

*Symposium on Corporate Political Spending*

AGAINST AN SEC-MANDATED RULE ON  
POLITICAL SPENDING DISCLOSURE:  
A REPLY TO BEBCHUK AND JACKSON

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ABSTRACT

*Professors Lucian Bebchuk and Robert Jackson argue that the Securities and Exchange Commission (SEC) should engage in rulemaking to consider rules mandating new corporate political-spending disclosures, but their rationale is inconsistent with the agency's statutory purpose of protecting investors, improving market efficiency, and facilitating capital formation. Corporations' political expenditures are tiny in relation to corporate budgets and clearly immaterial, in and of themselves, to investors' financial interests. Bebchuk and Jackson's argument that corporate political spending is more related to agency costs than to corporate leaders' legitimate desire to ameliorate the potential adverse impacts of government action on businesses' earnings, and that such agency costs could helpfully be reduced by further disclosures, is highly speculative. Instead, evidence strongly suggests that special-interest groups with viewpoints adverse to corporate interests have attempted to leverage existing disclosures to chill corporate political participation. Finally, shareholder proposals involving corporate political spending and political-spending disclosure have been overwhelmingly sponsored by some of these same special-interest groups and universally rejected by shareholders at large, when opposed by boards of directors.*

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## INTRODUCTION

In their article “Shining Light on Corporate Political Spending,”<sup>1</sup> professors Lucian Bebchuk and Robert Jackson articulate a case for rulemaking by the Securities and Exchange Commission (“SEC” or “Commission”), regarding the mandatory disclosure of publicly traded companies’ spending that may be related to politics. Bebchuk and Jackson’s new article expands upon the case they made in an earlier article they published on corporate political speech,<sup>2</sup> and on the rulemaking petition they submitted to the SEC on their own and certain other law professors’ behalf,<sup>3</sup> which the Commission is now considering.<sup>4</sup> Though their article is lucidly presented, the case made by professors Bebchuk and Jackson is ultimately unpersuasive.

At the outset, I note that for the purposes of this reply, I generally take no position on the constitutional issues underlying the Supreme Court’s controversial decision in *Citizens United v. Federal Election Commission*,<sup>5</sup> which held that independent political expenditures constitute speech protected by the First Amendment, regardless of whether the speaker is a corporation.<sup>6</sup> Indeed, under *Citizens United*, Congress may be able to regulate

<sup>1</sup> Lucian A. Bebchuk & Robert J. Jackson, Jr., *Shining Light on Corporate Political Spending*, 101 GEO. L.J. 923 (2013).

<sup>2</sup> See generally Lucian A. Bebchuk & Robert J. Jackson, Jr., *Corporate Political Speech: Who Decides?*, 124 HARV. L. REV. 83 (2010).

<sup>3</sup> Letter from Comm. on Disclosure of Corp. Pol. 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 the Petition].

<sup>4</sup> See Emily Chasan, *SEC Staff Considers Proposal on Corporate Political Donations*, WALL ST. J. CFO REP. (Nov. 8, 2012), <http://mobile.blogs.wsj.com/cfo/2012/11/08/sec-staff-considers-proposal-on-corporate-political-donations/>.

<sup>5</sup> 558 U.S. 310 (2010).

<sup>6</sup> See *id.* at 371–72.

certain further disclosures of political spending, corporate or otherwise, without running afoul of the First Amendment.<sup>7</sup> I note that professors Bebchuk and Jackson far too casually assume the constitutionality of their proposal,<sup>8</sup> without giving careful consideration to the distinction between facial and as-applied constitutional challenges and the Supreme Court's focus, in the *Citizens United* decision itself, on the potential harassment of speakers, including corporations.<sup>9</sup>

In addition, I agree with the following propositions advanced by professors Bebchuk and Jackson: (1) that SEC rules change over time;<sup>10</sup> (2) that corporations spend some money, which is not disclosed, on funding trade

<sup>7</sup> See *id.* at 366–67 (citing *McConnell v. FEC*, 540 U.S. 93, 198 (2003)) (rejecting facial and as-applied challenges to disclosure requirement).

<sup>8</sup> See Bebchuk & Jackson, *supra* note 1, at 954–55 (arguing that it is “clear” that “that the Constitution leaves ample room for disclosure rules of this kind”) (citing Bebchuk & Jackson, *supra* note 2, at 107–11 (asserting that “the constitutional permissibility of the disclosure requirements that [they] propose is straightforward”).

<sup>9</sup> Political spending disclosure requirements do not necessarily or easily pass constitutional muster. Rather, “[t]he Court has subjected these requirements to ‘exact[ing] scrutiny,’ which requires a ‘substantial relation’ between the disclosure requirement and a ‘sufficiently important’ governmental interest.” *Citizens United*, 558 U.S. at 366–67 (citing *Buckley v. Valeo*, 424 U.S. 1, 64 66 (1976)).

Even in cases in which a disclosure statute passes constitutional muster *on its face*, it may fail an “as applied” challenge when there exists “a ‘reasonable probability’ that disclosure of its contributors’ names ‘will subject them to threats, harassment, or reprisals from either Government officials or private parties.’” *Id.* (citing *McConnell*, 540 U.S. at 198 (quoting *Buckley*, 424 U.S. at 74)). In *Citizens United*, the Court reaffirmed this principle, *see id.* at 916 (observing that a disclosure statute “would be unconstitutional as applied to an organization if there were a reasonable probability that the group’s members would face threats, harassment, or reprisals if their names were disclosed”), but noted that “Citizens United . . . ha[d] offered no evidence that its members may face similar threats or reprisals. . . . [and indeed] ha[d] been disclosing its donors for years and ha[d] identified no instance of harassment or retaliation.” *Id.*

In contrast to the dearth of evidence demonstrating that disclosure of donors to Citizens United raised the risk of harassment or retaliation, ample evidence exists that companies would be subject to reprisals for donating to some of the very trade associations and business groups specifically targeted by the proponents of corporate political spending disclosure. See Petition, *supra* note 3, at 10 n.29 (asserting that disclosure of “contributions to intermediaries that spend a large fraction of their funds on politics . . . seems warranted,” and singling out the U.S. Chamber of Commerce); Bebchuk & Jackson, *supra* note 1, at 932. Both “socially responsible” investing funds, Walden Asset Management and the New York City Comptroller, have harassed and implicitly threatened reprisals against companies known to be affiliated with the U.S. Chamber. See Press Release, Walden Asset Mgmt., Investors Call on Companies Sitting on The U.S. Chamber of Commerce Board to Evaluate Their Role (Jan. 31, 2011), available at <http://climate.bna.com/climate/document.aspx?ID=153882>; Press Release, N.Y. City Comptroller, Comptroller Liu Calls On Siemens AG To Cut Ties To U.S. Chamber Of Commerce (Jan. 24, 2011), available at [http://comptroller.nyc.gov/press/2011\\_releases/pr11-01-007.shtm](http://comptroller.nyc.gov/press/2011_releases/pr11-01-007.shtm). In addition, the activist group Color of Change harassed companies known to be affiliated with the American Legislative Exchange Council, causing several such companies to drop their membership. See Press Release, Color Of Change, Color of Change Applauds Procter & Gamble’s Decision to End its Membership in ALEC: More Than A Dozen Companies Have Left the American Legislative Exchange Council (Apr. 23, 2012), available at <http://www.colorofchange.org/press/releases/2012/4/23/colorofchange-applauds-procter-gambles-decision-en/>.

<sup>10</sup> See Bebchuk & Jackson, *supra* note 1, at 928–30.

associations or other organizations that spend some of their money on politics;<sup>11</sup> (3) that some shareholders have expressed interest in additional disclosures of corporate political spending;<sup>12</sup> and (4) that some companies have disclosed certain forms of spending that may relate to politics, beyond that required by law.<sup>13</sup> Although I interpret somewhat differently the data presented by professors Bebchuk and Jackson in advancing these propositions, and augment it with other data that illuminate the issues raised, I do not dispute the reductionist forms of their broad assertions; indeed, the first proposition is an obvious truism, and the second, third, and fourth rather clear.

Contrary to professors Bebchuk and Jackson, however, I do not believe that the aforementioned four basic propositions, in combination, lead ineluctably to the conclusion that an SEC-based rule mandating political-spending disclosure is warranted. Disclosure of spending on politics is not only far afield from the Commission's stated purposes—protecting investors, ensuring market efficiency, and facilitating capital formation<sup>14</sup>—but a mandatory rule in this area is likely to harm investors, to generate market inefficiencies, and to inhibit capital formation.

In Part I, I argue that SEC-mandated disclosure of corporate political spending is likely to harm investors (a) because corporations' expenditures related to politics are not, *as expenditures*, material to shareholders' risk-adjusted expected returns; (b) because additional disclosures of corporate spending that may relate to politics would not, on balance, decrease shareholder ownership costs; and (c) because increased disclosure of political spending would chill publicly held corporations' political speech to shareholders' detriment. In Part II, I argue that shareholders' actual revealed preferences counsel against rulemaking in this area.

#### BACKGROUND INFORMATION

Under the Securities Exchange Act,<sup>15</sup> any SEC rulemaking is required to consider both the "protection of investors" and "whether the action will promote efficiency, competition, and capital formation."<sup>16</sup> Given this "unique obligation" upon the SEC, any "failure" on the Commission's part

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<sup>11</sup> See *id.* at 929–35.

<sup>12</sup> See *id.* at 935–37.

<sup>13</sup> See *id.* at 938–41.

<sup>14</sup> See *What We Do*, U.S. SEC. & EXCH. COMM'N, <http://www.sec.gov/about/whatwedo.shtml> ("The mission of the U.S. Securities and Exchange Commission is to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation.") (last visited Feb. 26, 2013).

<sup>15</sup> Pub. L. 73–291, 48 Stat. 881 (1934), codified at 15 U.S.C. § 78a et seq. (2006).

<sup>16</sup> 15 U.S.C. § 78c(f) ("Whenever pursuant to this title the Commission is engaged in rulemaking, or in the review of a rule of a self-regulatory organization, and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.").

to “‘apprise itself—and hence the public and the Congress—of the economic consequences of a proposed regulation’ makes promulgation of the rule arbitrary and capricious and not in accordance with law.”<sup>17</sup> As the D.C. Circuit’s recent decision in *Business Roundtable v. SEC* makes clear, the SEC’s statutory obligation is not merely *pro forma*; rather, the Commission must “quantify” the costs of proposed rules and evaluate the unintended economic consequences of any new rulemakings.<sup>18</sup> The rulemaking on political-spending disclosure proposed by professors Bebchuk and Jackson would inevitably fail to meet this threshold.

## I. ADDITIONAL DISCLOSURES OF CORPORATE POLITICAL SPENDING WOULD HARM INVESTORS

### A. *Corporations’ expenditures related to politics are not, as expenditures, material to shareholders’ financial interests as investors.*

Professors Bebchuk and Jackson correctly observe that public companies “engage in political spending that is never disclosed by channeling that spending through intermediaries.”<sup>19</sup> Such spending, however, is such a small percentage of corporate budgets that it is plainly, on its own, immaterial to investors’ financial interests as shareholders.

The Commission has long adopted the position that “in administering the disclosure process under the Securities Act and the Securities Exchange Act,” it requires disclosure “only of such information as the Commission believes is important to the reasonable investor—*material information*. This *limitation* is believed necessary in order to insure meaningful and useful disclosure documents of benefit to most investors without unreasonable costs to registrants and their shareholders.”<sup>20</sup>

<sup>17</sup> *Business Roundtable v. SEC*, 647 F.3d 1144, 1148 (D.C. Cir. 2011) (citations omitted).

<sup>18</sup> *See id.* at 1149–52, 1156 (rejecting as arbitrary and capricious SEC’s proposed proxy access rule, where Commission did not adequately conduct cost-benefit analysis and consider potential “that investors with a special interest, such as unions and state and local governments whose interests in jobs may well be greater than their interest in share value, can be expected to pursue self-interested objectives rather than the goal of maximizing shareholder value”)

<sup>19</sup> Bebchuk & Jackson, *supra* note 1, at 927.

<sup>20</sup> 40 Fed. Reg. 51,656, 51,660 (Oct. 16, 1975) (rejecting rulemaking petitions seeking mandatory disclosure of certain environmental impacts and minority and women hiring data); *see also* *Natural Res. Def. Council, Inc. v. SEC*, 606 F.3d 1031, 1062 (D.C. Cir. 1979) (reversing lower court decision that the Commission had acted arbitrarily and capriciously in denying the petition). *Cf.* *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438 (1976) (adopting materiality standard for securities-fraud litigation alleging inadequate proxy-statement disclosures).

