January 4, 2013

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, Northeast
Washington, D.C. 20549

Re: File No. 4-637, Petition for rulemaking to require public companies to disclose to shareholders the use of corporate resources for political activities

Dear Ms. Murphy:

These comments are submitted on behalf of the undersigned organizations, which collectively represent the interests of a broad cross-section of America.

The above-captioned petition for rulemaking, filed by a group of law professors, urges the Commission to "initiate a rulemaking project to require disclosure of corporate political spending to public-company shareholders."[1] The petition is entirely unspecific about the scope of the rule that it seeks:

- The petition discusses "political activity"[2] and the Supreme Court's decision in *Citizens United v. FEC*, 558 U.S. 310, (2010),[3] which related to expenditures in connection with elections, but also references amounts spent on "lobbying and politics"[4]—a dramatically broader category of activity.

- The petition observes that in designing a rule "the Commission may consider whether contributions that are restricted from political use will be subject to these rules,"[5]—but if a rule supposed to target "corporate political spending" would need an exemption for sums "restricted from political use," the petition's conception of the universe of activities that would be covered by its proposal is truly breathtaking.

- The petition blithely states that the Commission will face a number of "design questions"—including "the types of political spending subject to disclosure"[6]—and suggests that the Commission has the expertise to resolve these issues in the course of the rulemaking process. In fact, of course, the Commission has no expertise whatever

[1] Petition at 2.

[2] *Id*. at 4.

[3] *Id*. at 7-8.

[4] *Id*. at 8; *see also id*. at 10 n.29.

[5] *Id*. at 10.

[6] *Id*. at 9-10.

regarding the regulation of political and lobbying expenditures, which are the subjects of complex and detailed regulation at the federal, state and local levels.

The expansive and indeterminate rule sought by the petition would be wholly unsupportable as a matter of policy, would fall far outside the Commission's legal authority, and would plainly violate the First Amendment. The rulemaking petition accordingly should be denied.

Our comments include the following critical points:

- A rule of the type urged in the petition cannot be promulgated by the Commission, because there is no rational and non-arbitrary justification for adoption of a rule requiring only public companies to disclose political and lobbying expenditures not required to be disclosed under generally-applicable laws—especially in light of the Commission's statutory obligation to apprise itself about the economic consequences of a proposed regulation and to make a rational and non-arbitrary decision in light of those consequences. A number of recent Commission regulations have been set aside by the courts for failing to satisfy this standard—the Commission should not waste precious public resources on a rulemaking exercise that is similarly doomed to failure. That is especially true given the significant cost of such a rulemaking—the Commission indicated that a recent failed rulemaking cost taxpayers *$2.5 million*[7]—as well as the significant number of Commission rulemakings mandated under the Dodd-Frank Act and the JOBS Act that have not been completed, or even commenced.
    - There is no rational basis for issuance of the type of disclosure rule advocated by the petition.
        - A rule cannot be justified on the theory—advanced by some—that corporate political and lobbying activity hurts shareholder value. Government policies can have a tremendous impact on a company's fortunes; indeed, on its very existence. The leadership of a business therefore acts in accordance with its most fundamental fiduciary obligations to the company when it seeks to engage effectively with respect to government policies that could inflict financial harm upon, or provide a financial benefit to, the company. The overwhelming majority of academic studies confirm this conclusion. The few studies advocating the counterintuitive proposition that company engagement in policy hurts shareholder value are seriously flawed; and even they acknowledge that in some circumstances corporate engagement benefits shareholders. A rulemaking therefore would be wholly inconsistent with the SEC's mandate to protect investors; in fact issuance of a rule of the type sought in the petition would likely *harm* investors.
        - The alternative justification for a rule—that a company's board and management cannot be trusted to ensure that the corporation's political

[7] Letter from Chairman Mary Schapiro to Representative Scott Garrett, dated Aug. 5, 2011, *available at* http://www.law.du.edu/documents/corporate-governance/sec-and-governance/SEC-letter%208-5-11.pdf.

and lobbying activities are actually in the corporation's (and therefore the shareholders') interest—is similarly meritless. Fundamental principles of corporate governance entrust the board with responsibility to oversee management's activities, and there is no reason why the board cannot carry out that responsibility with respect to these activities, as it does in connection with a myriad of other corporate activities that, if not properly targeted and managed, could expose the corporation to serious risk. Again, many academic studies support this conclusion, and the few academic studies claiming that political activities are somehow different are seriously flawed and provide no basis for transferring this responsibility from the board to shareholders.

- A disclosure rule would without justification impose substantial costs on public companies and their shareholders.

  - The absence of any rational justification for the rule sought by the petition is confirmed by the real purpose of the advocates of special disclosure requirements for public companies: to eliminate, or at least substantially reduce corporate political and lobbying activity by using the one-sided disclosures mandated by the rule to attack corporations that engage in the political arena. It is no coincidence that the principal proponents of shareholder resolutions advocating increased disclosure, and of this rule, are minority "special interest" shareholders—union pension funds, social investment funds, and government pension funds controlled by elected officials with policy positions hostile to those of most companies. Their goal is to use the disclosures to mount attacks on public companies—and damage shareholder value—in order to force companies to stop policy engagement that would benefit the company and increase shareholder value. The Commission should not allow its regulatory process to be hijacked for this illegitimate purpose.

