); Executive Compensation and Related Person Disclosure, 71 Fed. Reg. 53,158 (Sept. 8, 2006). I participated in both of these rulemakings, as a member of the staff of Chairman Richard C. Breeden in 1992 and as a commissioner in 2006. Executive compensation disclosure rules are rooted in principles regarding the election of directors (who are representatives of shareholders). The executive compensation rules adopted in 1992 resulted from a compromise with business groups and, thus, the underlying materiality arguments have never been tested in court. While compensation of its highest-ranked individuals is usually not material to a company, the principle of disclosure in this regard is related to the ability of shareholders to judge the personal performance of management and directors. Thus, the formulation in Item 401(f) of Regulation S-K regarding legal proceedings against directors: “Describe any of the following events that occurred during the past ten years and that are material to an evaluation of the ability or integrity of any director, person nominated to become a director or executive officer of the registrant.” 17 C.F.R. § 229.401(f) (2012). Although some advocates of an SEC-mandated expenditure rule posit the same basis for their proposed rule (i.e., judging the personal performance of management and directors because of a suspicion of advancing personal political preferences), it lacks the direct material personal relationship of the compensation rules. Indeed, if these business-related expenditures are part of some suspect class of expenditures, almost any expenditure of a company could be said to involve potential self-interest by management or directors (including, for example, decisions regarding location of facilities, agreements with contractors, and purchase of office artwork). The exceptions to the concept of materiality would swallow the principle, especially considering the underlying political motivations of many advocates of the proposed rule. See Part II, *infra*.

²⁶ See HEIDI WELSH & MICHAEL PASSOFF, PROXY PREVIEW 2013 37–50 (2013), available at <http://asyousow.org/publications/2013/ProxyPreview-2013.pdf>.

²⁷ Bebchuk & Jackson, *supra* note 2, at 937.

tivist proposals regarding mandatory disclosure of the amount spent on public policy or lobbying activities.²⁸

Bebchuk and Jackson also point to the views of “large institutional investors,”²⁹ citing two California state pension funds and TIAA-CREF.³⁰ In fact, TIAA-CREF voted against nearly 80% of these proposals in 2012,³¹ and other large institutional investors actually demonstrate widespread opposition to these proposals. In 2012, “the seven largest mutual fund families—Vanguard, BlackRock, State Street, Fidelity, Capital World Investors, Capital Research Global Investors, and T. Rowe Price—supported only 3.6% of proposals calling for increased disclosure of corporate political spending.”³² Moreover, “the three largest mutual fund families in the United States failed to support a single political spending disclosure resolution.”³³

Bebchuk and Jackson further advance the argument that “a significant number of major public companies are voluntarily providing shareholders with information on their political spending . . . [which] is another manifestation of strong investor interest in political spending.”³⁴ Voluntary disclosure does not demonstrate investor interest, but more importantly, the vast majority of companies do not voluntarily disclose information other than that which is required by state and federal laws. In fact, “CPA’s own 2012 analysis . . . shows that fewer than 15 of [the] 196 companies [listed in the CPA-Zicklin Index] are disclosing political expenditures that are not already required to be disclosed by the applicable political contribution laws.”³⁵ Because the amount of the expenditures at issue is not material and, contrary to the petitioners’ claims, the vast majority of “reasonable shareholders” have demonstrated through their votes³⁶ that they do not consider the information

²⁸ See JAMES R. COPLAND, YEVGENIY FEYMAN & MARGARET O’KEEFE, PROXY MONITOR 2012: A REPORT ON CORPORATE GOVERNANCE AND SHAREHOLDER ACTIVISM 2 (2012), available at http://www.proxymonitor.org/pdf/pmr_04.pdf (stating that “only 17 percent of shareholders, on average, supported these proposals in 2012, down from 22 percent in 2011 and lower than any other year in the 2006–12 period”), (Manhattan Inst. for Pol’y Research, Fall 2012).

²⁹ Bebchuk & Jackson, *supra* note 2, at 940–41.

³⁰ “[T]he CalPERS board started using its newfound power to enforce its own political agenda, often without meeting its fiduciary responsibility to invest the fund’s money wisely.” Stephen Malanga, *The Pension Fund That Ate California*, CITY J. (Winter 2013), http://www.city-journal.org/2013/23_1_calpers.html (last visited May 20, 2013).

³¹ See TIAA-CREF, Annual Report of Proxy Voting Record of Registered Management Investment Company (June 30, 2012), available at <http://www.sec.gov/edgar/searchedgar/npx.htm>.