I note that professors Bebchuk and Jackson cite *Natural Resources Defense Council* for the broad deference it suggests is due the SEC in disclosure-related decisions, *see* Bebchuk & Jackson, *supra* note 1, at 929 n.16, but fail to acknowledge the “special deference” the court gave to the Commission in light of the “peculiar context” that case, *i.e.*, a challenge to “an agency decision Not to adopt a rule,” which led the court “to inquire seriously whether the SEC’s decision was reviewable at all.” *Natural Res. Def. Council, Inc.*, 606 F.3d at 1052. This

Professors Bebchuk and Jackson argue that certain evidence they offer of “spending by just eight of the most active intermediaries between public companies and politics” supports a materiality conclusion: according to the professors’ calculations, the amount spent by these groups “exceeded \$1.5 billion between 2005 and 2010, which is hardly a trivial sum.”<sup>21</sup> While \$1.5 billion is indeed not “trivial,” the question for the SEC is not whether spending is *trivial* but whether it is *material*. The spending identified by professors Bebchuk and Jackson amounts to \$260 million annually; but the combined revenues of the 200 largest U.S. companies in 2012 exceeded \$9.4 trillion.<sup>22</sup> Put differently, the annual spending listed by professors Jackson and Bebchuk constitutes only 0.0028 percent of Fortune 200 companies’ current revenues—a percentage which is hardly, on its own terms, material to a reasonable investor.<sup>23</sup>

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omitted context is particularly striking given the D.C. Circuit’s much more recent embrace of a more exacting cost-benefit review standard in *Business Roundtable*, 647 F.3d at 1149–51, in reviewing the Commission’s affirmative adoption of a proxy access rule, which Bebchuk and Jackson obliquely dismiss by citation to critical academic commentary, without further discussion, see Bebchuk & Jackson, *supra* note 1, at 965 n.143.

<sup>21</sup> See *id.* at 956. Bebchuk and Jackson’s numbers unhelpfully conflate these trade groups’ lobbying expenses with their independent political expenditures. Trade associations typically devote more resources to lobbying than to independent political expenditures: the U.S. Chamber of Commerce, for instance, spent almost four times as much on federal lobbying in 2012 as on political spending in the 2011–12 election cycle. See *Organization Profiles, CTR. FOR RESPONSIVE POL.*, <http://www.opensecrets.org/orgs/index.php> (last visited Aug. 19, 2013), and the Chamber, as the tenth-largest outside political spender in that election cycle, was the only 501(c)(6) trade association among the ten largest outside-spending organizations. See *Organization Profiles, Top Outside Spending Organizations 2011–12, CTR. FOR RESPONSIVE POL.*, <http://www.opensecrets.org/orgs/index.php> (last visited Aug. 19, 2013).

<sup>22</sup> See *Fortune 500, CNN MONEY* (May 21, 2012), [http://money.cnn.com/magazines/fortune/fortune500/2012/full\\_list/](http://money.cnn.com/magazines/fortune/fortune500/2012/full_list/) (listing top 500 U.S. companies by revenues). Note that certain of the Fortune 200 companies are not publicly held. That said, the 42 largest companies on the Fortune 200 list, with a combined revenues exceeding \$5 trillion, are publicly traded (Fannie Mae and Freddie Mac, however, were delisted upon entering government receivership). The two largest American private companies, Cargill and Koch Industries do not show up on the *Fortune* list, presumably due to data limitations. See Andrea Murphy & Scott DeCarlo, *America’s Largest Private Companies, FORBES* (Nov. 28, 2012), <http://www.forbes.com/largest-private-companies/>. The largest company on the *Fortune* list that is not a public C corporation is State Farm, a mutual insurer, at 43rd. *Id.* While the presence of such companies marginally inflates the revenues of the Fortune 200 attributable to public companies, it is also of course the case that many companies, beyond the 200 largest, make money, are publicly listed, and may be involved directly or indirectly in political spending.

<sup>23</sup> Auditors typically assume that for publicly traded companies, an item is not material if it is “not greater than 5 percent of net income before income taxes.” *Audit Manual Excerpt: Materiality Guidelines, WILLIAMS & ADAMS, CPAs*, [http://higherend.mcgraw-hill.com/sites/dl/free/0078025435/928516/WA\\_Materiality\\_Guidelines\\_8e.pdf](http://higherend.mcgraw-hill.com/sites/dl/free/0078025435/928516/WA_Materiality_Guidelines_8e.pdf) (last visited Aug. 19, 2013). Consistent with this general principle, under SEC rules, shareholder proposals are deemed not relevant and excludable from a publicly traded corporation’s proxy statement “[i]f the proposal relates to operations which account for less than 5 percent of the company’s total assets at the end of its most recent fiscal year, and for less than 5 percent of its net earnings and gross sales for its most recent fiscal year . . . .” 17 C.F.R. § 240.14a-8(i)(5) (2008). (Shareholder proposals involving corporate political spending, like other cases involving “political and moral predilections,” can appear on proxy ballots under an exception to this rule predicated on longstanding D.C. Circuit precedent. See *Med. Comm. for Human Rights v. SEC*, 432 F.2d 659, 682 (D.C. Cir. 1970) (remanding to the SEC for reconsideration a no-action letter that

To be sure, the eight groups identified by professors Bebchuk and Jackson—the U.S. Chamber of Commerce, the Business Roundtable, the National Association of Manufacturers, the Pharmaceutical Research and Manufacturers Association (PhRMA), the American Petroleum Institute, America’s Health Insurance Plans, the American Council on Life Insurance, and the Financial Services Roundtable—are not the only intermediaries receiving corporate funding that spend money on politics, though they are the “heavy hitters” among trade associations and related business groups organized under Section 501(c)(6) of the U.S. Code,<sup>24</sup> and there is no reason to believe that a substantial volume of corporate dollars flows into trade associations other than those listed by Bebchuk and Jackson, at least not sufficient to infer that such dollars, as expenditures, are material to shareholders’ investing interests, given the vast gap between the total dollar amounts in question and corporate budgets. In addition to such trade associations, however, corporations can contribute money to the political process through political action committees and other political committees organized under Section 527 of the Code,<sup>25</sup> as well as through social-welfare organizations organized under Section 501(c)(4) of the Internal Revenue Code.<sup>26</sup> The conclusion that corporate spending on politics is immaterial on its face to shareholders’ pecuniary interests still holds even if factoring in these other possible ways corporations might spend money in this area.

Among the political committees organized under Section 527 of the Internal Revenue Code, are, after *Citizens United*, political action committees that can, independently of candidate campaigns, spend money for political purposes (so-called “Super PACs”), though contributions to and expenditures by such organizations must be fully disclosed. In the 2012 political cycle, such PACs raised over \$838 million and spent over \$631 million<sup>27</sup>—significant sums, to be sure, but a pittance in comparison with overall public-company budgets. Moreover, contributions to these Super PACs from publicly traded companies have proved virtually nonexistent.<sup>28</sup>

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would have permitted Dow Chemical to exclude a shareholder resolution involving its sale of napalm), *aff’d* 404 U.S. 403 (1972) (affirmed for mootness, after Dow included the resolution on its proxy). Similarly, under Regulation S-K, the SEC deems that legal proceedings are not material “if the amount involved, exclusive of interest and costs, does not exceed 10 percent of the current assets of the registrant and its subsidiaries on a consolidated basis.” 17 C.F.R. § 229.103(2) (2008).

<sup>24</sup> See 26 U.S.C. § 501(c)(6) (2010). Cf. *Organization Profiles*, CTR. FOR RESPONSIVE POL., <http://www.opensecrets.org/orgs/index.php> (last visited Aug. 19, 2013) (listing the U.S. Chamber of Commerce as the only trade association among top outside spending organizations in the 2011–12 election cycle, at tenth).

<sup>25</sup> See 26 U.S.C. § 527 (2010).

<sup>26</sup> See 26 U.S.C. § 501(c)(4) (2010).

<sup>27</sup> See *Super PACs*, CTR. FOR RESPONSIVE POL., <http://www.opensecrets.org/pacs/super/pacs.php?cycle=2012> (last visited Mar. 5, 2013).

<sup>28</sup> See, e.g., Anna Palmer & Annie Phillip, *Corporations Don’t Pony Up for Super PACs*, POLITICO (Mar. 8, 2012), <http://www.politico.com/news/stories/0312/73804.html> (“When super PACs emerged two years ago, critics howled that corporations would take advantage of a newfound tool to flex their muscle in politics. But so far this campaign season, publicly traded

Five such PACs spent over \$20 million in the 2012 campaign: the pro-Romney Restore Our Future, the pro-Obama Priorities USA Action, Karl Rove's American Crossroads, and Super PACs supporting Senate and House Democrats;<sup>29</sup> all told, these five PACs raised and spent a majority of all Super PAC dollars in the campaign (raising and spending \$428 million and \$380 million, respectively).<sup>30</sup> Only *one* publicly traded corporation was among the top fifty organizational donors to any of these Super PACs: the small-cap, family-controlled but Nasdaq-listed Clayton Williams Energy, which contributed \$1 million to American Crossroads.<sup>31</sup> And the top-fifty donor lists comprised most of each Super PAC's funding, in total over \$314 million of the \$428 million these five political committees raised.<sup>32</sup>

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companies have shied away from the outside groups—giving less than one half of a percent of all the contributions raised by the most active super PACs.”).

<sup>29</sup> See *Super PACs*, *supra* note 27.

<sup>30</sup> See *id.*

<sup>31</sup> See *id.* Investors would have to have been particularly obtuse to be surprised by Clayton Williams Energy's contribution to American Crossroads. The firm's octogenarian founder, chairman, and chief executive officer, Clayton Williams, was the Republican nominee for governor in Texas in 1990, was a bundler for 2008 presidential candidate John McCain, and made headlines when McCain canceled a fundraiser at Williams's home after public controversy erupted surrounding some of the oilman's prior public comments. See Juliet Eilperin, *McCain Texas Fundraiser Back on, Sans Oilman*, WASH. POST THE TRAIL BLOG (June 15, 2008), <http://blog.washingtonpost.com/44/2008/06/mccain-texas-fundraiser-back-o.html?hpid=topnews#trove-tab-3>. Moreover, the roughly 0.25 percent of its sales that Clayton Williams Energy donated to American Crossroads is not material to investors' financial interests in that company. Finally, Mr. Williams and a limited partnership controlled by his adult children own 51 percent of the company's outstanding shares. See Clayton Williams Energy, Inc., Annual Report (Form 10-K) (Mar. 5, 2013), at 7 (“Clayton W. Williams, Jr. beneficially owns, either individually or through his affiliates, approximately 26% of the outstanding shares of our Common Stock. In addition, The Williams Children's Partnership, Ltd. (‘WCPL’), a limited partnership of which Mr. Williams' adult children are the limited partners, owns an additional 25% of the outstanding shares of our Common Stock. Mr. Williams is also Chairman of our Board of Directors (the ‘Board’), President and Chief Executive Officer.”), such that any shareholder vote on the donation would have affirmed the decision—as would be evident to any investor who read Item 1 of the company's 10-K filing.

<sup>32</sup> Cf. *Top Organizations Disclosing Donations to Restore Our Future, 2012*, CTR. FOR RESPONSIVE POL., <http://www.opensecrets.org/outsidespending/contrib.php?cmte=CO0490045&type=T> (last visited Mar. 5, 2013); *Top Organizations Disclosing Donations to American Crossroads, 2012*, CTR. FOR RESPONSIVE POL., <http://www.opensecrets.org/outsidespending/contrib.php?cmte=CO0487363&type=T> (last visited Mar. 5, 2013); *Top Organizations Disclosing Donations to Priorities USA Action, 2012*, CTR. FOR RESPONSIVE POL., <http://www.opensecrets.org/outsidespending/contrib.php?cmte=CO0495861&type=T> (last visited Mar. 5, 2013); *Top Organizations Disclosing Donations to Majority PAC, 2012*, CTR. FOR RESPONSIVE POL., <http://www.opensecrets.org/outsidespending/contrib.php?cmte=CO0484642&type=T> (last visited Mar. 5, 2013); *Top Organizations Disclosing Donations to House Majority PAC, 2012*, CTR. FOR RESPONSIVE POL., <http://www.opensecrets.org/outsidespending/contrib.php?cmte=CO0495028&type=T> (last visited Mar. 5, 2013).

Note that organizations *did* contribute in significant volume to these Super PACs: direct organizational contributions constituted 14 percent of top 50 donations to Restore Our Future, 20 percent to American Crossroads, 24 percent to Priorities USA Action, and 53 percent to each of the Democratic Congressional PACs. Such direct organizational contributions, however, came from *privately owned* companies (with the aforementioned exception of Clayton Williams), as well as, in the case of the Democrat-oriented funds, labor unions and law firms. Indeed, labor unions, not corporations, appear to be the organizations most utilizing the ability to donate directly to Super PACs under *Citizens United*.