- The costs of such a disclosure rule would far outweigh the non-existent benefits.

  - Given the costs of the type of rule sought by the petition—in terms of injury to shareholders by deterring actions beneficial to the corporation and the disadvantage in public debate that will result from the skewed disclosure of political and lobbying activities, and the absence of any benefit—no rule could survive the analysis of economic effects mandated by the Commission's governing statute and enforced by the courts.

- The Commission lacks the statutory authority to require these disclosures. Contrary to the petition's assertion, the Commission's focus has been on disclosure of material information—and there is no basis whatever for finding this information material, either on quantitative or qualitative grounds.

- A disclosure rule targeting only public companies would violate the First Amendment. The Supreme Court has invalidated disclosure requirements in a variety of contexts, and government measures distinguishing among speakers present serious free speech concerns. Here, where the measure singles out public companies, and does not apply to the entities that frequently oppose public companies' positions, and cannot be justified by any sufficiently weighty government interests, the constitutional violation is clear.

- Even if such a rule were legally permissible, which it is not, there are numerous additional reasons why the Commission should not institute a rulemaking proceeding.
    - Congress has long been the source of these disclosure requirements at the federal level; action by the Commission would violate this long-standing principle and would be especially unjustified in view of the fact that Congress recently considered—and declined to adopt—the very sort of disclosure requirements sought by the petition. In addition, disclosure requirements regarding political and lobbying activities have long been governed by the basic principle that they should apply even-handedly and should not be gerrymandered to favor one side of policy debates. By seeking to single out public companies for enhanced disclosure requirements without extending the same rules to those who often oppose corporations in policy debates (such as law firms, public interest entities, and unions), a Commission rule would violate this fundamental principle.
    - The petition's claim that shareholders support these uneven disclosure requirements is simply false. ***A subset of minority "special interest" shareholders*** plainly want disclosure, but that position is a product of their other interests, not their interests as shareholders—and the courts have warned the Commission in a related context that it may not accept them as representative of all shareholders. The best information about shareholder interest is the number of votes received by shareholder proposals advocating special disclosure rules. Support of these proposals averaged only 17% last year for Fortune 200 companies, the lowest level in seven years.
    - The petition is also wrong in asserting that companies are adopting these special disclosure standards voluntarily. Only a very few companies have agreed to disclose expenditures not required to be disclosed by generally applicable law.
    - Initiating a rulemaking based on the assertion of a small minority of shareholders with "special interests" other than the desire to maximize shareholder value that the board and management cannot be trusted to act in the interests of shareholders would have far-reaching negative consequences.

A. The Rule Sought By The Petition Could Not Satisfy The Basic Requirement That Regulatory Action Must Be Rational And Non-Arbitrary.

Although the legal and constitutional objections to the rule contemplated by the petition (which we discuss in detail below) by themselves require the petition's denial, the petition suffers from an even more fundamental flaw: there simply is no rational justification for the rule sought by the petition.

The legal standard is well established for determining whether a rule promulgated by the Commission satisfies the Administrative Procedure Act's requirement that agency action be invalidated when it is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law."[8] The Commission must demonstrate to a court that it

> has "examine[d] the relevant data and articulate[d] a satisfactory explanation for its action including a rational connection between the facts found and the choices made." The Commission also has a "statutory obligation to determine as best it can the economic implications of the rule."
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> Indeed, the Commission has a unique obligation to consider the effect of a new rule upon "efficiency, competition, and capital formation," 15 U.S.C. §§ 78c(f), 78w(a)(2), 80a-2(c), and its failure 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.[9]

Courts have repeatedly found rules promulgated by the Commission invalid because the Commission failed "adequately to assess the economic effects of a new rule."[10]

Here, there is no rational justification for the rule. Moreover, any reasonable assessment of the relevant costs and benefits will show that the costs that would be inflicted on corporations and shareholders would far outweigh any meager benefits that might result. Indeed, the inevitable result of such a rule would be to hobble corporations' ability to engage effectively in public policy arenas by subjecting them to a disclosure regime that does not apply to those who typically advocate opposing policy views.[11] That government mandated imbalance in advocacy, in turn, would create a substantial risk that insufficiently informed public policy makers will be led to enact laws and otherwise adopt policies that would unjustifiably inflict financial injury upon corporations and, as a result, their shareholders.

1. The Petition Fails To Identify A Single, Credible Reason Why The Additional Disclosure It Seeks Would Be Useful To Shareholders.

The reasoning of the rulemaking petition is almost entirely circular: the fact that certain shareholders have sought disclosure of political and lobbying expenditures through proxy resolutions conclusively demonstrates that the information would be sufficiently useful to all shareholders to mandate promulgation of a rule requiring its disclosure. Even the premise of this

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[8] 5 U.S.C. § 706(2)(A).

[9] *Business Roundtable & U.S. Chamber of Commerce v. SEC*, 647 F.3d 1144, 1148 (D.C. Cir. 2011) (citations omitted).

[10] *Id.*; *see also Am. Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166, 167-68 (D.C. Cir. 2010); *Chamber of Commerce v. SEC*, 412 F.3d 133, 144 (D.C. Cir. 2005).