³² James R. Copland, *Public Citizen and social investors peddling falsehoods*, POINTOFLAW.COM (Feb. 7, 2013), <http://www.pointoflaw.com/archives/2013/02/public-citizen-and-social-investors-peddling-falsehoods.php>.

³³ See JACKIE COOK, CTR. FOR POLITICAL ACCOUNTABILITY, CORPORATE POLITICAL SPENDING AND THE MUTUAL FUND VOTE 6 (2012), available at <http://politicalaccountability.net/index.php?ht=A/GetDocumentAction/i/7380>.

³⁴ Bebchuk & Jackson, *supra* note 2, at 946.

³⁵ See Letter from 60 Plus Ass’n et al., to Elizabeth M. Murphy, Sec’y, U.S. Sec. & Exch. Comm’n 18 (Jan. 4, 2013), available at <http://www.sec.gov/comments/4-637/4637-1198.pdf>.

³⁶ The shareholder proposals regarding disclosure of corporate spending are merely precautionary. For precautionary proposals, most institutional investors do not deem it worthwhile to spend a

important to the total mix of information available to shareholders, the Commission cannot require the disclosure of this information.

II. THE COMMISSION CANNOT MOVE FORWARD WITH A RULEMAKING
BECAUSE THE COSTS OF THE RULEMAKING WOULD EXCEED
THE BENEFITS.

The Administrative Procedure Act requires that an agency action be invalidated when it is “arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.”³⁷ To determine whether a promulgated rule satisfies this standard, the Commission must demonstrate that it has “examine[d] the relevant data and articulate[d] a satisfactory explanation for its action including a rational connection between the facts found and the choices made.”³⁸ Moreover, courts have invalidated SEC action when the Commission has failed to meet its “statutory obligation to determine as best it can the economic implications of the rule.”³⁹ Here, the Commission cannot satisfy this standard, as the real damage to corporations and shareholders resulting from a promulgated rule outweighs the purported benefits put forward by proponents of the rulemaking.

Professors Bebchuk and Jackson argue that an SEC rule mandating disclosure of political contributions would benefit investors by providing them with information “necessary to help ensure that directors and executives make decisions in this area that are consistent with investors’ interests.”⁴⁰ Professors Bebchuk and Jackson, however, fail to establish how corporate public policy expenditures are in any way unique from other ordinary business expenditures that management and directors routinely oversee, and even if there were some undefined benefit from disclosure, that benefit is dwarfed by the harm that will result to companies and shareholders.

It is well documented that the intent of many of those calling for disclosure is not to enhance shareholder value, but rather to prevent companies from engaging in speech that is opposed to the groups seeking disclosure.⁴¹

great deal of effort or money to build a staff that analyses how the advisor will vote on these sorts of proposals, because they do not view the effort as enhancing investment performance. See also David F. Larcker, Allan L. McCall & Gaizka Ormazabal, *Proxy Advisory Firms and Stock Option Exchanges: The Case of Institutional Shareholder Services 1* (Stanford Graduate Sch. of Business, 2011), available at <https://gsbapps.stanford.edu/researchpapers/library/RP2077&100.pdf> (noting that “many institutional investors subscribe to third party proxy advisory firms such as Institutional Shareholder Services (ISS) and Glass Lewis to complete the mechanics of share voting and in many cases determine whether they should vote for or against a management or shareholder proposal presented in the proxy statement Since proxy advisory firms can sway substantial numbers of shareholder votes, they have the ability to influence corporate governance choices.”).

³⁷ 5 U.S.C. § 706(2)(A).

³⁸ *Business Roundtable v. SEC*, 647 F.3d 1144, 1148 (D.C. Cir. 2011).

³⁹ *Id.*

⁴⁰ See Bebchuk & Jackson, *supra* note 2, at 965.

⁴¹ For example, Charles Schwab Corporation became a target of labor unions for the personal support of Social Security reform by the company’s founder, Charles Schwab. Deneen

Those most often seeking to impose disclosure requirements, particularly union and state pension funds and social investment funds, regularly take policy positions directly opposed to those of most public companies. By forcing disclosure, activists can then browbeat corporate opponents, through public intimidation and private threats, thereby discouraging companies from participating in important public policy issues, even through trade associations. Such tactics are often directed at company boards and corporate management, especially those in retail-related lines of business which seek to avoid controversy, even if the controversy is not broad-based but generated by a relatively small, loud minority that is inconsistent with the views of the majority of the company's shareholders.