Apart from Super PACs, “social welfare” organizations organized under Section 501(c)(4) of the Internal Revenue Code can make political expenditures, and unlike PACs (but like 501(c)(6) trade associations), 501(c)(4) organizations’ donors do not have to be publicly disclosed.<sup>33</sup> In the 2012 election cycle, four such organizations spent over \$20 million each related to federal campaigns: Crossroads GPS (the smaller (c)(4) adjunct to Rove’s American Crossroads Super PAC), Americans for Prosperity, the American Future Fund, and the National Rifle Association.<sup>34</sup> Although publicly traded corporations could contribute to these organizations, the aggregate amounts spent by such groups on the 2012 elections—while certainly significant relative to overall spending on the elections—were immaterial in terms of corporate budgets. Indeed, the 93 entities organized under Section 501(c) of the Internal Revenue Code that spent at least \$100,000 in the 2012 campaign—including not only (c)(4) organizations but also (c)(6) trade associations and labor unions—spent a total of just over \$463 million in the election cycle,<sup>35</sup> an amount equivalent to 0.0049 percent of Fortune 200 companies’ revenues in the same year.

In all, outside groups—including Super PACs, 527 committees, and 501(c) organizations, drawn from all sources (corporate or not)—spent just over \$1 billion on the 2012 campaigns,<sup>36</sup> equivalent to 0.011 percent of the Fortune 200 companies’ 2012 budgets. This total sum is less than the development cost of a single biotechnology product,<sup>37</sup> and less than the amount that automobile manufacturers and dealers spent on television advertising spots with local broadcasting stations in the third quarter of 2012.<sup>38</sup> It is impossible to conclude that political spending, on its own, is material to investors’ pecuniary interests as shareholders.<sup>39</sup>

<sup>33</sup> Cf. *NAACP v. Alabama*, 357 U.S. 449 (1958) (holding that organization’s freedom of association rights prevented Alabama from requiring disclosure of its contributor lists).

<sup>34</sup> See *2012 Outside Spending, by Group*, CTR. FOR RESPONSIVE POL., <http://www.opensecrets.org/outsidespending/summ.php?cycle=2012&type=p&disp=O> (last visited Mar. 5, 2013).

<sup>35</sup> Cf. *id.* (aggregation of 501(c) filings on file with author).

<sup>36</sup> See *id.*

<sup>37</sup> See Joseph A. DiMasi & Henry G. Grabowski, *The Cost of Biopharmaceutical R&D: Is Biotech Different?*, 28 *MANAGERIAL & DEC’N ECON.* 469–79 (2007) (estimating the total development cost of a biotechnology product at \$1.2 billion).

<sup>38</sup> See *Top 25 Local Broadcast TV Categories, Spot TV Q3*, TVB LOCAL MEDIA MARKETING SOLUTIONS, <http://www.tvb.org/trends/4705> (last visited Feb. 25, 2013) (citing Kantar Media) (showing local spot TV “automotive” spend of \$925 million and “car and truck dealers” of \$273 million in the third quarter of 2012).

I am not the first to make this sort of comparison. In a 2010 blog post, UCLA’s Stephen Bainbridge compared total 2008 political spending to Procter & Gamble’s 2008 advertising on soap and toilet paper. See *Is Citizens United the death of democracy*, PROFESSORBAINBRIDGE.COM (Oct. 19, 2010), <http://www.professorbainbridge.com/professorbainbridgecom/2010/10/is-citizens-united-the-death-of-democracy.html>.

<sup>39</sup> The fact that corporate political spending, in the aggregate, is far too insignificant to be material for disclosure on investors’ balance sheets does not mean that corporate political spending, in the aggregate, is irrelevant to the financial interests of diversified shareholders. Indeed, the principal problem with increased disclosure of corporate spending that may affect

*B. Additional disclosures of corporate spending that may relate to politics would not, on balance, decrease shareholder ownership costs.*

Even though corporate spending that may relate to politics is not, on its face, material to shareholders' financial interests as investors, an SEC rulemaking in this area might conceivably be warranted if, on balance, further disclosures of such spending decreased shareholders' cost of ownership (i.e., agency costs).<sup>40</sup> Indeed, mitigating a potential divergence of interests between *managers'* political preferences and *shareholders'* interests is central to the argument professors Bebchuk and Jackson advance.<sup>41</sup>

In assessing the potential impact of political-spending disclosure rules on shareholders' cost of ownership, it is critical to understand that the cost of monitoring managers is not the only cost of ownership.<sup>42</sup> Rather, ownership

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politics—including through trade associations and 501(c)(4) social-welfare organizations—is that such disclosure would necessarily chill corporate political speech in such associational forms by subjecting corporations' participation in such groups to attacks, including consumer boycotts, by political activists hostile to corporations' or industries' concerns. Even though corporations' contributions to politics are so small as to be insignificant, on their face, to companies' bottom lines, it does not follow that companies would be no worse off if all companies unilaterally exited from politics; to the contrary, trade associations and other coordinated corporate efforts advance companies' interests in the political sphere by mitigating free-rider problems and facilitating corporate electoral participation without fear of consumers' or politicians' reprisals. See *infra*, section I(C).

<sup>40</sup> I thus agree with professors Bebchuk and Jackson when they note “a finding that political spending is financially significant is not a necessary condition to SEC rules mandating disclosure of that spending.” Bebchuk & Jackson, *supra* note 1, at 956. That said, the evidence they cite for that proposition—relatively low SEC reporting thresholds for executive compensation and related-party transactions—seems to beg the question they are asking, *i.e.*, whether corporate political spending generates sufficient net agency costs (balancing any benefits from monitoring managers against the costs of such monitoring, including collective-decision-making costs and possible adverse reactions on the part of non-owner consumers) to justify a mandatory political-spending disclosure rule, in light of the lack of materiality of such spending on its face. Executive compensation and related-party transactions are both directly pertinent to the classic agency-cost case for management monitoring; and, even if not material on their face, would seem to serve as reasonable proxies helping investors “ferret out” management's possible spoliation of firm assets—a significant consideration given the potential for camouflaging managerial rent extraction. See generally Lucian A. Bebchuk et al., *Managerial Power and Rent Extraction in the Design of Executive Compensation*, 69 U. CHI. L. REV. 751, 788–89 (2002) (discussing the “camouflaging” of managerial rent extraction); Lucian A. Bebchuk & Christine Jolls, *MANAGERIAL VALUE DIVERSION AND SHAREHOLDER WEALTH*, 15 J.L. ECON. & ORG. 487, 501 (1999) (showing that “within the standard principal-agent framework, permitting value-diversion imposes a cost on shareholders that may reduce *ex ante* share value”). Bebchuk and Jackson's political-spending-as-management-misappropriation hypothesis simply lacks the theoretical rigor and empirical foundation underlying management-pay and self-dealing disclosures; and their analysis fails to consider the serious risks that investors and customers would try to pressure corporations over their political spending, for non-financial reasons, to the average shareholder's detriment.

<sup>41</sup> See Bebchuk & Jackson, *supra* note 1, at 942–44; Bebchuk & Jackson, *supra* note 2, at 90–93.

<sup>42</sup> The proper scope of shareholder voting rights more generally, and the costs as well as benefits to expanding such rights, is fiercely debated in the corporate-governance literature. Compare Lucian A. Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833 (2005) (arguing for increased shareholder power over corporate governance) with Stephen

costs include (1) the cost of monitoring managers, (2) the cost of collective decision-making, and (3) the cost of risk-bearing.<sup>43</sup> The second and third forms of ownership costs are highly significant: although the cost of monitoring managers in large C-corporations with large numbers of shareholders has long been understood to be relatively high,<sup>44</sup> and even though there are commonplace alternative forms of ownership,<sup>45</sup> the largest for-profit enterprises overwhelmingly assume a shareholder-ownership form.

1. *The significance of collective decision-making costs for shareholder corporations*

The fact that shareholder-owned corporations have avoided the high costs of *heterogeneous* collective decision-making by orienting shareholders around a single *homogeneous* concern, shareholder return,<sup>46</sup> is profoundly important in explaining this pattern.<sup>47</sup> As Yale Law professor Henry

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M. Bainbridge, *The Case for Limited Shareholder Voting Rights*, 53 UCLA L. REV. 601 (2006) (arguing that increasing the power of shareholders to hold managers accountable, including through increased disclosure, imposes significant costs in reduced managerial authority).

<sup>43</sup> See generally HENRY HANSMANN, *THE OWNERSHIP OF ENTERPRISE* 35–49 (1996).

<sup>44</sup> See generally ADOLPH A. BERLE & GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* (1932) (the classic exploration of agency costs in the American corporation).

<sup>45</sup> See generally HANSMANN, *supra* note 43. Producer ownership (*e.g.*, agricultural cooperatives and employee-owned firms) and consumer ownership (*e.g.*, retail or wholesale cooperatives, co-op housing structures, and mutual insurance companies and banks) are commonplace, albeit (critically) less so for most of the largest-scale for-profit enterprises.

<sup>46</sup> Shareholder primacy—the notion that corporate managers have a near-exclusive fiduciary obligation to shareholders rather than other corporate “stakeholders”—is deeply rooted in American law, tracing at least as far back as *Dodge v. Ford Motor Company*, in which the Michigan Supreme Court ruled that Henry Ford had a fiduciary duty to manage Ford Motor Company for the benefit of shareholders rather than employees or the broader community. 170 N.W. 668. (Mich. 1919). In the academic literature, Adolph Berle and Gardiner Means were early defenders of the primacy of shareholders’ interests in governing corporate managers’ fiduciary duties, see BERLE & GARDINER, *supra* note 44, and shareholder primacy was buttressed by later law and economics articles conceiving of the corporate form as a nexus of contracts. See, *e.g.*, Armen A. Alchian & Harold Demsetz, *Production, Information Costs, and Economic Organization*, 62 AM. ECON. REV. 777 (1972); Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure*, 3 J. FIN. ECON. 305 (1976). Notwithstanding the more modern push for “corporate social responsibility,” *cf.* CHRISTOPHER STONE, *WHERE THE LAW ENDS* (1975); RALPH NADER, MARK GREEN & JOEL SELIGMAN, *TAMING THE GIANT CORPORATION* (1976); *but see* David L. Engel, *An Approach to Corporate Social Responsibility*, 32 STAN. L. REV. 1, 1 (1979) (“Any mandatory governance reforms intended to spur more corporate altruism are almost sure to have general institutional costs within the corporate system itself. . . . But the proponents of ‘more’ corporate social responsibility have never bothered to analyze or examine, from any clearly defined starting point, even just the benefits they anticipate from reform . . .”), the legal duties of corporate managers have remained essentially shareholder-focused.

<sup>47</sup> In response to Professor Bebchuk’s influential article calling for increased shareholder voting rights, see Bebchuk, *supra* note 42, Professor Stephen Bainbridge argued that the general absence of increased shareholder voting rights in initial public offering documents *ipso facto* suggested their net efficiency, and Bainbridge therefore concluded that limited shareholder voting rights should be preserved as a default rule. See Stephen A. Bainbridge, *Director Primacy and Shareholder Disempowerment*, 119 HARV. L. REV. 1735, 1735–38 (2006).

Hansmann explains in his seminal book *The Ownership of Enterprise*, which empirically analyzes alternative forms of enterprise ownership:

Most fundamentally, political representation evidently performs poorly, relative to markets, where there is any significant conflict of interest among the participants. Or at least this seems to be the obvious conclusion to be drawn from the fact that, although there are hundreds of thousands of firms in the economy, and although these firms exhibit a diverse variety of ownership structures, including a surprisingly large number of firms in which ownership is not in the hands of investors, in virtually all cases the group of individuals to whom ownership is given is extremely homogeneous in its interests. It is extraordinarily rare to find a firm in which control is shared among individuals who have stakes in the enterprise that are at all dissimilar.<sup>48</sup>

The high costs of aggregating votes along heterogeneous interests is self-evident to any observer of real-world electoral republics, as well as to anyone remotely familiar with the public-choice literature, which is predicated substantially upon the notion that it is *impossible* to aggregate heterogeneous interests in binary elections.<sup>49</sup> The significant attention that the D.C. Circuit gave to concerns about special-interest capture of shareholder-voting mechanisms, in its recent *Business Roundtable* decision,<sup>50</sup> implicitly credits the serious risks that heterogeneous shareholder interests can pose when expanding the scope of shareholder voting.

## 2. *The weak case for monitoring corporate managers in this area.*

At the core of professor Bebchuk and Jackson's argument for increased disclosure of corporate spending that may relate to politics is the concern that "corporate political spending may reflect not only directors' and executives' business judgment, but also their political preferences."<sup>51</sup> The professors offer the following hypothetical:

Suppose, for example, that the CEO of Company A has conservative political views and hopes someday to campaign to be Governor in a conservative state, while the CEO of Company B has liberal views and hopes to run for Governor in a liberal state.

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<sup>48</sup> HANSMANN, *supra* note 43, at 288. I note that Professor Hansmann (a valued former teacher and mentor) is among the professors joining Professors Bebchuk and Jackson in their SEC rulemaking petition. See Petition, *supra* note 3. Although he and I obviously differ on the merits of this question, his framework is invaluable to assessing the issue.