[11] This is, of course, the goal of advocates of such a rule, as we discuss below.

argument is false—as we discuss below, there is no evidence whatever that shareholders generally are clamoring for this information, as demonstrated by the small number of votes that these proxy resolutions receive. And the proxy resolutions themselves hardly provide credible evidence, because they have been filed by a small but extremely vocal minority of shareholders that take positions on numerous public policy issues directly opposite from those of most public companies.

More fundamentally, shareholder interest, which can easily be manufactured in this manner, cannot be the sole test for whether the Commission should promulgate a disclosure rule. The Commission's obligation to undertake an independent assessment of the costs and benefits of a proposed rule, as well as its obligation not to act arbitrarily, require that the Commission find that the rule will provide real benefits to shareholders at large that outweigh the rule's adverse economic effects.

To the extent any such justifications can be discerned in the petition, they fall far short of meeting this exacting and rigorous standard.

a) A Rulemaking Cannot Be Justified On The Theory That Political Activity Harms Shareholder Value—The Evidence Plainly Shows That Corporate Political Activity Enhances Shareholder Value.

The petition states: "Members of our group differ in their views on the extent to which, even with perfect information, the existing procedures of corporate democracy will ensure that corporate political activity is aligned with shareholder interests."[12] This appears to be a carefully disguised reference to the argument advanced by many proponents of mandatory disclosure by public companies—that engaging in political activity harms shareholder value, and that disclosure is required to enable shareholders to pressure companies to stop this activity.

This contention is contrary to basic common sense as well as all of the available credible evidence.

Government action (and inaction) can and does have a significant impact—both positive and negative—on the value of every business in America. "Corporations are created by statutes. Governments, through statutes, regulate the business affairs of corporations in ways that can affect the strategy and economic success of the venture."[13]

"In the highly-regulated environment in which most corporations compete, participating in the regulatory process may be necessary to franchise protection. One needs only to consider the health care or financial reform legislation of 2010 for examples of government programs with far-reaching ramifications for business. Thus, the reality for many corporations is that

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[12] Petition at 8.

[13] Roger Coffin, *A Responsibility To Speak: Citizens United, Corporate Governance and Managing Risks*, 8 Hastings Bus. L.J., 103, 107 (2011), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id-=1766583&download=yes.

government action may have a significant effect on firm value. And, of course, to participate in the regulatory process involves participating in political discourse."[14]

Economy-wide regulations—general tax rules, labor laws, and import and export regulations, for example—also can have a significant impact on the operation and profitability of a business.

In view of the direct and very substantial effect upon business of numerous types of government action, it is not surprising that businesses of all stripes participate in the political and policy-making processes. They do so by lobbying government officials, by purchasing advertisements relating to government policy issues, by encouraging employees to make their views known to government officials, by encouraging employees to make political contributions—either directly or through a company-affiliated political action committee, and by making political contributions and expenditures themselves (where permitted by law). Many companies also choose not to engage in these activities directly but rather do so through trade associations and other membership organizations.

As a report issued by a committee appointed by the Conference Board observes,

> Public policy decisions can have a profound effect on a corporation—from the board room to the bottom line. Legislative proposals, laws, government regulations, taxes, trade agreements or sanctions, and a host of other policy measures can affect how corporations operate at home and abroad, and may have a significant impact on their business performance. Those policies, in turn, affect the company's shareholders, employees and customers as well as nearby communities and other stakeholders. As a result many corporations consider participation in the political process, and the opportunity to help shape public policy, a necessary part of their responsibility to shareholders: to strengthen and grow their business.
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> The industry and countries in which a company operates can greatly affect whether it chooses to actively engage in the political process and, if so, in what capacity. But one thing is clear: a growing number of corporations, many for the first time, now see engaging with policymakers at all levels of government as an increasingly important part of their business responsibility and strategy.[15]

Corporations are not at all unique in recognizing the need to engage in the political and policy-making processes in order to protect their interests. Labor unions devote considerable resources to both lobbying and political expenditures. For example, political action committee

[14] *Id*. at 2.

[15] Conference Board, *Corporate Political Spending*, at 6 (2011), *available at* https://www.conference-board.org-/retrievefile.cfm?filename=Committee-Report---Advance-Copy1.pdf&type=subsite.

("PAC") and individual contributions from unions for the 2012 elections totaled over $100 million.[16] And unions were the largest donors to "527" groups during the 2012 election cycle: eight of the ten largest donors were unions, and their contributions amounted to $20.6 million.[17]

Given this virtually universal recognition of the importance of participating in the political and policy-making processes because of the government's huge impact on the fortunes of participants in the economy, and the universal engagement in that process by businesses and labor unions (the two groups that at a high level encompass most, if not all, participants in the economy), the basic premise on which the proposal rests—that making political expenditures by itself in some way negatively affects a business's value—is plainly wrong. "[T]he regulatory environment in which corporations must compete is complex, costly and burdensome. Armed with the right to speak, and to possibly influence the political environment from which regulations flow, corporations have a responsibility to consider political speech as a legitimate means to advance their economic goals."[18]

It therefore is not surprising that a recent comprehensive study of the economic literature in this area by distinguished economist (and former Clinton Administration official) Robert J. Shapiro found that "[e]xtensive analysis and evidence . . . support the view that corporate participation in the political process yields generally positive returns to firms and their shareholders" and that "[c]orporate political activity appears to have a generally positive effect on firm value, as reflected in excess market returns."[19]

Dr. Shapiro's review of dozens of academic studies concluded:

- "The dominant academic view for the last 20 years is that companies undertake political activity to secure advantages for themselves, based on a combination of opportunity and necessity. Their incentives to do so are clear, given that modern governments influence national economies in ways that affect the sales and returns of particular industries and companies."[20]

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[16] Data compiled by The Center for Responsive Politics, *available at* http://www.opensecrets.org/pacs/sector.php?txt=P01&cycle=2012, and http://www.opensecrets.org/overview/topcontribs.php.