For example, Media Matters for America (which bills itself as a "progressive research and information center") has embraced a plan to "aggressively attack" and "create a multitude of public-relations challenges for corporations that make the decision to meddle in political campaigns."⁴² The group seeks to accomplish this by portraying disclosed spending as a corporate endorsement of "everything that a politician has said or done."⁴³ Thus, if a company supports a candidate that "once voted against an appropriations bill containing funding for special education programs," Media Matters will work with its "partners" to attack the company "for supporting policies to cease funding education programs for children with special needs."⁴⁴ Media Matters believes that such a strategy will make it "easy to frame their corporate backers as out of touch with their customers" and "provide backlashes among companies' shareholders, employees, and customers and the public at large."⁴⁵

In the case of Target Corporation's 2010 contribution to Minnesota Forward, activists used such information as part of a broader campaign to silence a nonprofit opponent with which they disagreed. Minnesota Forward, based in the state in which Target is headquartered, is a political action group funded by local corporations to promote economic issues. Target's support of Minnesota Forward was intended to support a "business climate conducive to growth" that Target believed critical to its future and to increasing share-

Moore, *Union Activists' Strong-Arm Tactics*, NAT'L CTR. FOR PUB. POL'Y RESEARCH, <http://www.nationalcenter.org/P21NVMooreInfluence90906.html> (last visited May 20, 2013). Labor unions attacked the corporation for its membership in trade associations supporting this effort, including Alliance for Worker Retirement Security. *Id.* "Although the company wanted to enhance shareholder value through this advocacy, its participation in the public policy debate and exercise of political freedoms seemed too much of a threat to union activists. To teach Schwab and his company a lesson, union activists masquerading as shareholders disrupted the company's 2005 shareholder meeting. Activists also staffed protests outside of local Schwab branches nationwide to intimidate customers and otherwise disrupt business." *Id.*

⁴² See MEDIA MATTERS, MEDIA MATTERS 2012: A THREE-YEAR CAMPAIGN 82 (2009), available at <http://dailycaller.com/wp-content/uploads/2012/02/MMFA-2012-full.pdf>; see also Editorial, *The Corporate Disclosure Assault*, WALL ST. J., Mar. 19, 2012, at A16; Bradley A. Smith, *Another Union Attack on Corporate Speech*, WALL ST. J., Nov. 10, 2011, at A21.

⁴³ MEDIA MATTERS, *supra* note 42, at 83.

⁴⁴ *Id.*

⁴⁵ *Id.*

holder value in the company.⁴⁶ In 2010, Minnesota Forward ran ads supporting gubernatorial candidate Tom Emmer, a Republican supporting a lower state corporate tax rate. However, Mr. Emmer's stance on same-sex marriage drew criticism from an advocacy organization for homosexuals that supported Mr. Emmer's opponent.

Portraying Target's support of Minnesota Forward as an endorsement of all of Mr. Emmer's political positions, the group criticized Target for its donation and worked with MoveOn.org and others to organize a boycott of the company. For example, Mike Dean, the director of Minnesota Common Cause,⁴⁷ a self-described "nonpartisan citizen's lobbying organization," but in fact a politically left-oriented group, attended Target's 2011 shareholder meeting on behalf of the Tides Foundation.⁴⁸ Mr. Dean's stated purpose was to address Target's board of directors and "make the case that political spending is not good for business – you're going to offend your customer base no matter who [sic] you give to."⁴⁹

Several politicians also rallied behind the campaign against Target. While not present at Target's annual meeting, Bill de Blasio, New York City Public Advocate and board member of the New York City Employees Retirement System (NYCERS), publicly asked NYCERS to vote its one million shares of stock⁵⁰ against any Target director who refused to stop the company's political expenditures.⁵¹ Moreover, Mr. de Blasio, who is cur-

⁴⁶ See Jia Lynn Yang & Dan Eggen, *Campaign spending puts Target in bull's-eye*, WASH. POST, Aug. 19, 2010, at A1.

⁴⁷ Common Cause has coordinated the filing of comment letters supportive of the SEC rulemaking petition. The organization has publicized several form letters, which can be submitted to the SEC from its website. See *Help Us Send A LOUD Message to the SEC*, COMMON CAUSE, <http://www.commoncause.org/siteapps/advocacy/ActionItem.aspx?c=DKLNK1MQIwG&b=8503321> (last visited June 1, 2013); see also Jack Mumby, *Tell the SEC: We need transparency!*, COMMON CAUSE (July 18, 2012), <http://www.commonblog.com/2012/07/18/tell-the-sec-we-need-transparency/>.