<sup>49</sup> See KENNETH K. ARROW, SOCIAL CHOICE AND INDIVIDUAL VALUES (1963) (articulating Arrow's Impossibility Theorem, which holds that, given certain fairness criteria, voters facing three or more ranked alternatives cannot convert their preferences into a consistent, community-wide ranked order of preferences).

<sup>50</sup> 647 F.3d at 1151–52.

<sup>51</sup> Bebchuk & Jackson, *supra* note 1, at 18.

There is no reason to expect that the shareholders of both companies—or even a majority of the investors in each company—have political views that reflect those of the CEOs. Thus, if the companies' political spending is significantly influenced by the CEOs' beliefs, the interests of one or both of the CEOs may be significantly different from those of each company's shareholders.<sup>52</sup>

Bebchuk and Jackson's hypothesis, at its heart, is rather self-contradictory, at least when considering the political spending of intermediaries that receive undisclosed corporate funding. Managers interested in diverting corporate resources to advance their own future political prospects would surely not do so through trade associations. It would be a funny strategy indeed to try to advance one's political career by having one's company make undisclosed donations to the Chamber of Commerce, as opposed to through corporate PACs whose donations and activities would be known by prospective political allies.

Moreover, even if one assumes that some corporate political spending is wasteful, professors Bebchuk and Jackson offer no evidence of how, in practice, such waste has *materially harmed shareholders*,<sup>53</sup> a critical omis-

<sup>52</sup> *Id.*

<sup>53</sup> Professors Bebchuk and Jackson merely observe that the effects of corporate political spending on shareholder value are disputed, *see* Bebchuk and Jackson, *supra* note 1, at 32. Although research in this area continues to evolve, the body of research tended to show that "corporate spending decisions on campaign contributions and lobbying efforts are generally made in a rational and strategic manner" and that "corporate political activity appears to have a generally positive effect on firm value, as reflected in excess market returns," based on a June 2012 literature review published by the Manhattan Institute and principally authored by Robert J. Shapiro—former Under Secretary of Commerce for Economic Affairs in the Clinton administration, where he oversaw the Bureau of Economic Analysis. ROBERT J. SHAPIRO & DOUGLAS DOWSON, CTR. FOR LEGAL POL'Y, MANHATTAN INST., CORPORATE POLITICAL SPENDING: WHY THE NEW CRITICS ARE WRONG 22 (2012), available at [http://www.manhattan-institute.org/pdf/lpr\\_15.pdf](http://www.manhattan-institute.org/pdf/lpr_15.pdf). In an online blog post, *see* John C. Coates IV, *Update on Corporate Political Activity*, HARV. L. SCH. FORUM ON CORP. GOVERNANCE (July 2, 2012), <http://blogs.law.harvard.edu/corpgov/2012/07/03/update-on-corporate-political-activity/>, and in a submission to the SEC, *see* Letter from John C. Coates IV, to Elizabeth M. Murphy, Sec'y, U.S. Sec. & Exch. Comm'n, at 1 (Feb. 4, 2013), available at <http://www.sec.gov/comments/4-637/4637-1473.pdf>. Harvard law professor John C. Coates IV disputes this characterization and defends his own findings, recently published in the *Journal of Empirical Legal Studies*, which present several empirical tests that he claims buttress the corporate-political-spending-as-agency-cost hypothesis. *See* John C. Coates IV, *Corporate Politics, Governance, and Value Before and After Citizens United*, 9 J. EMPIRICAL LEGAL STUD. 657, 680–90 (2012) [hereinafter Coates, *Corporate Politics, Governance, and Value*].

Coates' analysis is unpersuasive. Most critically, Professor Coates' empirical tests assess corporate political engagement solely through companies' *binary* decisions to lobby or spend money through political action committees, without regard to the *intensity* of such efforts—a curious choice, given that Coates lists lobbying and PAC *spending levels* in his table of summary statistics. *See* Coates, *Corporate Politics, Governance, and Value*, *supra*, at 673–74 tbl. 1; *see also* SHAPIRO & DOWSON, *supra*, at 22 ("[I]n contrast to most of the literature in this area, both Coates studies consider only the decision to contribute or lobby while ignoring the level and intensity of the associated expenditures. This surprising and unexplained omission from Coates's models render his remaining conclusions, at best, highly problematic."). There would seem to be little justification for Coates's decision not to attempt to demonstrate that the

relationship he observes is robust using spending levels as an explanatory variable, as well as when using a simple dummy variable; indeed, a Manhattan Institute review of political spending by the 250 largest companies in America reveals that *not a single one* spent no money on politics in the 2011–12 electoral cycle.

Shapiro's Manhattan Institute study assessed data presented in an earlier, simpler version of Coates's study, *see* John C. Coates IV, *Corporate Governance and Corporate Political Activity: What Effect Will Citizens United Have on Shareholder Wealth?* (Sept. 21, 2010) (unpublished manuscript), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1881883](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1881883) [hereinafter "Coates Unpublished Manuscript"], and showed that Coates's own "data show that the correlation reverses when one looks at PAC-contribution levels: as corporate governance improves from 4 to 3, 3 to 2, 2 to 1, and 1 to zero, the average level of PAC contributions increases." SHAPIRO & DOWSON, *supra*, at 20 fig. 7. "Coates does not discuss" this association, which "contradicts his basic thesis." *Id.* at 20. While professor Coates's published 2012 study, unlike his earlier unpublished manuscript, employs firm size and industry as controls in its regression analyses of firm value and political activity, *see* Coates, *Corporate Politics, Governance, and Value*, *supra*, at 680–88; *but see* Coates Unpublished Manuscript, *supra*, at 28, tbl.8, he continues to use only a binary dummy variable for corporate lobbying and PAC contributions and fails to show evidence that his analysis is robust using spending levels as explanatory variables. *See* Coates, *Corporate Politics, Governance, and Value*, *supra*, at 680–88, tbls. 5, 6. And tellingly, in his later study, Coates finds the binary decisions to lobby and to contribute to PACs are each *positively* associated with firm value, when control variables are included, for "highly regulated industries," *see id.* at 682–84, tbl. 5—a subset that "encompasses roughly one-third of GDP and includes alcohol, tobacco, aircraft, pharmaceuticals, utilities, telecommunications, transportation, banking, and insurance." Shapiro & Dowson, *supra*, at 21.

Coates's 2012 study also includes an additional regression analysis showing that "[f]irms that were politically active in 2008 experienced an average 8 percent lower increase in their industry-relative shareholder value from their crisis-era lows when compared to firms that were politically inactive in 2008." Coates, *Corporate Politics, Governance, and Value*, *supra*, at 686–88, tbl.6. Curiously, for this analysis, Coates aggregates whether firms lobbied or contributed to a PAC in 2008 into a single dummy variable, for which he tracks an interaction effect with firm value in 2010. *See id.* He does not show that this finding is robust using separate lobbying and PAC dummy variables (the very variables he tested in his other analysis); nor does he show any test for the subset of firms in "heavily regulated" industries that his other regressions found to be positively associated with firm value. *See id.* Nor, again, does he show that his findings are robust using *spending levels* as opposed to the binary decision to lobby and/or contribute to a PAC. *See id.*

Even assuming that Coates's difference-in-differences test using aggregated binary dummy variables to capture 2008 political activity and post-2010 firm value were robust, his results are open to an interpretation other than the one he posits. Coates suggests that his results are consistent with the hypothesis that the exogenous shock of the Supreme Court's *Citizens United* decision, in 2010, caused a drop in firm value for companies that had lobbied or contributed to a PAC in 2008. It would seem at least as plausible, however, that those firms that decided to be politically active in 2008—a presidential-election year, with a significant likelihood of a White House change in party control—were those whose managements considered the companies vulnerable to political shifts; and that exogenous shocks in 2010 *other than Citizens United*—including but not limited to profound legislative overhauls in the health-care and financial sectors—disproportionately hurt those companies with managements who had felt vulnerable to political shifts back in 2008. Coates claims that his "model rules out potential confounding factors by including (for example) industry controls, which absorb any industry-driven changes in shareholder value between 2008 and 2010, such as may have been induced by debates over healthcare or financial reform," *see id.* at 687, but this seems a far-too-confident treatment of the confounding variables at play and the 2010 exogenous shocks apart from the Supreme Court's decision—many of which bear a relationship to firm value far less attenuated than the one Coates posits.

Coates's responses to Dr. Shapiro's critiques offering forth arguments more notable for their vitriol and *ad hominem* character than their candor. Coates never addresses Shapiro's core concern that his regression analyses are limited by his decision to use exclusively dummy

sion given that these expenses are so small as to be immaterial, on their face, relative to corporate budgets, *see supra* section I(a). Indeed, Bebchuck and Jackson “do not take a position as to whether corporate spending on politics is beneficial to shareholders.”<sup>54</sup>

Instead of resting their argument on the proposition that corporate spending on politics harms shareholders’ financial interests *per se*, Bebchuk and Jackson claim that the SEC should mandate disclosure of corporate political spending because “disclosure [would] deter companies from engag-

variables for corporate lobbying and PAC contributions, without any showing that his findings are robust using spending levels—a concern that is particularly pronounced given that his presentation of the data in his earlier manuscript would suggest they are not. Instead, Coates focuses his defense on referencing others’ published and unpublished studies and focusing on three issues about his study that Shapiro raised: Shapiro’s discussion of Coates’s decision to use Tobin’s Q, exclusively, as his dependent variable of interest; Shapiro’s claims about the effects of including firm-size and industry control variables in Coates’s second, published study; and Shapiro’s assessment of the range of possible results conceivably inferred from Coates’s regression analysis. *See id.* at 3–4. In each case, Coates misrepresents Shapiro’s claims.

Shapiro’s statement that “Tobin’s Q is sometimes used as a control variable but not as the primary variable of interest,” SHAPIRO & DOWSON, *supra*, at 20–22, in context, clearly is intended to refer back to his characterization of “[s]tudies trying to measure the impact of corporate political activity on firm value”—the focus of Shapiro’s literature review—not to *all* “prior research,” as Coates mischaracterizes it in his letter to the SEC. *See* Letter from Coates, *supra*, at 4. Coates’s own 2012 paper notes that only “[o]ne prior paper used Tobin’s Q to study politics,” and in that case without using Coates’s preferred industry-relative adjustment to the variable. *See* Coates, *Corporate Politics, Governance, and Value*, *supra*, at n.28 (citing Philip Hersch, Jeffrey M. Netter & Christopher Pope, *Do Campaign Contributions and Lobbying Expenditures by Firms Create ‘Political’ Capital?*, 36 ATLANTIC ECON. J. 395 (2008)). Moreover, one of the very studies Coates cites as an example using Tobin’s Q as a primary independent variable, Charles Himmelberg et al., *Understanding the determinants of managerial ownership and the link between ownership and performance*, 53 J. FIN. ECON. 353 (1999), extensively discusses theoretical concerns that parallel those discussed, more briefly, by Shapiro. *See id.* at 357–58. It is striking that Coates’s 2010 paper fails to wrestle with this issue and that Coates opts not to perform the tests of robustness embraced in the Himmelberg et al. paper.

Similarly, in context, it is clear that when Shapiro says that Coates’s results “largely disappear” when controlling for size and industry, Shapiro is comparing the results in Coates’s 2012 study *to those in his earlier 2010 study*, which lacked such controls; and Coates’s contrary claim that “the negative relationship between corporate political activity and corporate value *increases* when those controls are included,” Letter from Coates, *supra*, at 4, is deceptive in referring exclusively to *Table 6* of his published paper (his difference-in-differences test using a binary dummy variable aggregating lobbying and PAC spending), as opposed to *Table 5*, to which, in context, Shapiro is obviously referring in noting that “[t]he only correlation that remains statistically significant is a negative relationship between the decision to lobby and firm value for unregulated firms.” SHAPIRO & DOWSON, *supra*, at 21. Finally, Coates’s assertion that Shapiro’s for-a-general-audience characterization of the implications the results implied by the confidence intervals in Coates’s published study “suggests a failure to understand elementary statistics,” *see* Letter from Coates, *supra*, at 4, is quite strange: Shapiro’s characterization of Coates’s confidence interval in *Table 5*, Panel (A)(2) is absolutely, positively correct. Because Coates does not display standard errors or t-statistics in presenting his regression results, it is not wholly clear at what confidence interval the upper bound of his regression results would be zero or positive, but it most assuredly would be at some level: a 95 percent confidence interval is not a 100-percent confidence interval, as anyone who understands elementary statistics is well aware.

<sup>54</sup> Bebchuk & Jackson, *supra* note 1, at 957.

ing in political spending that is not consistent with shareholders' interests,"<sup>55</sup> because some shareholders want it,<sup>56</sup> and because the issue has "expressive significance" to shareholders.<sup>57</sup> These arguments are unavailing.