[17] Data compiled by The Center for Responsive Politics, *available at* http://www.opensecrets.org/527s/527contribs.php0.

[18] Coffin, *supra*, at 165.

[19] Robert J. Shapiro & Douglas Dowson, *Corporate Political Spending: Why the New Critics are Wrong*, at 17, 22 (June 2012), *available at* http://www.manhattan-institute.org/html/lpr_15.htm.

[20] *Id*. at Executive Summary; *see also id*. at 4 ("countless large regulatory decisions have large economic effects for particular companies and industries. These decisions range from the application of a tariff or quota on certain imported goods, the sale or award of spectrum, and the application of reserve requirements to new financial products, to bailouts for certain companies deemed 'too big to fail' and approval of certain alternative energy products for the renewable fuel standard program" and "[t]he powers wielded by lawmakers and other public officials to spend, tax, regulate, and otherwise constrain or stimulate certain economic activities create powerful incentives for firms and industries to compete for

- "For publicly traded firms, the benefits of lobbying have been reported in stronger financial performance and stronger stock-market returns. Moreover, firms that lobby intensively tend to outperform their benchmarks to larger degrees. While the estimated benefits of lobbying vary from study to study, and lobbying in specific cases may not produce benefits, the literature contains no instance in which lobbying is associated with lower returns for firms and their shareholders."[21]

- "Case studies show that companies that make PAC contributions, conduct lobbying campaigns, and establish political connections sometimes win and sometimes do not. However, there are no case studies showing that industries or firms are worse off than they would have been, had they never become involved at all." [22]

Those who argue the contrary position rely principally on three studies.[23] But, as Dr. Shapiro points out, "close examination of these studies shows that their reasoning and findings do not actually challenge, much less refute, the academic consensus that corporate political activity benefits shareholders or, at a minimum, does not harm them."[24]

First, although the Aggarwal *et al*. study recognizes the various categories of political activity by companies or their employees, its correlation analysis is based only on a very small subset—"soft money" contributions and donations to 527 groups, types of expenditures that the study itself recognizes were made only by 11.27% of all publicly-traded companies.[25] That is an extremely small sample of companies and an extremely small subset of company-related political activity. Such a gerrymandered definition obviously could have a very significant impact on the study's outcome.

The study also asserts arbitrarily that the impact of political activity on a company's value should be assessed based on the change in market value during the one-year beginning on the day after the election to which the political contribution related.[26] In fact, of course, the legislative and regulatory processes take longer to reach decisions than the ten months allowed under that approach—most significant statutes are considered over a period of several years, and most regulatory actions take just as long.

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access to the political system, in order to influence the decision-making process in ways that could benefit their interests").

[21] *Id*. at 14.

[22] *Id*. at 22.

[23] Rajesh K. Aggarwal, Felix Meschke, and Tracy Wang, *Corporate Political Contributions: Investment or Agency?* (Apr. 2012), *available at* http://ssrn.com/abstract=972670; John C. Coates IV, *Corporate Governance and Corporate Political Activity: What Effect Will* Citizens United *Have on Shareholder Wealth?* (Sept. 2010), *available at* http://ssrn.com/abstract=1680861 ("Coates I"); John C. Coates IV, *Corporate Politics, Governance, and Value Before and After* Citizens United (2012), *available at* http://ssrn.com/abstract=2172638.

[24] Shapiro & Dowson, *supra*, at 17.

[25] Aggarwal, *supra*, at 3.

[26] *Id.* at 6.

If a product development cycle, from initial research and development investment to public announcement of a new product, were three years, no one would say that the value produced by the initial investment should be assessed on the basis of the change in the company's market value after 12 months. But that is the bizarre approach taken by the Aggarwal *et al*. study. The study accordingly cannot support any valid conclusion regarding the relationship between political activity and shareholder value.

In addition, Dr. Shapiro points out that

> Aggarwal and his associates virtually concede that they have not proved their case. The study yields two main observations. First, they find a positive correlation between certain features that they consider evidence of poor governance—large boards of directors, CEOs who also serve as chairmen of their boards of directors, and low ownership by institutional investors—and soft-money contributions and donations to 527 entities. Second, they observe that firms that made such contributions and donations underperform the market. Those observations, however, do not tell us how political donations influence firm performance. How much of this underperformance can be attributed to the elements of weak corporate governance that they use, independent of any political activity? Do firms that already perform poorly choose to allocate more corporate funds to political donations? If that is the case, their poor performance may be wholly unrelated to governance issues or political donations. Finally, how much of this poor performance, if any, can be attributed to its political donations? The authors cannot answer these questions. Further, they fail to identify any mechanism by which unregulated corporate campaign spending could damage firm performance.[27]

Second, the 2010 Coates study was based on a similarly narrow definition of corporate political activity. The author defined the relevant political contributions to include only contributions by PACs, thereby disregarding entirely all of the other types of contributions and expenditures that corporations may make (or encourage employees to make), including donations by employees to individual candidates, "soft money" donations to the national parties, and donations to tax exempt organizations formed under Section 527 of the Internal Revenue Code ("527 groups").[28] Furthermore, many companies do not sponsor PACs and instead ask employees to make political contributions to trade association PACs. And even companies that do sponsor PACs may ask employees to make such contributions instead of or in addition to contributing to the company PAC.