⁴⁸ The Tides Foundation ("Tides") is a not-for-profit organization that has donated more than \$300 million towards left-leaning causes. Cf. TIDES FOUND., *GLOBAL CHANGE 6*, available at http://www.sourcewatch.org/index.php?title=Tides_Foundation (last visited May 20, 2013). Tides has joined several unions and activist efforts to press companies for their corporate public policy spending, particularly trade association expenditures. See Press Release, Walden Asset Management, *Institutional Investors Continue to Press Companies For Disclosure of Lobbying 1* (Feb. 1, 2013), available at http://www.waldenassetmgmt.com/social/action/Lobbying_PR_212013.pdf; see also Press Release, Walden Asset Mgmt., *Investors Call on Companies Sitting On The U.S. Chamber of Commerce Board to Evaluate Their Role 1* (Jan. 31, 2011), available at http://www.waldenassetmgmt.com/social/action/Chamber_Commerce_Jan2011.pdf; Press Release, Walden Asset Mgmt., *Investors Announce Challenges on Political Spending to Corporate Responsibility Leaders 1* (Nov. 4, 2010), available at http://www.waldenassetmgmt.com/social/action/Pol_Spending_PR.pdf.

⁴⁹ Jim Spencer, *Target urged to change tune on political giving*, STARTRIBUNE (June 7, 2011), <http://www.startribune.com/printarticle/?id=123425179>.

⁵⁰ The one million shares owned by NYCERS accounted for only 0.14% of Target's 693,063,352 shares of outstanding common stock. See Target Corporation, Form 10-K (Mar. 20, 2013).

⁵¹ Change to Win (CtW), a coalition of four member unions (The International Brotherhood of Teamsters; Service Employees International Union; United Farm Workers; and United Food and Commercial Workers), spearheaded similar efforts to intimidate corporate board

rently campaigning to become the next mayor of New York City, threatened that “what happened to Target was child’s play” compared to the boycotts, shareholder action, and litigation efforts he and his allies would bring against other corporations.⁵²

What happened to Target is only one example of an orchestrated campaign being waged against corporate free speech. “The larger political goal is also to stigmatize and shut down funding sources for any business group that seeks to influence policy debates.”⁵³ Unions and social investment funds also seek the disclosure of payments being made to trade associations, particularly those disagreeing with the policy positions of labor unions.

For example, the American Legislative Exchange Council (ALEC) is a partnership of state legislators, entrepreneurs, and civil society organizations that drafts model legislation for state legislatures on issues such as reducing corporate regulation and taxation.⁵⁴ However, ALEC’s support of voter-ID laws and “stand your ground” legislation sparked a campaign to portray ALEC as racist and unworthy of business support.⁵⁵ In 2012, Color of Change, a not-for-profit corporation founded by former White House aide Van Jones, wrote to its members to demand that Coca-Cola stop supporting ALEC, citing ALEC’s “effort to disenfranchise African Americans, Latinos, students, the elderly, the disabled and the poor.”⁵⁶ The letter also criticized

members from participating in the public policy debate. *See About Us, CHANGE TO WIN*, <http://www.changetowin.org/about> (last visited May 20, 2013). In May 2012, CtW launched a “vote no” campaign against the re-election of WellPoint board members Susan Bayh and Julie Hill at the company’s annual meeting, citing a refusal of the board to disclose the details of “high risk political spending.” This effort stemmed from WellPoint’s reluctance to answer questions about its donations to a America’s Health Insurance Plans (AHIP), which gave the U.S. Chamber of Commerce \$86 million in 2009 when the Chamber was actively opposing President Obama’s health-care overhaul. *See Editorial, Intimidation by Proxy*, WALL ST. J., May 9, 2012, at A12; *see also* Jim Spencer, *Target urged to change tune on political giving*, STARTRIBUNE (Jun. 7, 2011, 9:07 PM), <http://www.startribune.com/printarticle/?id=123425179>. Despite this public, concerted politicized effort, Ms. Bayh and Ms. Hill were overwhelmingly reelected. *See Push For More WellPoint Political Disclosure Falls Short*, FOX BUSINESS, <http://m.foxbusiness.com/quickPage.html?page=32811&content=72404346&pageNum=-1> (last visited May 20, 2013).