The premise underlying Bebchuk and Jackson's first argument—that even if corporate political spending on balance helps shareholders, some of it, sometimes, is surely wasteful—is doubtless correct. But it does not follow from that premise that disclosing corporate political spending would help align such spending with shareholders' financial interests. Though it is a rather dubious proposition to assume that outside shareholders would be capable of assessing corporate political and lobbying *strategy* better than management, it is at least theoretically possible that shareholders might play a useful role in policing outlier political spending *levels* if some companies spent significantly above-average sums on politics, relative to their bottom lines (and to the detriment of shareholders). But that hypothesis does not accord with observed reality, given Bebchuk and Jackson's contention that "no organization or source currently provides a means of searching for an individual or company's aggregate [political] spending at the federal and state level during a particular period."<sup>58</sup> Though Bebchuk and Jackson cite this proposition to suggest that a mandatory SEC disclosure rule is necessary, it really leads to the inverse inference: if investors thought they could improve shareholder returns by analyzing a comprehensive aggregation, synthesis, and comparison of corporations' currently disclosed political activities, surely a proxy advisory firm or other intermediary would find it valuable to perform such a service to sell to investors. Any suggestion that such an aggregation service, while not valuable with respect to currently disclosed corporate spending, would for some reason be valuable for currently undisclosed corporate contributions to 501(c)(4) or 501(c)(6) intermediaries, is far too speculative to be plausible, particularly given the theoretical disconnect between Bebchuk and Jackson's agency-cost hypothesis and non-disclosed political spending.

Even if political spending is immaterial, does not generally harm investors, and would not be useful to investors seeking to maximize their financial returns, professors Bebchuk and Jackson argue that "we should not limit our attention to the financial stakes," because political spending "carries unique expressive significance for shareholders as well."<sup>59</sup> This argument gets it exactly backwards. Precisely because political concerns are divisive among shareholders, as among the general populace, they are peculiarly ill-suited to efficient corporate governance in shareholder-owned firms. Again, shareholder-owned corporations are the dominant form of for-profit enterprise precisely because, notwithstanding agency costs, their collective-decision-

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<sup>55</sup> *Id.* at 958.

<sup>56</sup> *See id.* at 942–44.

<sup>57</sup> *Id.* at 944.

<sup>58</sup> *Id.* at 936.

<sup>59</sup> *Id.* at 943.

making costs of ownership are low. And those costs are low precisely because owners' interests are typically aligned around a single variable, share value. In public-choice terms, by aligning decision-making around a single variable, shareholder corporate governance avoids the costs more generally inherent in collective decision-making, as exemplified by Arrow's Impossibility Theorem.<sup>60</sup>

To be sure, Bebchuk and Jackson are correct that "the SEC has for some time recognized that investors may well have an interest in social issues that goes beyond those issues' direct relevance to the company's bottom line,"<sup>61</sup> by requiring companies to include on their proxy statements shareholder proposals involving social and political issues.<sup>62</sup> I am skeptical that the benefits of this requirement exceed its costs, particularly given the fact that among the 910 such proposals introduced at Fortune 250 companies from 2006 through 2012, only one received a majority of shareholders' votes over board opposition (a 2011 proposal encouraging the military-contracting company KBR to add sexual orientation to its corporate equal-opportunity, non-discrimination policy).<sup>63</sup>

But whether or not the D.C. Circuit's 1970 decision pushing the SEC to permit proposals of this type was wise,<sup>64</sup> and whether or not today's D.C. Circuit would rule similarly,<sup>65</sup> there is a world of difference between allowing shareholders to sponsor *precatory* proposals expressing a political or social view to management and adopting a *mandatory disclosure rule* forcing all publicly traded companies to modify their behavior. Even if special-interest shareholders abuse the shareholder proposal process and impose unnecessary costs on companies to the average shareholder's detriment—and I am rather convinced they do—the costs of precatory proposals relating to social or political causes are essentially limited to those incurred by corporate secretaries' offices, upper management, and boards in responding to the proposals; as well as to residual publicity damage generated by shareholders with a non-financial bone to pick with the company. Yes, green-oriented social-investing funds can generate publicity for their cause by introducing

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<sup>60</sup> See ARROW, *supra* note 49.

<sup>61</sup> See Bebchuk & Jackson, *supra* note 1, at 943.

<sup>62</sup> See JAMES R. COPLAND, YEVGENIY FEYMAN & MARGARET O'KEEFE, PROXY MONITOR 2012: A REPORT ON CORPORATE GOVERNANCE AND SHAREHOLDER ACTIVISM 11 (2012), available at [http://www.proxymonitor.org/pdf/pmr\\_04.pdf](http://www.proxymonitor.org/pdf/pmr_04.pdf) (showing that from 2006 through 2012, 38 percent of shareholder proposals on Fortune 200 companies' proxy ballots involved social or political issues, not corporate governance or executive compensation).

<sup>63</sup> See *Search Fortune 250 Shareholders Proposals*, PROXY MONITOR, <http://www.proxymonitor.org/> (sorting Social Policy proposal types, 2006–12) (last visited Apr. 8, 2013); KBR, Inc., Proposal 5 (Schedule 14A) (Apr. 4, 2011), available at [http://www.sec.gov/Archives/edgar/data/1357615/000119312511089878/ddef14a.htm#toc161840\\_18](http://www.sec.gov/Archives/edgar/data/1357615/000119312511089878/ddef14a.htm#toc161840_18).

<sup>64</sup> See *Med. Comm. for Human Rights v. SEC*, 432 F.2d 659, 682 (D.C. Cir. 1970) (remanding to the SEC for reconsideration a no-action letter that would have permitted Dow Chemical to exclude a shareholder resolution involving its sale of napalm), *aff'd* 404 U.S. 403 (1972) (affirmed for mootness, after Dow included the resolution on its proxy).

<sup>65</sup> *Cf. Business Roundtable*, 647 F.3d 1144 (D.C. Cir. 2011).

shareholder proposals at oil companies related to climate change, and the People for Ethical Treatment of Animals for its cause by introducing proposals at food-processing companies. But precisely because shareholders and customers alike are unlikely to change their behavior significantly based on such special-interest shareholders' activities—shareholders and customers of ExxonMobil are well aware that it emits carbon dioxide,<sup>66</sup> and those of Tyson Foods that it slaughters chickens—the costs imposed by social and political shareholder proposals are cabined (though real).

In contrast, mandatory rules forcing companies to disclose political spending that is not material to shareholders' financial interests but instead relevant only to special-interest shareholders' "expressive" interests—and which forced companies to reveal political spending and activity beyond that required under current regulations—would open up corporations to attacks from political activists, including in the form of consumer boycotts, designed to chill corporate speech hostile to their *political* interests. As discussed *infra* in section I(c), such attacks are not merely hypothetical.

There is little reason to believe such activities would, as Bebchuk and Jackson seem to assume, correspond to shareholders' financial interests. To the contrary, it is highly likely that consumer boycotts targeting companies over political issues would harm the average investor, either directly (by lowering sales) or indirectly (by chilling speech, in the aggregate, to the detriment of corporate profits). And in terms of the SEC's statutory mission, it would seem perverse to mandate disclosure rules accommodating the non-financial "expressive" interests of a minority of shareholders, when such rules seem highly likely to hurt the financial interests of the average shareholder.

### 3. *Special-interest shareholders' dominant role in pushing for further disclosures in this area.*

The proposition that the push for further corporate disclosure of political spending is relevant to politically rather than financially motivated shareholders is not merely theoretical. In fact, shareholder activism over corporate political spending has been dominated by labor-union pension funds, "socially responsible" investing funds, and charities with a "social justice"

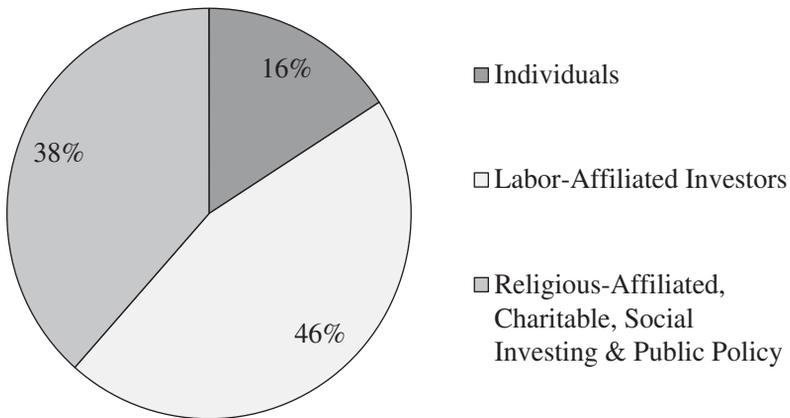
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<sup>66</sup> ExxonMobil and other companies might be adversely affected by mandatory new disclosures of climate-change-related risks, adopted in 2010 by the SEC, in a contested 3–2 vote. See Commission Guidance Regarding Disclosure Related to Climate Change, Exchange Act Release No. 34-61469, 75 Fed. Reg. 6290, 6291, 6296; John M. Broder, *S.E.C. Adds Climate Risk to Disclosure List*, N.Y. TIMES, Jan. 27, 2010, at B1. But even if the costs imposed by climate change risks *per se* would be minimal to shareholders, given reasonable stock-market discount-rate assumptions, the legislative and regulatory risks related to climate change concerns could be quite significant to many businesses. Thus, a mandatory disclosure rule related to climate change, unlike that for political spending, would seem to meet a basic materiality threshold.

mission—the very sorts of special-interest investors that concerned the D.C. Circuit in *Business Roundtable*.<sup>67</sup>

The Manhattan Institute's ProxyMonitor.org database<sup>68</sup> catalogs all shareholder proposals introduced at the 250 largest publicly traded U.S. companies by revenues, as listed by *Fortune* magazine.<sup>69</sup> Among the 195 political-spending-related shareholder proposals with identified sponsors that were introduced at these companies between 2006 and 2012, fully 46 percent were backed by the pension funds of public- or private-sector labor unions, and another 38 percent by institutional investors with an express socially responsible investing orientation or an affiliation with a religious organization, social-justice charity, or public-policy group (see Figure 1). Not a single such proposal was sponsored by an institutional investor without a social-religious-policy orientation or an affiliation with organized labor. There were 31 political-spending-related shareholder proposals sponsored by individual investors, a majority of which came from a single individual, Evelyn Davis,<sup>70</sup> who repeatedly filed proposals seeking to have companies whose shares she owned buy advertisements in major newspapers detailing their political spending.

FIGURE 1:  
SPONSORSHIP OF POLITICAL-SPENDING-RELATED SHAREHOLDER  
PROPOSALS, FORTUNE 250, 2006–12



Proposals such as Ms. Davis's are of course beyond the scope of the rulemaking advocated by Professors Bebchuk and Jackson. But the narrower subset of shareholder proposals focused exclusively on political-spending

<sup>67</sup> *Business Roundtable*, 647 F.3d at 1151–52.

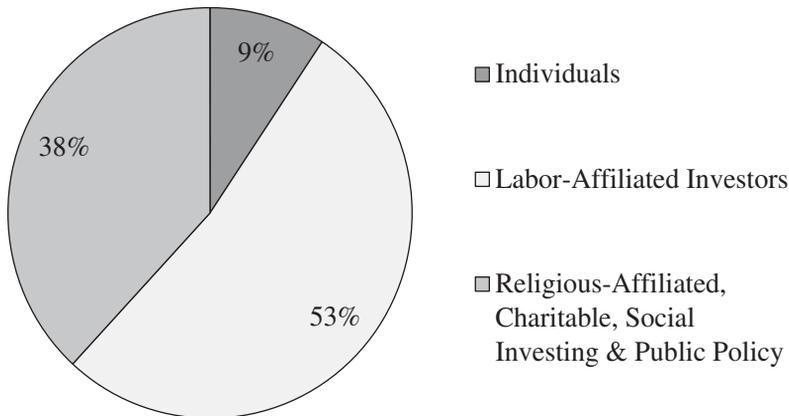
<sup>68</sup> See PROXY MONITOR, <http://www.proxymonitor.org/>.

<sup>69</sup> See *Fortune 500*, *supra* note 22.

<sup>70</sup> Ms. Davis is an eclectic shareholder who makes frequent use of the shareholder-proposal process. See COPLAND ET AL., *supra* note 62, at 9.

disclosure of the type advocated by the Center for Political Accountability (CPA)<sup>71</sup>—excluding Ms. Davis’s proposals as well as others in the broader class of political-spending-related proposals (such as those asking corporations to affirm their non-partisanship, those involving lobbying disclosure, those seeking shareholder advisory votes on corporate political spending, and those seeking to prohibit corporate political spending)—shows an even greater degree of special-interest dominance. Among the 139 such proposals with an identified sponsor that were introduced at Fortune 250 companies from 2006 through 2012, fully 53 percent were sponsored by labor-union pension funds, with another 38 percent sponsored by social-religious-policy-oriented institutional investors (see Figure 2). Only 13 such proposals were sponsored by individual investors, spread among seven shareholders.