The 2010 Coates study includes lobbying in determining the level of a corporation's political activity, but confines lobbying activity to only *reported* lobbying expenses. The

[27] Shapiro & Dowson, *supra*, at 19.

[28] Coates I, *supra*, at 11.

challenge with that definition, as the author acknowledges, is twofold. An individual need register as a lobbyist only if the individual spends more than 20% of his or her time lobbying.[29] And companies are not required to disclose a broad range of "activities that are essentially political in nature, and [that] would be identified as 'lobbying' in ordinary speech."[30] While companies do not have to report these types of activities as lobbying expenditures under current law, there are still potentially thousands of individuals who engage in activity to influence opinion for corporations but who are not legally required to be registered as lobbyists and whose activities are ignored in Coates' analysis.

Given these restrictive definitions, it is not surprising that the 2010 Coates study concluded that only 70% of the corporations comprising the S&P 500 made political donations and 71% engaged in lobbying.[31] Accurate definitions would have likely yielded numbers approaching 100% in both categories, and would have provided a more accurate picture of the amount of political and policy-making activity engaged in by the companies. The claimed correlation between political activity and decline in market value is thus based on inaccurate measures. It may turn out that the companies engaging in more political activity actually increased in market value, when all of their engagement is considered.[32]

In addition, Dr. Shapiro points out in detail the numerous "inconsistencies and technical problems" with Coates' analysis.[33] He concludes that these defects "would be sufficient basis for any study's rejection by any peer-reviewed journal" and "may explain why Coates's 2010 results so thoroughly contradict the rest of the literature on the subject."[34]

Third, as Dr. Shapiro explains, the 2012 Coates study "concedes that the political activities of regulated industries and industries with large sales to government—for example, financial services, telecommunications, and defense—enhance the returns of their shareholders."[35] Although Coates tries to maintain his prior position with respect to other companies, when he applies his improved statistical approach, "*his correlations largely disappear*. The only correlation that remains statistically significant is a negative relationship between the decision to lobby and firm value for unregulated firms. Even in that case, the coefficient's 95 percent confidence interval reaches a value of –0.01, which means that the actual effect could very well be zero."[36]

Finally, because all three studies rely solely on correlations without providing any real-world evidence demonstrating a causal connection between political activity and market value,

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[29] 2 U.S.C. § 1602(a)(10); *see also* Coates I, *supra*, at 7

[30] Coates I, *supra*, at 7.

[31] *Id.* at 11.

[32] The Aggarwal *et al*. study does not include lobbying in delineating a company's political activity.

[33] Shapiro & Dowson, *supra*, at 20.

[34] *Id*. at 21.

[35] *Id*.

[36] *Id*.

there is no reason to credit the authors' assertion that political expenditures have an adverse effect on shareholder value. Assuming that "correlation implies causation . . . is a logical error."[37] Indeed, even if one were to "assume that the presence of correlation between two variables implies the presence of causation, the correlation says nothing about the direction of causation, and furthermore, correlation can be explained by both variables being caused by some third variable."[38] For this reason, both Coates and Aggarwal *et al*. must—and do concede—that their analyses do not prove that corporate political activity diminishes shareholder value.[39] As Professor Lawrence Ribstein observed with respect to the Coates 2010 study, "the negative correlation . . . may be because firms hurt most by government regulation must engage in political activity."[40] Indeed, another recent study reached a conclusion different from that of the Coates and Aggarwal *et al.* studies. It found "a positive and significant relationship" between corporate political contributions and future firm profitability.[41]

Separately, Professor Roger Coffin examined a variety of relevant empirical data and found the following based on statistical analyses of that data:

- "[i]f public firms engage in corporate political speech, their abnormal returns are *not* significantly lower than the broad market. Abnormal returns are in fact significantly *greater* than the broad market at some dates examined";[42]

- "the stock prices of those companies which publicly declared that they would not use corporate treasury funds in political speech did not fare better than those that did not"—rebutting the notion that declining to engage in political activity is correlated with increased shareholder value;[43] and

- "[a]bnormal index returns of industries more likely to engage in corporate political speech are *not* lower than broad market indices. Abnormal index returns of industries less likely to engage in corporate political speech are *not* greater than broad market indices. Thus, abnormal index returns for industries involved in pending government regulation,

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[37] Eric Neufeld & Sonje Kristtorn, *Does non-correlation imply non-causation?*, 46 Int'l J. of Approximate Reasoning 257, 269 (2007).

[38] *Id.*

[39] Coates I, *supra*, at 16; Aggarwal, *supra*, at 9, 19.

[40] Larry E. Ribstein, *The First Amendment and Corporate Governance*, 27 Ga. St. U.L. Rev. 1019, 1035 (2011).