⁵² Last year, Mr. de Blasio launched a disclosure group called the Coalition for Accountability in Political Spending (CAPS), a group of unions and governmental pension funds controlled by elected officials. CAPS has spearheaded several protests at corporate shareholder meetings and coordinated the filing of form letters to the SEC supportive of the rulemaking petition. *See COALITION FOR ACCOUNTABILITY IN POLITICAL SPENDING, ROLLING IN DOUGH BUT SILENT IN SPENDING: SETTING OUR TARGETS ON THE 20 LEAST TRANSPARENT CORPORATIONS* (2012), available at http://www.politicalspending.org/corp_profiles; *see also* Bill de Blasio, *Keeping Money Out of Our Elections*, N.Y. CITY PUB. ADVOCATE, <http://pubadvocate.nyc.gov/politicalspending> (last visited May 20, 2013) (encouraging citizens to “[f]ill in your information below to send a letter to the S.E.C. calling for full disclosure of corporate political spending”).

⁵³ *See Editorial, Intimidation by Proxy*, *supra* note 51.

⁵⁴ *History*, AM. LEG. EXCH. COUNCIL, <http://www.alec.org/about-alec/history> (last visited May 20, 2013).

⁵⁵ *See Editorial, Shutting Down ALEC*, WALL ST. J., Apr. 18, 2012, at A16.

⁵⁶ Letter from Common Cause Re: Coca-Cola’s ALEC membership, to Color of Change members (Apr. 4, 2012), available at <http://www.colorofchange.org/blog/2012/apr/4/tell-coca-cola-stop-funding-alec>.

ALEC's support of legislation "to privatize education, and to break unions."⁵⁷ The concerted campaign against ALEC caused Coca-Cola, as well as 41 other companies, to terminate its ALEC membership.⁵⁸ Building on this momentum, activists are actively attempting to identify ALEC's other corporate sponsors. For example, the American Federation of State, County and Municipal Employees (AFSCME) is spearheading an investor movement to press companies for disclosure of membership and payments to "any tax-exempt group that writes and endorses model legislation."⁵⁹ This year, AFSCME coordinated the filing of shareholder proposals requesting this type of information to over 50 companies.⁶⁰

Bebchuk and Jackson suggest that placing significant obstacles to public policy activity by companies is a good thing: "To the extent that disclosure deters directors and executives from engaging in spending that is disfavored by the company's shareholders, discouraging that spending should be considered a benefit, not a cost, of the proposed disclosures."⁶¹ Moreover, if the spending at issue "enjoys the support of a majority of shareholders, a minority of special interest investors will not be able to use evidence of such spending as a means of pressuring insiders."⁶²

This rationale simply ignores the reality that corporate managers are conflict-averse and may conclude that limiting public policy advocacy to avoid "relentless, albeit unjustified, attacks"⁶³ is an easier alternative than defending the company, as well as their own personal reputations, against protests and public smear campaigns. This disclosure, together with the intimidating tactics used by its proponents, actually diminishes free speech and public debate of issues. Moreover, it fails to enhance, and may potentially depress, shareholder value.

A June 2012 study by economist (and former Clinton Administration official) Robert J. Shapiro found that "[e]xtensive analysis and evidence . . . support the view that corporate participation in the political process yields generally positive returns to firms and their shareholders" and that "[c]orporate political activity appears to have a generally positive effect on firm value, as reflected in excess market returns."⁶⁴ Moreover, *The Economist* reports that "[a]n index based on the amount of lobbying that American firms do has outperformed the broader market since its creation in

⁵⁷ *Id.*

⁵⁸ See Welsh & Passoff, *supra* note 26, at 36.

⁵⁹ *Id.* at 37.

⁶⁰ See Press Release, Walden Asset Mgmt., Institutional Investors Continue to Press Companies For Disclosure Of Lobbying (Feb. 1, 2013), available at http://www.waldenassetmgmt.com/social/action/Lobbying_PR_212013.pdf.

⁶¹ See Bebhuk & Jackson, *supra* note 2, at 958.

⁶² *Id.* at 960.

⁶³ See Letter from 60 Plus Ass'n et al., *supra* note 35, at 18.

⁶⁴ ROBERT J. SHAPIRO & DOUGLAS DOWSON, CORPORATE POLITICAL SPENDING: WHY THE NEW CRITICS ARE WRONG 17, 22 (2012), available at http://www.manhattan-institute.org/html/lpr_15.htm.