FIGURE 2:  
SPONSORSHIP OF POLITICAL-SPENDING-DISCLOSURE  
SHAREHOLDER PROPOSALS, FORTUNE 250, 2006–12



From 2006 through 2012, nine different investors sponsored five or more shareholder proposals at Fortune 250 companies seeking political-spending disclosure along the CPA model. These included three public employee pension funds (the New York City pension funds and Comptroller’s Office,<sup>72</sup> the New York State Common Retirement Fund,<sup>73</sup> and the Firefight-

<sup>71</sup> The CPA, headed by former Democratic Congressional staffer Bruce Freed, articulates the following goals: “to encourage responsible corporate political activity, protect shareholders, and strengthen the integrity of the political process.” Center for Political Accountability, *About the CPA*, CTR. FOR POL. ACCOUNTABILITY, <http://www.politicalaccountability.net/index.php?ht=d/sp/i/870/pid/870> (last visited Feb. 3, 2013). The CPA has drafted a “model” shareholder resolution that is regularly proposed, occasionally with some modification, by investors sponsoring shareholder proposals. See *Political Disclosure and Oversight Resolution 2013*, CTR. FOR POL. ACCOUNTABILITY, <http://www.politicalaccountability.net/index.php?ht=d/sp/i/867/pid/867> (last visited Feb. 3, 2013).

<sup>72</sup> The New York City Comptroller, an elected official (currently John C. Liu), is the custodian and investment advisor for the City’s five public employee pension funds. See *Overview*

ers' Pension of Kansas City, Missouri); two private-sector union pension funds (the AFL-CIO and International Brotherhood of Teamsters); three social-investing funds (Domini Social Investments,<sup>74</sup> Green Century Capital Management,<sup>75</sup> and Trillium Asset Management);<sup>76</sup> and one charitable foundation (the Nathan Cummings Foundation)<sup>77</sup> (see Figure 3).

By their own self-definition, social-investing funds such as Domini, Green Century, and Trillium consider factors other than shareholder return and actively seek to change the behaviors of corporate management to comport with their preferred social vision. Although most pension funds are required under ERISA to maximize share value in their pension management,<sup>78</sup> both the Office of the Inspector General of the U.S. Department of Labor and the U.S. Court of Appeals for the D.C. Circuit have questioned the degree to which labor-union pension funds' activities in the proxy process conform to this mandate.<sup>79</sup> In prior research, I have shown that, con-

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*of the NYC Public Pension Funds*, N.Y. CITY COMPTROLLER, [http://www.comptroller.nyc.gov/bureaus/bam/pension\\_funds.shtml](http://www.comptroller.nyc.gov/bureaus/bam/pension_funds.shtml) (last visited Feb. 3, 2013).

<sup>73</sup> The New York State Comptroller, an elected official (currently Thomas P. DiNapoli), is the sole trustee of the New York State Common Retirement Fund. *See Fiduciary Responsibilities of the Comptroller*, OFF. OF N.Y. STATE COMPTROLLER, <http://www.osc.state.ny.us/pension/fiduciary.htm> (last visited Feb. 3, 2013).

<sup>74</sup> Domini Social Investments is "an investment firm specializing exclusively in socially responsible investing" that "manage[s] funds for individual and institutional investors who wish to integrate social and environmental standards into their investment decisions." *Welcome to Domini*, DOMINI SOCIAL INVESTMENTS, <http://www.domini.com/about-domini/index.htm> (last visited Feb. 3, 2013).

<sup>75</sup> Green Century Capital Management manages Green Century Funds, "a family of environmentally responsible mutual funds" that invests "in a broad mix of companies selected for environmental, social, and financial reasons" and is "committed to using the ownership stake in the companies held by the Green Century Funds to advocate for improved environmental performance and more sustainable business practices." About Us: Overview, GREEN CENTURY, <http://www.greencentury.com/about/> (last visited Feb. 3, 2013).

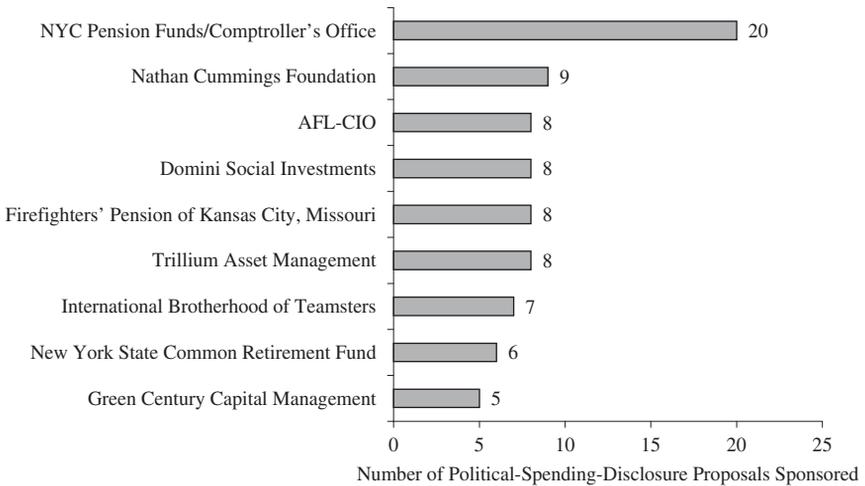
<sup>76</sup> Trillium Asset Management is "the oldest independent investment advisor devoted exclusively to sustainable and responsible investing, and the fund actively "leverages the power of stock ownership to promote social and environmental change." *About Us*, TRILLIUM ASSET MGMT., <http://www.trilliuminvest.com/socially-responsible-investment-company/> (last visited Feb. 3, 2013).

<sup>77</sup> The Nathan Cummings Foundation is a charitable foundation "committed to democratic values and social justice" that "seek[s] to build a socially and economically just society that values nature and protects the ecological balance for future generations; promotes humane health care; and fosters arts and culture that enriches communities." *About the Foundation*, NATHAN CUMMINGS FOUND., <http://www.nathancummings.org/about-the-foundation> (last visited Feb. 3, 2013).

<sup>78</sup> Under the Employee Retirement Income Security Act of 1974 (ERISA), fiduciary duties governing employee benefit plan investment portfolios require that "in voting proxies. . . the responsible fiduciary shall consider only those factors that relate to the economic value of the plan's investment and shall not subordinate the interests of the participants and beneficiaries in their retirement income to unrelated objectives." 29 C.F.R. § 2509.08-2(1) (2008).

<sup>79</sup> *See* DEPT OF LABOR, OFFICE OF THE INSPECTOR GENERAL, PROXY-VOTING MAY NOT BE SOLELY FOR THE ECONOMIC BENEFIT OF RETIREMENT PLANS, (2011), available at <http://www.oig.dol.gov/public/reports/oa/2011/09-11-001-12-121.pdf> (questioning whether labor pension funds are using "plan assets to support or pursue proxy proposals for personal, social, legislative, regulatory, or public policy agendas"); Business Roundtable, 647 F.3d 1144, 1152 (D.C. Cir. 2011) (citing proposition that "unions and state and local governments whose inter-

FIGURE 3:  
MOST FREQUENT SPONSORS OF POLITICAL-SPENDING-DISCLOSURE  
SHAREHOLDER PROPOSALS, FORTUNE 250, 2006–12



sistent with this hypothesis, labor pension funds have targeted their sponsorship of shareholder proposals disproportionately at industries and companies that “are both lightly unionized and are significant public targets of union-organizing campaigns,”<sup>80</sup> and that companies facing multiple labor-funded shareholder proposals had “had share returns that outperformed” peer groups’ but that had been involved in “public disputes with labor unions or had played an active role in the political process against organized labor’s interests.”<sup>81</sup> Moreover, state and municipal employee pension funds, which have assumed a leading role in sponsoring shareholder proposals related to political spending, are not governed by ERISA’s fiduciary voting requirements,<sup>82</sup> and the funds most active in sponsoring such proposals are entrusted wholly or partly to partisan elected officials.<sup>83</sup>

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ests in jobs may well be greater than their interest in share value, can be expected to pursue self-interested objectives rather than the goal of maximizing shareholder value”).

<sup>80</sup> COPLAND ET AL., *supra* note 62, at 16.

<sup>81</sup> *Id.* at 2, 16–17.

<sup>82</sup> See 29 U.S.C. § 1003(b)(1) (2010).

<sup>83</sup> The sole trustee of the New York State Common Retirement Fund, which holds assets in trust for the New York State & Local Retirement System, is the state’s elected comptroller. See Off. of the State Comptroller, *Fiduciary Responsibilities of the Comptroller*, <http://www.osc.state.ny.us/pension/fiduciary.htm> (last visited May 22, 2013). New York City’s elected comptroller serves as investment advisor and managing trustee of the City’s five public-employee pension funds, though oversight is spread various boards whose members tend to be political officials or union delegates; for example, the Teachers Retirement System includes the comptroller, two mayoral delegates, a delegate from the education chancellor, and three teacher delegates, and the Employees’ Retirement System includes the comptroller, the public advocate, a mayoral representative, each of the five New York City borough presidents, and three union delegates. See *Our Retirement Board*, TEACHERS’ RET. SYS. OF THE CITY OF NEW

C. *Disclosure of political spending would chill corporate political speech to shareholders' detriment.*

The public record amply demonstrates that many of the same sponsors of shareholder proposals seeking additional corporate disclosures of political spending also seek to influence corporations to disassociate from trade associations or to dissuade such groups from taking positions contrary to the special-interest sponsors' particular political preferences. For instance, in January 2011, leaders of the AFL-CIO Office of Investment, Domini Social Investments, Green Century Capital Management, the Nathan Cummings Foundation, and Trillium Asset Management all co-signed a letter sent to 35 companies serving on the board of the U.S. Chamber of Commerce urging the companies "to evaluate" their role with the trade association and objecting to the Chamber's "education and lobbying efforts to defeat legislative [sic] and regulation related to climate change, consumer protection, and financial reform."<sup>84</sup> New York City Comptroller John Liu, who manages the city's five pension funds for retired public employees, sent a similar letter to at least one company in which the funds invested.<sup>85</sup> The Center for Political Accountability, which coordinates the introduction of shareholder proposals related to the disclosure of corporate political spending, and which often holds itself out as interested solely in corporate disclosure of political spending, has both led and joined coalition letters pressuring companies to vocalize disagreement with trade association political positions.<sup>86</sup>

While such pressure tactics might be defended in theory as attempting to encourage companies to modify trade associations' behavior better to correspond to shareholders' financial interests, evidence suggests that the ultimate objective of such efforts is instead to *curtail* corporate political spending. For instance, the social investing fund Trillium Asset Management sponsored various proposals in 2011 and 2012 that sought not only to increase disclosure of political spending or lobbying policies and practices but

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YORK, <https://www.trsnyc.org/trsweb/aboutUs/ourRetirementBoard.html> (last visited May 22, 2013); *Board of Trustees*, N.Y. CITY EMPLOYEES' RET. SYS., <http://www.nycers.org/%28S%284wrsvjx1mhxv2ru45mnycd445%29%29/about/Board.aspx> (last visited May 22, 2013). Highlighting the potential for such funds to act with political as opposed to financial motives, a current candidate for New York City Comptroller, the state's former governor and attorney general Eliot Spitzer, has expressly called on elected comptrollers to use their investments to "fundamentally alter" American corporations, including by restricting corporations' power "to sway the course of legislation or regulation in Washington or any state capital." James R. Copland, *Eliot Spitzer's Great Big (Bad) Idea*, NY Post, July 26, 2013, at 29 (quoting Eliot Spitzer, "We Own Wall Street", SLATE (Dec. 21, 2011), [http://www.slate.com/articles/news\\_and\\_politics/the\\_best\\_policy/2011/12/occupy\\_wall\\_street\\_we\\_own\\_wall\\_street\\_a\\_new\\_move\\_ment\\_to\\_stop\\_corporate\\_america\\_s\\_misbehavior\\_.html](http://www.slate.com/articles/news_and_politics/the_best_policy/2011/12/occupy_wall_street_we_own_wall_street_a_new_move_ment_to_stop_corporate_america_s_misbehavior_.html)).

<sup>84</sup> Press Release, Walden Asset Mgmt., *supra* note 9.

<sup>85</sup> Press Release, N.Y. City Comptroller, *supra* note 9.