[41] Michael J. Cooper *et al.*, *Corporate Political Contributions and Stock Returns*, 65 J. of Fin. 687, 715 (Apr. 2010). Using political contribution data for a 25-year period, the study measured political contribution practices based on the number of candidates supported by a firm's political action committee. *Id*. at 688.

[42] Coffin, *supra*, at 150 (emphasis added).

[43] *Id*. at 134-35.

and therefore more likely to engage in corporate political speech, are not lower than those of industries not involved in pending government regulation."[44]

Moreover, the Economist recently reported that "[a]n index based on the amount of lobbying that American firms do has outperformed the broader market since its creation in 2008; data going back to 1998 show that it has done better over the longer term, too."[45] The index of 50 firms has "outperformed the S&P 500 by 11% a year since 2002."[46] That too undermines the Coates studies' assertions to the extent it relies on lobbying activity as part of its model.

The overwhelming weight of the statistical analyses confirms what is obvious based on public behavior: engaging in political activity is an essential element of good stewardship. The Commission plainly cannot justify a rule on a determination that political and lobbying activity hurts shareholder value.

b) A Rulemaking Cannot Be Justified On The Ground That A Company's Board And Management Are Unable To Manage Any Potential Risk Associated With Political Activity.

The petition appears to advance a second argument—that management and the board of directors cannot be trusted to ensure that political and lobbying activity undertaken by the corporation will in fact be directed in a manner designed to enhance shareholder value and will not expose the business to unacceptable risk. The petition states, "[a]bsent disclosure, shareholders are unable to hold directors and executives accountable when they spend corporate funds on politics in a way that departs from shareholder interests."[47]

But the petition does not even attempt to explain why these decisions are different from the myriad other sensitive areas of corporate activity in which internal risk management procedures implemented by management and overseen by the board are sufficient to protect the company's (and therefore shareholders') interests. That is because there is no such difference—as Dr. Shapiro's analysis of the relevant economic literature concluded, the studies confirm that "corporate spending decisions on campaign contributions and lobbying efforts are generally made in a rational and strategic manner."[48]

Basic corporate governance principles assign distinct roles to management, the board of directors, and shareholders. "Decisions made in the ordinary course of business are generally within the purview of the management as overseen by the board of directors. Shareholders . . .

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[44] *Id*. at 150 (emphasis added).

[45] *Money and Politics – ask what your country can do for you*, The Economist (Oct. 1, 2011), *available at* http://www.economist.com/node/21531014.

[46] *Id*.

[47] Petition at 8.

[48] Shapiro & Dowson, *supra*, at 22..

have no direct role, either in a pre-approval or an *ex post facto* review context, in the decision-making process."[49] Thus,

> [t]he rationale underlying the business judgment rule includes that by shielding decision making from undue judicial review, the directors, as opposed to the shareholders, manage the corporation. Centralized decision-making, without unwarranted interference by shareholders preserves the corporate structure of a board elected by shareholders for the purpose of overseeing management. In fact, it has been stated that the business judgment rule, as a lynch pin of the corporate governance structure itself, "ultimately serves the more important function of protecting the stockholders from themselves."[50]

Moreover,

> compositional changes in the boards of directors of public companies have increased the independence of the board from the CEO and management, and have facilitated the ability of a board to act as an effective monitor on behalf [of] shareholders. Beginning with Sarbanes-Oxley and audit committees, the listing standards of the securities exchanges, and Dodd-Frank mandates for the independence of the compensation committee, the number of inside directors on public company boards is shrinking. The independence of directors from management, together with the proper incentives and alignment of interests with shareholders through director equity ownership, is a hallmark of sound corporate governance.[51]

Directors and boards today thus have a unprecedented degree of independence, mandated by law and regulation.[52] There simply is no reason to believe that corporate political activity is exempt from searching scrutiny by directors.

Indeed, the relevant evidence indicates that corporate political and lobbying expenditures, just like the expenditures by individuals and other entities, are focused on electing individuals whose views are consistent with the corporation's interests and on advocating public policies that accord with the corporation's interest. Studies of corporate PAC contributions indicate "that

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[49] Coffin, *supra*, at 126 (citing Del. Code. Ann. tit. 8, § 141(a) ("The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors . . . .").

[50] *Id.* at 129 (footnote omitted) (quoting Michael P. Dooley & E. Norman Veasey, *The Role of the Board in Derivative Litigation: Delaware Law and the Current ALI Proposals Compared*, 44 Bus. Law. 503, 522 (1989)).

[51] *Id.* at 163 (footnotes omitted).

[52] *Id*. at 107-08.

corporate PACs strategically target their congressional campaign contributions, generally directing them to those members who they expect will be most likely to pursue and deliver on legislative provisions consistent with the corporation's interests. . . . [T]here are no case studies showing that corporations that provide PAC contributions were *worse* off for having been involved."[53]

A few studies have claimed that corporate political activity supposedly presents an "agency" problem because "at least at a large number of public companies, managers cannot be trusted with other people's money" and "faithless managers divert shareholder wealth for their own ends, destroy corporate wealth, and reduce public welfare."[54]

There is no empirical support whatsoever for the assertion that "managers cannot be trusted" at "a large number of public companies." As Professor Coffin points out, "[t]o the degree that *Citizens United* has the potential to introduce an agency problem that diminishes firm value," such an effect would be apparent in the data. The "empirical results [of Professor Coffin's study] showing no harm to shareholders post-*Citizens United*, is solid even in the face of this problem."[55]

Any "agency" problem that might possibly exist with respect to political activity is no different than the agency issues that could arise—and would be more likely to arise—in a myriad of other areas. Here are just a few examples:

- Has a CEO selected a city in which to locate the corporate headquarters—or locations for factories or other offices—based on the best interests of the company or his or her own preferences?
- Has a CEO decided to create a new product line based on the best interests of the company or a desire to inflate his or her own prestige?
- Has a CEO adopted labor or employee relations practices that are in the company's best interests or reflective of his or her personal beliefs?
- Has a CEO adopted environmental practices that are in the company's best interests or reflective of his or her personal beliefs?