2008.”⁶⁵ In fact, the index of 50 firms has “outperformed the S&P 500 by 11% a year since 2002.”⁶⁶

Most companies and investors correctly understand that government regulations can have a tremendous effect on their bottom line, and indeed, the companies’ very existence. Further,

the regulatory environment in which corporations must compete is complex, costly and burdensome. Armed with the right to speak, and to possibly influence the political environment from which regulations flow, corporations have a responsibility to consider political speech as a legitimate means to advance their economic goals.⁶⁷

“Economic goals” means building shareholder value. A reduction in or elimination of public policy activities defies this objective, as it creates “substantial risk that insufficiently informed public policy makers will be led to enact laws and otherwise adopt policies that would unjustifiably inflict financial injury upon corporations and, as a result, their shareholders.”⁶⁸ Thus, it is unsurprising that businesses seek to involve themselves in the policymaking process, both directly and through participation in membership organizations. Moreover, attempts to place significant obstacles to companies’ public policy activity, pushed largely by unions, environmentally focused investment funds, and public pensions, would outweigh the alleged benefits put forth by proponents of the petition. In fact, the data dump sought by petitioners “serves no one save the political activists who can use it as a [public relations] club to harass companies until they stop donating.”⁶⁹

The disclosure of expenditures related to public policy advocacy enables narrow shareholder and non-shareholder interests to intimidate value-creating corporate behavior and stifle corporate speech, and therefore a rulemaking would have detrimental effects on shareholders. The SEC cannot rationally find that the benefits of such a rule (*e.g.*, the need to satisfy the political agenda of a small, but extremely vocal, minority of shareholders) outweigh the detrimental effects caused by facilitating the ability of political activists to inflict brand damage to public companies and deter corporate participation in the public policy arena. As we saw in *Business Roundtable v. SEC*,⁷⁰ challenges to SEC actions on cost-benefit grounds can be successful, and a rulemaking could mire the Commission in yet more burdensome and unnecessary litigation.

⁶⁵ See Editorial, *Money and Politics – ask what your country can do for you*, ECONOMIST (Oct. 1, 2011), <http://www.economist.com/node/21531014>.

⁶⁶ *Id.*

⁶⁷ Roger Coffin, *A Responsibility To Speak: Citizens United, Corporate Governance and Managing Risks*, 8 HASTINGS BUS. L.J., 103, 165 (2011).

⁶⁸ See Letter from 60 Plus Ass’n et al., *supra* note 35, at 5.

⁶⁹ Editorial, *The Corporate Disclosure Assault*, *supra* note 42.

⁷⁰ 647 F.3d 1144 (D.C. Cir. 2011).

III. ABSENT AN EXPLICIT CONGRESSIONAL MANDATE, THE COMMISSION SHOULD NOT CONSIDER A RULEMAKING RELATED TO THE DISCLOSURE OF PUBLIC POLICY SPENDING, WHICH IS ANTITHETICAL TO THE COMMISSION'S MISSION AND UNRESPONSIVE TO WHAT SHOULD BE THE SEC'S PRIORITY: RESPONDING TO THE 2008 FINANCIAL CRISIS AND OTHER MARKET-RELATED ISSUES.

Even if the Commission could move forward with a rulemaking on this subject, which it cannot given the lack of materiality and the fact that the costs entailed by such a rulemaking would dwarf the purported benefits, such a rulemaking is clearly inappropriate given the lack of a Congressional mandate in this area.

The SEC's mission is to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation.⁷¹ While both the Jumpstart Our Business Startups Act ("JOBS Act") and the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank Act") mandate that the Commission take various regulatory actions that it has not yet completed, the Dodd-Frank Act mandates are often ill-defined, controversial, complex, and even contradictory both internally and to the SEC's mission. The SEC has taken a haphazard approach to implementation of the Dodd-Frank Act, failing to properly prioritize its rulemakings to address issues most central to the 2008 financial crisis.⁷² Indeed, the U.S. Circuit Court of Appeals for the District of Columbia severely criticized the lackluster nature of the first rule that the SEC promulgated approximately a month after enactment of Dodd-Frank and vacated it.⁷³

Nonetheless, these statutes place significant burdens on the SEC, and one need look no further than the words of current SEC officials to understand these challenges for the SEC. For example, in February 2013, then-Chairman Elisse Walter stated that the "Dodd-Frank Act has required the SEC to undertake the largest and most complex rulemaking agenda in the history of the agency."⁷⁴ Commissioner Dan Gallagher made similar comments in January 2013, stating that the Dodd-Frank Act has led to "a dramatic increase in both the volume and pace of SEC rulemaking" and that

⁷¹ 15 U.S.C. § 78c(f) (2006).