<sup>86</sup> See CPA Leads Effort to Press Companies on Climate-Change Misalignment; Company Cuts Chamber Dues, CTR. FOR POL. ACCOUNTABILITY NEWSLETTER (Nov. 2009), <http://www.politicalaccountability.net/index.php?ht=a/GetDocumentAction/i/2663> (last visited Feb. 3, 2013).

also to prohibit any corporate political participation altogether.<sup>87</sup> A 2012 strategy memorandum from the left-leaning advocacy group Media Matters for America expressed an “end goal” for “corporate transparency” efforts of “mak[ing] the case that political spending is not within the fiduciary interest of publicly traded companies and therefore should be limited.”<sup>88</sup>

Whatever the merits or demerits for the broader body politic of prohibiting or limiting corporate political participation, it would be hard to argue that burdening and reducing corporations’ ability to speak on political concerns would help shareholders improve their financial positions as shareholders.<sup>89</sup> To the contrary, as the late corporate law professor Larry Ribstein observed, in general, “diversified shareholders . . . would prefer that business views be heard.”<sup>90</sup>

Trade associations, in particular, fulfill a vital role in communicating corporate concerns to policy makers and regulators. Companies seeking to advocate for or against a given law or regulation tend to face a classic free-rider problem, given that most such rules affect not only the company in question but also a company’s competitors. A proposed rule that would change Food and Drug Administration rules in a manner that increased costs and delays in bringing new pharmaceuticals to market would affect Merck, Pfizer, and Johnson & Johnson alike. A proposed rule that increased the costs of writing insurance policies would similarly affect State Farm, Allstate, and Geico. Although each individual pharmaceutical company and insurance company would likely oppose such proposals, each company also has an individual incentive to *under-communicate* opposition (i.e., spend less) and free ride off competitors’ efforts. By collectively pre-committing to

<sup>87</sup> See PROXY MONITOR, <http://www.proxymonitor.org/> (searching for Proponent, Trillium Asset Management); compare 3M Company, Proxy Statement (Schedule 14A), at 27–28 (Mar. 23, 2011), available at <http://www.sec.gov/Archives/edgar/data/66740/000104746911002539/a2202430zdef14a.htm#ProposalFive> (CPA model proposal), with 3M Company, Proxy Statement (Schedule 14A), at 44–45 (May 8, 2012), available at <http://www.sec.gov/Archives/edgar/data/66740/000104746912003038/a2207846zdef14a.htm#ProposalSeven> (proposing “that the board of directors adopt a policy prohibiting the use of corporate funds for any political election or campaign”).

<sup>88</sup> Memorandum on file with author.

<sup>89</sup> Although professors Bebchuk and Jackson are correct that the effects of corporate political spending are disputed, see Bebchuk & Jackson, *supra* note 1, at 32, the body of research overwhelmingly shows that “corporate spending decisions on campaign contributions and lobbying efforts are generally made in a rational and strategic manner” and that “corporate political activity appears to have a generally positive effect on firm value, as reflected in excess market returns.” SHAPIRO & DOWSON, *supra* note 53, at 22.

But regardless of whether there is a positive or negative relationship between corporate political spending and firm value, at the level of the individual firm, it is almost certainly the case that *diversified* shareholders would be worse off if corporations in general were unable to advocate through intermediaries like trade associations. Indeed, even if companies were on average made worse off if they spent (or spent more) on politics, that could reflect merely the free-rider problem described above: companies exiting the political process are profiting, relative to their peers, by free-riding on other companies’ and trade associations’ efforts.

<sup>90</sup> Larry E. Ribstein, *The First Amendment and Corporate Governance* (Illinois Pub. L. Research Paper No. 10-24, 2011), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1739264](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1739264).

associations that communicate common interests, however, companies can mitigate free-rider concerns and voice common political interests at a level more properly aligned with shareholders' interests.

Trade associations and other intermediaries also play an important role in helping companies participate in the electoral process—by opposing candidates hostile to business or industry interests, or the inverse—both by mitigating free-rider problems and by lowering the prospect of offending customers who are sharply divided on political questions. The quote often attributed to a young Michael Jordan, in declining to endorse Charlotte's African-American mayor Harvey Gantt over former hard-line segregationist Jesse Helms, in the 1990 U.S. Senate campaign in the ballplayer's native North Carolina—"Republicans buy shoes, too"<sup>91</sup>—may be apocryphal;<sup>92</sup> but the sentiment is surely sound: supporting a political candidate or party risks alienating customers, at least for companies (or endorsers) selling products to individuals as opposed to other businesses. In 2010, the Minnesota-headquartered retailer Target donated \$150,000 to MN Forward, a pro-private-sector state-level political action committee,<sup>93</sup> and the company came under fire from gay-rights activists—who organized a consumer-boycott campaign—after the PAC backed the socially conservative Republican nominee for governor, Tom Emmer, who opposed same-sex marriage rights.<sup>94</sup> Little wonder, after this experience, that only one public company was a significant contributor to a major Super PAC in the 2012 federal election cycle.<sup>95</sup>

Just as political activists organized boycotts of Target for its PAC contribution, so too have they targeted corporations' trade association memberships, when such affiliations were known. In 2012, the political activist group Color of Change,<sup>96</sup> in coordination with labor-union members, organized consumer pressure against companies known to be affiliated with the American Legislative Exchange Council,<sup>97</sup> a market-oriented group with

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<sup>91</sup> See, e.g., L.Z. Granderson, *The Political Michael Jordan*, ESPN.COM (Aug. 14, 2012), [http://espn.go.com/nba/story/\\_id/8264956/michael-jordan-obama-fundraiser-22-years-harvey-gantt](http://espn.go.com/nba/story/_id/8264956/michael-jordan-obama-fundraiser-22-years-harvey-gantt).

<sup>92</sup> See Brendan Nyhan, *An Elusively Sourced Michael Jordan Quote*, BRENDAN-NYHAN.COM (Nov. 5, 2005), [http://www.brendan-nyhan.com/blog/2005/11/an\\_elusively\\_so.html](http://www.brendan-nyhan.com/blog/2005/11/an_elusively_so.html).

<sup>93</sup> See *Who We Are*, MN FORWARD, <http://www.mnforward.com/who-we-are/> (last visited Mar. 1, 2013).

<sup>94</sup> See Brian Montopoli, *Target Boycott Movement Grows Following Donation to Support "Anti-Gay" Candidate*, CBSNEWS.COM (July 28, 2010), [http://www.cbsnews.com/8301-503544\\_162-20011983-503544.html](http://www.cbsnews.com/8301-503544_162-20011983-503544.html).

<sup>95</sup> The fact that publicly traded companies opted not to contribute to Super PACs in 2012 does not lead to an inference that they are better off, in the aggregate, not participating in the electoral process at all. Indeed, as mentioned, *privately held* companies regularly contributed to Super PACs, which suggests that public companies' special sensitivity to differing shareholder preferences on this issue—i.e., high collective-decision making costs—primarily explains public companies' decision not to make disclosed Super PAC donations, particularly in the case of companies who sell primarily or exclusively to other businesses, and thus would not be subject to the type of consumer boycotts that faced Target.

<sup>96</sup> See *What Is ColorOfChange.org?*, COLOR OF CHANGE, <http://colorofchange.org/about/>.

<sup>97</sup> See *About ALEC*, ALEC, <http://www.alec.org/about-alec/>.

corporate members that drafts state-level model legislation.<sup>98</sup> At least sixteen consumer-oriented businesses—including Amazon, Coca-Cola, Kraft, Mars, McDonalds, Pepsi, and Wendy’s—left the organization.<sup>99</sup> And similarly, under previously described pressure applied by activists including the sponsors of shareholder proposals calling for increased disclosure of corporate political spending,<sup>100</sup> several prominent companies—including Apple, Exelon, and PG & E—resigned from the U.S. Chamber of Commerce or withdrew support for the organization’s political spending and lobbying efforts.<sup>101</sup> It is almost certain that full disclosure of corporations’ trade association memberships and dues would lead to more such efforts to curb corporate participation in such groups, to the financial detriment of the average diversified shareholder.<sup>102</sup>

## II. SHAREHOLDERS’ REVEALED PREFERENCES COUNSEL AGAINST RULEMAKING IN THIS AREA

Bebchuk and Jackson accurately note that the *number* of shareholder proposals relating to corporations’ political spending has been growing in recent years and that in 2012 “proposals on political spending were more common than proposals on any other topic.”<sup>103</sup> But it does not follow that, as Bebhuk and Jackson assert, the growing and significant *incidence* of such shareholder “proposals reflect[s] more than just the proposing shareholder’s interest in the subject.”<sup>104</sup>

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<sup>98</sup> See Trymaine Lee, *Amazon Drops ALEC Under Pressure From Advocacy Group*, HUFFINGTON POST (May 24, 2012), [http://www.huffingtonpost.com/2012/05/24/amazon-alec-press-ure\\_n\\_1544028.html](http://www.huffingtonpost.com/2012/05/24/amazon-alec-press-ure_n_1544028.html).

<sup>99</sup> See *id.*

<sup>100</sup> See text accompanying notes 84–86, *supra*.

<sup>101</sup> See Press Release, Walden Asset Mgmt., *supra* note 9.

<sup>102</sup> Bebhuk and Jackson argue, to the contrary, that “[t]here is no reason to expect that disclosure would undermine directors’ and executives’ ability to pursue political spending that shareholders want,” and that “disclosure [would] likely bolster insiders’ defenses against any pressure from special interests.” Bebhuk & Jackson, *supra* note 1, at 560. But in fact there *is* “reason to expect” that disclosure would undermine companies’ ability to pursue political spending. Again, apart from one small-cap company with a family control stake, *not a single public company* was a major contributor to a Super PAC that played a significant role in the 2012 electoral cycle. See text accompanying note 31, *supra*. What there is little reason to expect is that disclosure would somehow help “bolster insiders’ defenses against any pressure from special interests,” as Bebhuk and Jackson claim. Indeed, special-interest investors pressured *each corporation serving on the board* of the U.S. Chamber of Commerce to “evaluate” its role with the trade group, and induced some companies to leave the board, leave the Chamber, or make their Chamber contributions unavailable for political spending or lobbying. See Press Release, Walden Asset Mgmt., *supra* note 9.

<sup>103</sup> Bebhuk & Jackson, *supra* note 1, at 938; see also COPLAND ET AL., *supra* note 62, at 13, 19 (noting that “Fortune 200 companies have faced an average of 0.28 proposals related to political spending or lobbying in 2012, up from 0.20 proposals in 2011 and just 0.09 proposals as recently as 2008” and that “political-spending-related proposals constitute[ed] a plurality of shareholder proposals in 2012”).

<sup>104</sup> Bebhuk & Jackson, *supra* note 1, at 938.

Bebchuk and Jackson reach their conclusion deductively, by suggesting that “[b]ecause shareholder proponents focus their limited time and attention on proposals that are likely to attract substantial support, evidence about shareholder proposals also indicates the type of proposals most likely to be supported by other shareholders.”<sup>105</sup> But Bebhuk and Jackson’s premise that the sponsors of shareholder proposals are only interested in proposals “likely to attract substantial support” is a false one. As previously mentioned, 910 shareholder proposals related to social and political issues were introduced at Fortune 250 companies from 2006 through 2012—indeed, the last two years have “witnessed a slight increase in the number of social policy proposals relative to those involving corporate governance”—and yet *only one* such proposal received a majority of shareholders’ votes over board opposition.<sup>106</sup> The People for the Ethical Treatment of Animals, for instance, sponsored thirty animal-rights-related shareholder proposals at Fortune 250 companies from 2006 through 2012, notwithstanding that not a single of their proposals garnered as much as ten percent of the shareholder vote.<sup>107</sup>

Special-interest investors are willing to sponsor shareholder proposals likely (or certain) to be opposed by a majority of shareholders not only because they gain publicity for their cause, but also because they may gain a seat at the “bargaining table” with management to advance their agenda. Corporate managements sensitive to the costs associated with informing shareholders about companies’ interests on politically divisive questions, and to the potential that political controversy might cause branding damage with consumers, regularly negotiate with shareholder proponents to withdraw ballot items from corporate proxies.<sup>108</sup> Indeed, my research suggests that a significant number of shareholder proposals never make it to the proxy statement; and that proposals related to social and political issues, and those sponsored by social-political-religious investors, are more likely to be “negotiated off” proxy ballots.<sup>109</sup> Such context is useful to understanding corporations’ “voluntary disclosures” of various forms of corporate political spending that figure prominently in Bebhuk and Jackson’s article.<sup>110</sup>

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<sup>105</sup> *Id.*

<sup>106</sup> See PROXY MONITOR, <http://www.proxymonitor.org/> (sorting Social Policy proposal types, 2006–12); COPLAND ET AL., *supra* note 62, at 12.