The constraints that protect shareholders against management action not in the best interest of the corporation in all of these contexts also protect against political spending that is not in the interests of the corporation.

[53] Shapiro & Dowson, *supra*, at 8-9.

[54] Coates I, *supra*, at 2.

[55] Coffin, *supra*, at 107.

Indeed, board members today directly oversee a variety of risk management practices and policies—political and reputational risk fall squarely within that responsibility.[56] "[T]he actors best suited to make the determination of what speech is appropriate for the corporation to make are the same actors charged with the overall job of wealth building": management, under the general supervision of the board.[57] There simply is no justification for imposing special standards in this area at all, and certainly not in the absence of any evidence whatever that there is a unique problem to be addressed.

As Professor Coffin explained, "[i]f existing duties of care, loyalty and its by-product good faith are not sufficient to prevent a director from ignoring his or her fiduciary responsibilities to the corporation and its shareholders in the political speech context, then we cannot rely on those duties to protect corporate and shareholder interests in any of the other myriad situations in which public companies act. Were this to be the case, the corporate form would be unworkable, inefficient and dysfunctional."[58]

The petition disregards these fundamental corporate governance realities. It asserts that detailed disclosure of corporate decisions is necessary to provide "investors [with] the information they need to assess and respond to" those decisions.[59]

But it fails to provide any explanation—let alone any evidence—of why shareholder oversight is either appropriate or necessary in this context, when it plainly is not appropriate with respect to the myriad other corporate decisions discussed above. On the petition's theory, Apple shareholders should have received detailed information on the company's research and development activities leading to the iPhone and iPad; otherwise, how could they be sure that management and the board were investing research and development funds in the best interests of shareholders? The argument would necessitate disclosure to shareholders of the information relevant to every corporate decision.

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[56] *Id*. at 132-33, 164-65. Professor Ribstein states: "[M]arkets operate fairly well to constrain managers' use of shareholders' money, including on corporate speech." Ribstein, *supra*, at 1033. These "agency costs" include "not only the costs of agency cheating but also the costs of monitoring by principals and bonding by agents to minimize this cheating. There are many potential mechanisms for controlling these costs, including independent directors, shareholder voting mechanisms, transferable shares, fiduciary duties and remedies, disclosure rules, and gatekeeper responsibilities." *Id*. (footnotes omitted). "Shareholders might have to worry about lucrative compensation packages or costly empire-building acquisitions, but executives would be unlikely to risk board dismissal for potentially embarrassing or costly political speech whose potential benefits are long-range and speculative. Market discipline helps explain why fiduciary duties focus on clearly selfish conduct and leave other types of agent misbehavior to the light touch of the business judgment rule." *Id*. at 1034-35.

[57] Coffin, *supra*, at 162.

[58] *Id*. at 158. "[S]hareholders are not in a position to know the non-public details of the corporation and have rightly delegated the daily affairs of the corporation to management, as overseen by a board of directors. For that reason, the actors best suited to make the determination of what speech is appropriate for the corporation to make are the same actors charged with the overall job of wealth building—management and the board." *Id*. at 162. Board members "have the necessary objectivity and the incentive to exercise that independence to oversee the political speech of the corporation." *Id*. at 165.

[59] Petition at 8.

It is the board, not shareholders, that is responsible for determining whether management is failing to act in the best interests of the company. Indeed, substituting shareholder oversight for board oversight creates the very real risk that shareholders will react based on their personal political interests, not the corporation's interest.[60]

2. A Rulemaking Would Impose Substantial Costs On Corporations And Investors.

The petition frames its proposal as a neutral effort seeking additional disclosure of corporate expenditures. In reality, however, the inevitable—and intended—result of these

[60] Some proponents of these proposals have argued in other contexts that deciding to engage in political activity differs from other forms of corporate decision-making because shareholders should be permitted to disassociate themselves from political activities with which they disagree. But the corporation's actions are not the actions of the shareholders in any other context, and there is no basis for adopting a different rule with respect to political speech. A corporation presents itself to the public through "its advertising and branding, labor practices, employee relations," among other things.

> Any and all of these activities may conflict with, offend or run contra to the personal beliefs and/or preferences of the shareholders. None of these activities are illegal in and of themselves, and all are generally undertaken by the corporate form in good faith and with the corporate purpose in mind. In this sense a shareholder's political beliefs are as unimportant to the primary goal of a corporation as are the shareholder's tastes in other personal items, such as art, movies or clothing. To believe otherwise opens the lid on the shareholder and stakeholder derivative interests, none of which should assume, on balance, primacy over the First Amendment right of the corporation.