⁷² At least one commissioner has called into question the "scatter-shot" approach taken by former Chairman Schapiro in setting priorities for implementing Dodd-Frank. See Speech of Comm'r Daniel M. Gallagher (Sept. 24, 2012, available at <http://www.sec.gov/news/speech/2012/spch092112dmg.htm>).

⁷³ *Business Roundtable v. SEC*, 647 F.3d 1144 (D.C. Cir. 2011).

⁷⁴ Elisse B. Walter, Chairman, U.S. Sec. & Exch. Comm'n, *Testimony on "Wall Street Reform: Oversight of Financial Stability and Consumer and Investor Protections,"* U.S. SEC. & EXCH. COMM'N (Feb. 24, 2013), available at <http://www.sec.gov/news/testimony/2013/ts021413ebw.htm>.

“it’s no exaggeration to say that the Commission is handling ten times its normal rulemaking volume.”⁷⁵

Moreover, the Commission’s lack of leadership also has exacerbated its failure to adequately fulfill its core responsibilities. For example, the principles of the JOBS Act are central to the SEC’s mission. Nevertheless, the SEC has failed to implement the JOBS Act in a timely fashion following its enactment in April 2012. The statutory deadline for the SEC final rule implementing Title II of the JOBS Act passed unmet almost one year ago; the Commission has not even proposed a rule to implement Title III of the JOBS Act, even though the statutory deadline for a final rule was December 31, 2012; and the Commission has failed to propose a rule to implement Title IV of the JOBS Act.⁷⁶

Unlike rulemakings mandated by Congress, there is no mandate to embark on a rulemaking related to public policy spending. In fact, one could argue that the SEC has the opposite of a Congressional mandate in that, in 2011, Congress considered expanding current disclosure requirements and explicitly decided not to act.⁷⁷ It is thus not surprising that the Commission’s use of resources in the process of merely considering a rulemaking related to public policy expenditures has led to a strong rebuke from members of Congress charged with overseeing the SEC. On March 5, 2013, Jeb Hensarling, Chairman of the House Committee on Financial Services; Darrell Issa, Chairman of the House Committee on Oversight and Government Reform; Patrick McHenry, Chairman of the Financial Services Subcommittee on Oversight and Investigations; and Jim Jordan, Chairman of the Oversight Subcommittee on Economic Growth, Job Creation and Regulatory Affairs, wrote a letter to then-Chairman Walter, stating:

The Commission appears to be allocating its limited resources on a *discretionary* project wholly unrelated to its mandate to “protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation.” . . . In light of the SEC’s extraordinary delays in meeting the JOBS Act’s mandatory statutory deadline, an allocation of resources devoted to non-essential rulemaking raises serious questions. In the meantime, *mandatory* reforms critical to our economic recovery are languishing.⁷⁸

⁷⁵ Daniel M. Gallagher, Comm’r, U.S. Sec. & Exch. Comm’n, Remarks before the U.S. Chamber Center for Capital Markets Competitiveness (Jan. 16, 2013), *available at* <http://www.sec.gov/news/speech/2013/spch011613dmg.htm>.

⁷⁶ Letter from Chairmen Hensarling, Chairman, H. Comm. On Fin. Services et al., to Elisse B. Walter, Chairman, U.S. Sec. & Exch. Comm’n (Mar. 5, 2013), *available at* <http://www.mofo.com/files/Uploads/Images/130305-DEI-Hensarling-Jordan-McHenry-to-Walter-SEC.pdf>.

⁷⁷ See Shareholder Protection Act of 2011, H.R. 2517, 112th Cong. (2011).

⁷⁸ Letter from 4 Congressmen et al., to Elisse Walter, Chairman, U.S. Sec. & Exch. Comm’n 2 (Mar. 5, 2013), *available at* <http://about.bloomberglaw.com/files/2013/03/letterjobs.pdf>.