<sup>107</sup> See PROXY MONITOR, <http://www.proxymonitor.org/> (searching for Proponent PETA, 2006–12);

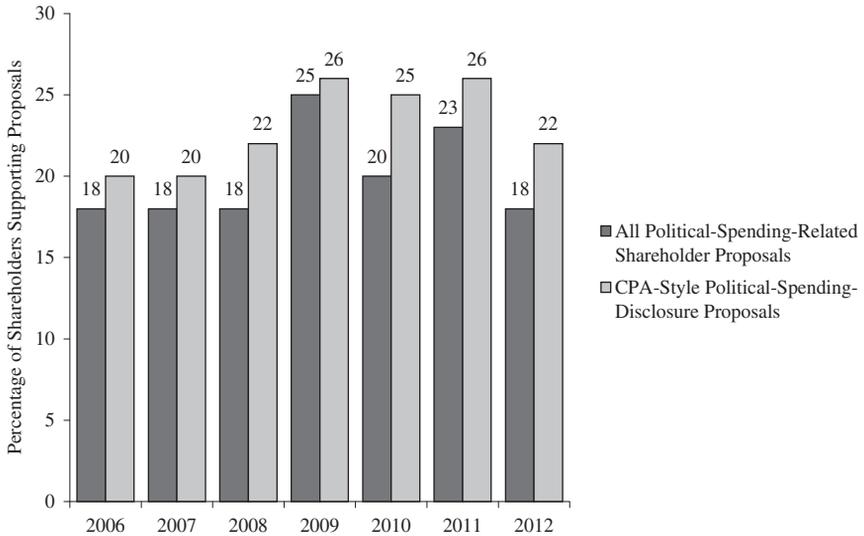
<sup>108</sup> See James R. Copland, *Proxy Monitor Winter Report 2013*, PROXY MONITOR, [http://proxymonitor.org/forms/pmr\\_05.aspx](http://proxymonitor.org/forms/pmr_05.aspx) (last visited June 10, 2013).

<sup>109</sup> See *id.*

<sup>110</sup> See Bebhuk & Jackson, *supra* note 1, at 945–49. Bebhuk and Jackson argue *both* that such voluntary disclosures evidence “significant investor demand for” political-spending disclosure, *id.* at 946, *and* that the disclosures that have been done voluntarily are inadequate to meet investors’ needs, *see id.* at 947–49. Two significant points warrant mention.

First, it is absolutely the case that *some* public companies may find it in their interests to disclose various types of political spending beyond that currently required by law. Companies are subject to different legal and regulatory risks, so different companies have different *demands* for political spending. Companies also vary significantly in the degree to which they would be subject to pressures from political activists, including consumer boycotts. Some

FIGURE 4:  
 PERCENTAGE OF SHAREHOLDERS SUPPORTING POLITICAL-  
 SPENDING-RELATED PROXY PROPOSALS,  
 FORTUNE 250, 2006–12



The actual shareholder votes held in recent years on the numerous shareholder proposals introduced on corporate political spending, including those calling for increased disclosure such as that advocated by professors Bebchuk and Jackson, shows clearly that a majority of shareholders believe that *increased disclosure of corporate political spending is not in their interests*. As shown in Figure 4, shareholder proposals calling for increased disclosure of political spending, of the sort advocated by the Center for Political Accountability and professors Bebchuk and Jackson, won the backing of

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companies sell primarily or exclusively to other businesses, whereas other companies sell directly to consumers and have high brand identities—such as those that withdrew from the American Legislative Exchange Council following political pressure from Color of Change, see text accompanying note 98.

Second, most large public companies *do not* voluntarily disclose payments to 501(c)(4) social welfare organizations or 501(c)(6) trade associations. The most recent assessment of the Center for Political Accountability (CPA)—which coordinates and supports efforts to increase corporations' political-spending disclosure, assesses corporations' performance in this area, and pressures corporations to influence trade associations to change their political postures, see text accompanying notes 71, 86, *supra*—shows that 59 percent of public companies in the S&P 200 make “no disclosure” of their payments to trade associations and 75 percent make “no disclosure” of payments to 501(c)(4) groups. See THE 2012 CPA-ZICKLIN INDEX OF CORPORATE POLITICAL ACCOUNTABILITY AND DISCLOSURE: HOW LEADING COMPANIES NAVIGATE POLITICAL SPENDING IN THE WAKE OF CITIZENS UNITED 13 (2012), available at <http://politicalaccountability.net/index.php?ht=aA/GetDocumentAction/i/6903>. Moreover, it is far from clear that the companies making some disclosures of such payments are disclosing what the CPA and other activists in this area would prefer.

only 22 percent of shareholders at the Fortune 250 companies facing such proposals in 2012, down from 26 percent in 2011.<sup>111</sup> Indeed, notwithstanding the intense pressure mounted by activists pushing for this type of disclosure, the percentage of shareholders supporting proposals on this topic last year was actually lower than that in 2009, the year before *Citizens United* was decided.<sup>112</sup> Of the 160 political-spending-disclosure shareholder proposals introduced between 2006 and 2012, not a single one received majority shareholder backing over management's opposition.<sup>113</sup>

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<sup>111</sup> See PROXY MONITOR, <http://www.proxymonitor.org/> (searching for Proposal Type Political Spending) (additional calculations on file with author) (last visited Mar. 7, 2013).

The average 22 percent support shareholders gave to political-spending disclosure in 2012 probably *overstates* informed investor support for these proposals. Econometric modeling I conducted with Manhattan Institute colleagues examining voting on shareholder proposals at Fortune 200 companies, from 2006 through 2012, shows that after controlling for various factors (including company size, industry, proposal type, proposal sponsor, and year fixed effects), a "Vote For" recommendation from the proxy advisory firm ISS is associated with a 15-percentage-point increase in shareholder votes for any given shareholder proposal. See COPLAND ET AL., *supra* note 62, at 20–23, 25–28.

It seems that many smaller mutual funds and hedge funds "effectively 'outsourc[e] their government-mandated fiduciary voting obligations" to proxy advisors, since they find performing their own voting analyses prohibitively costly. James R. Copland, *Politicized Proxy Advisors vs. Individual Investors*, WALL ST. J., Oct. 7, 2012, available at <http://www.manhattan-institute.org/html/miarticle.htm?id=8546>; see Robyn Bew & Richard Fields, *Voting Decisions at US Mutual Funds: How Investors Really Use Proxy Advisers 5* (Tapestry Networks, Inc. & Inv. Research Ctr. Inst., June 2012), available at <http://www.tapestrynetworks.com/issues/corporate-governance/upload/Voting-Decisions-at-US-Mutual-Funds-June-2012.pdf> ("In the late 1980s, the SEC and Department of Labor formally attached fiduciary obligations to voting on corporate governance matters. These actions demand that, instead of passive adherence to management's recommendations, each institutional investor vote all of its portfolio shares on every matter brought to shareholders in accordance with the standards of the proverbial prudent man." (internal quotation marks omitted)); 68 Fed. Reg. 6585 (Feb. 7, 2003) (requiring of investment advisers a "duty of care" to vote on corporate proxy ballot questions and a "duty of loyalty" to "cast the proxy votes in a manner consistent with the best interest of its client" (internal citations omitted)).

ISS, in keeping with its general tendency to support many more shareholder proposals than most shareholders themselves, see COPLAND ET AL., *supra* note 62, at 22–23 ("Because ISS's business model depends on a large, diverse set of shareholder proposals, the company has an institutional incentive to support more such proposals," and "ISS receives significant revenues from social investment vehicles and labor-union pension funds, which gives the company an incentive to favor 'socially responsible' investing proposals."), has generally supported shareholder proposals calling for increased disclosure of corporations' political spending, see *id.*, a position it formalized in its 2012 Guidelines. See INST. S'HOLDER SERVICE, 2012 U.S. PROXY VOTING CONCISE GUIDELINES 15 (2011), available at <http://www.issgovernance.com/files/2012USConciseGuidelines.pdf>.

Notably, however, the seven largest mutual fund families—Vanguard, BlackRock, State Street, Fidelity, Capital World Investors, Capital Research Global Investors, and T. Rowe Price—collectively supported *fewer than 4 percent* of proposals calling for increased disclosure of corporate political spending during last year's proxy season. See James R. Copland, *Public Citizen and Social Investors Peddling Falsehoods*, POINTOFLAW.COM (Feb. 7, 2013, 11:44 a.m.) (last visited Mar. 7, 2013) (citing Form N-PX proxy filings, available at <http://www.sec.gov/edgar/searchedgar/n-px.htm>) (aggregation on file with author).

<sup>112</sup> See PROXY MONITOR, <http://www.proxymonitor.org/> (searching for Proposal Type Political Spending) (additional calculations on file with author) (last visited Mar. 7, 2013).

<sup>113</sup> Professors Bebchuk and Jackson discount the significance of actual shareholder voting on political-spending-disclosure shareholder proposals by pointing to SEC rules mandating

## CONCLUSION

The SEC should not adopt rules mandating new corporate political-spending disclosures, which would harm investors, reduce market efficiency, and inhibit capital formation.<sup>114</sup> The low level of corporate political spending relative to corporate budgets, the thinness of agency-cost rationales for monitoring corporate managers in this area and dominance of special-interest shareholders in sponsoring shareholder proposals relating to political-spend-

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disclosure on executive compensation and matters related to climate change, neither of which received majority shareholder backing before the SEC adopted such requirements. See Bebchuk & Jackson, *supra* note 1, at 949. Whatever the merits of these SEC rules—and the climate-change requirement was adopted with some controversy by a divided 3-2 Commission, see Broder, *supra* note 66—they are clearly distinguishable from a rule mandating additional political-spending disclosures.

Executive compensation is at the core of the classic agency-cost case for management monitoring. See generally Bebchuk et al., *supra* note 40. Unlike the agency-cost hypothesis that Bebchuk and Jackson advance vis-à-vis corporate political spending, without empirical foundation, the agency costs associated with paying corporate managers are not attenuated and indirect but direct and profound: executive pay packages can serve to align managers' incentives with shareholders', or not, so investors have a clear interest in seeing the compensation packages of those with whom they are in a fiduciary relationship.

While the direct costs that climate change could pose to companies would not, on their face, seem material to shareholders—given that such costs would lie far enough in the future that their present value would make them relatively minimal if discounted to present—the *legislative and regulatory risks* related to climate change could be quite significant to many businesses, particularly but not limited to those in the energy and manufacturing sectors. Thus, unlike political spending, “climate change” meets a basic materiality threshold.

<sup>114</sup> While my analysis here has focused on whether a SEC rule mandating further disclosures of corporate political spending would hurt or harm equity investors, the central concerns raised here also apply to the SEC's “market efficiency” and “capital formation” statutory concerns. I note that recent years have seen a significant decline in the number of U.S. initial public offerings (IPOs), an increase in delistings, and a fall in the number of publicly listed companies. See, e.g., IPO TASK FORCE, REBUILDING THE IPO ON-RAMP: PUTTING EMERGING COMPANIES AND THE JOB MARKET BACK ON THE ROAD TO GROWTH 6–7 (2011), available at [http://www.sec.gov/info/smallbus/acsec/rebuilding\\_the\\_ipo\\_on-ramp.pdf](http://www.sec.gov/info/smallbus/acsec/rebuilding_the_ipo_on-ramp.pdf) (observing a decline from 791 IPOs in 1996 to 157 per year from 2001 through 2008 and a drop of over 75 percent in venture-backed emerging-growth company IPOs from the 1990s to the following decade; and noting that the U.S. raised only 15 percent of global IPO proceeds in 2010, down from 28 percent in the prior ten years); Alix Stuart, *Missing: Public Companies*, CFO.COM (Mar. 22, 2011), at <http://www.cfo.com/article.cfm/14563859> (observing a 42-percent decline in the number of companies listed on major U.S. exchanges from 1997 to 2011, and noting that “[a]bout 140 companies left the public markets in 2010 through going-private transactions”); Ted Farris, “Going Dark”—*Voluntary Delisting and Deregistration under the Securities Exchange Act of 1934: The Attractions of the “Dark Side”*, DORSEY.COM (Mar. 17, 2009), [http://www.dorsey.com/going\\_dark\\_voluntary\\_delisting\\_deregistration/](http://www.dorsey.com/going_dark_voluntary_delisting_deregistration/) (arguing the case for small companies delisting in light of regulatory burdens); James R. Copland, *The Capital Market Crackup*, CHIEF EXECUTIVE (Dec. 1, 2006), available at <http://www.manhattan-institute.org/html/miarticle.htm?id=5284> (pointing to early indicators of these trends).

Observers have placed significant emphasis on the role new regulations have played in precipitating these trends. See IPO TASK FORCE, *supra*, at 8 (pointing to “well-intentioned but ‘one-size-fits-all’ regulations” that helped drive “outcomes [that] contradict the spirit and intent of more than 75 years of U.S. securities regulation”). The extent to which new SEC rules mandating political-spending disclosure might exacerbate these trends is debatable, but the significant differences observed between the way public and private companies behaved in the 2012 elections—with the latter but not the former playing a major role in contributing to Super PACs working to influence the election's outcome—counsel caution.

ing disclosure, the real threat that disclosures would chill corporate political activity to shareholders' detriment, and shareholders' revealed preferences opposing such disclosures, all strongly argue against involving our national *securities regulators* in this area. The constitutional and policy issues surrounding corporate spending on politics are many and profound, and many of the concerns raised by activists in this area, and by professors Bebchuk and Jackson, call for careful consideration by Congress and the Supreme Court, as well as by the Internal Revenue Service and Federal Elections Commission. But the SEC—which has important and growing obligations,<sup>115</sup> and limited resources—would be well advised to leave this issue alone.

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<sup>115</sup> See generally Dodd-Frank Act § 951 (2010).