In the same letter, Congressional leaders also pointed out that “SEC staff have neither experience nor expertise regulating the disclosure of political expenditures.”⁷⁹ This lack of expertise is unsurprising given that the disclosure of political expenditures is thoroughly governed by statutes enacted by Congress and regulations implemented by the Federal Election Commission (FEC) at Congress’s explicit instruction.⁸⁰ Current campaign finance law requires that any corporation making a political expenditure report it to the FEC or, in state and local elections, to the appropriate regulators in those jurisdictions.⁸¹ “Specifically, federal law requires that a corporation file FEC Form 5 and report any independent expenditures once spending exceeds \$250 in the aggregate with respect to any given election.”⁸² Federal law also requires that political action committees (including Super PACs) receiving corporate money for independent expenditures report those receipts and their subsequent expenditures.⁸³

In fact, the Commission has long recognized Congress as the source of federal disclosure requirements. In 1972, the Commission rejected a petition requesting corporate disclosure of information concerning “the establishment, administration and solicitation of contributions to a separate segregated fund to be utilized for political purposes by a corporation”⁸⁴ The Commission reasoned that Congress had expressly

specified the channels by which this dissemination was to be accomplished and did not include proxy material under the Securities Exchange Act of 1934. [The Commission] cannot assume that the channels chosen by the Congress are inadequate for its purposes or that the agencies with whom the responsibility is placed will not adequately discharge that responsibility.⁸⁵

The Commission also expressed its concern that the disclosure of such information would unduly lengthen a company’s proxy statement, which “serves its intended purpose only if it is read, and any unnecessary deterrents to this objective should be avoided.”⁸⁶

Considering the importance that Congress, through legislation, has placed on issues other than corporate disclosure of public policy expendi-

⁷⁹ *Id.*

⁸⁰ *See* 2 U.S.C. §§ 431–34.

⁸¹ *See* Letter from 11 Constitutional Law Scholars et al., to Elizabeth M. Murphy, Sec’y, U.S. Sec. & Exch. Comm’n 3 (Mar. 23, 2013), available at <http://www.sec.gov/comments/4-637/4637-318.pdf>. Federal reporting requirements are mandated by 2 U.S.C. §§ 432–34; organizational requirements are mandated by 2 U.S.C. §§ 431(4), 431(8). An example of a similar state law is A.R.S. §§ 16-914.02, 16-919, 16-920 (Arizona).

⁸² Letter from 11 Constitutional Law Scholars et al., *supra* note 81.

⁸³ *Id.*

⁸⁴ Denial of Petition Seeking to Amend Rules Promulgated Under Section 14(a) of the Securities Exchange Act of 1934, Exchange Act Release No. 10,325, 1973 SEC LEXIS 2639 (Aug. 7, 1973).

⁸⁵ *Id.*

⁸⁶ *Id.*

tures and Congress's refusal to enact legislation to require this sort of disclosure, the Commission should focus its efforts on issues of much more significance as determined by Congress, such as those that are responsive to the 2008 financial crisis and central to the economically important capital-raising functions of the capital markets.

CONCLUSION

Efforts to force mandatory disclosure of corporate spending on political and other advocacy activities should be viewed as primarily political rather than economic and, as such, would not serve to help shareholders evaluate corporate performance or promote shareholder value. In fact, many advocates seeking to impose such requirements, specifically union and social investment funds, have emphasized their intentions to curb speech that they see as opposed to their own political interests.

Historically, Congress has decided issues of federal disclosure standards, enacting detailed legislation governing both political and lobbying expenditures. Efforts by activists to expand such legislation have failed. In 2010, Congress explicitly decided not to require the types of disclosure rules set forth by the Petition. Frustrated by this outcome, activists seek to circumvent the congressional process through the SEC, an entity with far less experience in regulating political and lobbying expenditures.

Ultimately, the SEC is not the appropriate body to address this issue, primarily because SEC does not have the authority to require disclosure of information on these sorts of immaterial expenditures. Rational shareholders, considering their economic interests and not political interests, do not consider this information material to their investment decisionmaking. Even if the SEC were to forge ahead and consider a rule, an impartial economic analysis of the costs and benefits of such a requirement would find that the costs exceed the purported benefits because the narrow interests of an extremely vocal minority of shareholders (and even non-shareholder activists) could more easily intimidate value-creating corporate behavior, create brand damage to the disclosing companies, and stifle corporate speech, all of which would have a detrimental economic effect on the company and its shareholders. Finally, considering the importance that Congress has placed on issues other than corporate disclosure of public policy expenditures and its refusal to enact legislation to require this sort of disclosure, the Commission should focus its efforts on issues of much more significance as determined by Congress, such as those that are responsive to the 2008 financial crisis and central to the economically important capital-raising functions of the securities markets.

During her tenure, SEC Chairman Mary Jo White will have an opportunity to focus on many issues of import to shareholders and securities markets. Chairman White would be best advised to side with real investors instead of partisan, political activists.