Coffin, *supra,* at 105. A shareholder in a corporation is no more associated with the corporation's political speech than a shareholder in the New York Times or Washington Post is associated with the views expressed in those publications' editorials.

Furthermore, Professor Ribstein observed that "it is more reasonable to hypothesize based on the nature of the shareholders' investments that most do not identify with the speech of corporations they invest in. Individual shareholders generally invest in publicly held corporations through diversified portfolios and through other institutions such as mutual or pension funds. These shareholders may have little idea which stocks they are holding and are concerned only with the total risk and return of their portfolio." Ribstein, *supra*, at 1029.

The personal beliefs of shareholders—who voluntarily associate themselves with the corporation—are therefore irrelevant in determining the propriety of the corporation's actions "so long as the corporation is pursuing its legitimate [economic] goals in good faith." Coffin, *supra,* at 166.

It is important to note that the position of shareholders, who voluntarily decide whether to purchase shares in a particular company, is completely different from the position of individuals who are required to join a union as a condition of taking a job. Even those who try to make this analogy recognize that the situation of a union member "can be distinguished on the ground that workers may be required to join unions and therefore to associate with their political positions." Ribstein, *supra*, at 1032. In addition, "a worker's association with his union almost certainly is closer than that between a corporation and its diversified investors." *Id*. Shareholders who disapprove of a corporation's political activities can disassociate themselves from those acts by selling their shares and investing their funds elsewhere.

unique disclosure requirements will be to impose a new, very significant obstacle to political activity by public companies:

- Companies will have to face public disclosure of their activities without equivalent disclosure by those supporting a contrary view in political debates (for example: trial lawyers, "public interest" groups, unions, etc.)—a distinction that may lead companies to decide not to participate. Indeed, companies' opponents will be able to exploit the different disclosure requirements, arguing that corporations spent "millions" for some purpose, while concealing their own spending of an equivalent amount, thereby deceiving the public regarding their own activities and illegitimately placing public companies in a poor public light.

- More importantly, corporations that disclose political activity will quickly be attacked by opponents of their political views. A recent *Wall Street Journal* editorial explained:

> Disclosure is pitched as an apple-pie corporate virtue, but a basic question is whom it is supposed to benefit. None of the spending that these outfits want disclosed is material to the company's bottom line—which is what shareholders really need to know. Companies must already follow the campaign-finance and lobbying laws that provide significant political transparency.
>
> . . . . The data dump serves no one save the political activists who can use it as a PR club to harass companies until they stop donating.
>
> That harassment strategy was explicitly laid out in the "corporate transparency" section of a document describing its agenda for 2010-2102 from the left-wing agitprop outfit, Media Matters. "Media Matters Action Network will create a multitude of public relations challenges for corporations that make the decision to meddle in political campaigns," says the document. The data from corporate disclosure "may also be used to launch shareholder resolution campaigns to prevent corporations from making these types of expenditures."[61]

Some companies will conclude that the need to protect their brands against relentless, albeit unjustified, attacks necessitates a reduction in or elimination of political activities, even if that could lead to government policy actions harmful to shareholder value.

It certainly is no coincidence that all of the shareholders that have proposed resolutions seeking to impose disclosure requirements of the type sought by the petition—union pension funds, liberal-oriented social investment funds, and government pension funds controlled by elected officials with policy positions hostile to those of most companies—take positions on

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[61] *The Corporate Disclosure Assault*, WALL ST. J., Mar. 20, 2012; *see also* Brad Smith, *Another Union Attack on Corporate Speech*, WALL ST. J., Nov. 10, 2011, at A21.

numerous public policy issues directly opposite from the public companies. The reason these groups are seeking disclosure is that it will facilitate their efforts to stop companies from engaging in political activity, and thereby eliminating a key opponent from policy debates.

The disclosure mandated by any rule adopted by the Commission will be used to mount attacks against public companies—and damage shareholder value—in order to force the companies to stop activity that is being pursued to promote government policy that will benefit the company and increase shareholder value. Stopping corporate activity simply because it is not in the political interest of certain groups does not provide any benefit to shareholders as a whole. Rather, it significantly *injures* shareholders by preventing companies from engaging in activities beneficial to the corporation's activities that enhance shareholder value. And even if corporations' are not dissuaded by these attacks, they potentially will suffer brand damage that will diminish shareholder value. The Commission should not initiate a rulemaking procedure at the importunity of corporations' political opponents that is designed to provide those opponents with information to stop those very corporations from engaging in policy debates in order to promote shareholder value.

Finally, the petition quotes from the Supreme Court's *Citizens United* decision,[62] implying that the ruling has somehow justified adoption of these disclosure rules. But the full passage containing those quotes makes clear that the Supreme Court was referring to a disclosure rule ***applicable to independent expenditures generally***, not a rule targeting only the expenditures of public corporations.[63]

[62] Petition at 7.

[63] Here is the full quotation (only citations are omitted; emphasis added):

> Shareholder objections raised through the procedures of corporate democracy, can be more effective today because modern technology makes disclosures rapid and informative. A campaign finance system that pairs corporate independent expenditures with effective disclosure has not existed before today. It must be noted, furthermore, that **many of Congress' findings in passing BCRA were premised on a system without adequate disclosure.** With the advent of the Internet, prompt disclosure of expenditures can provide shareholders and citizens with the information needed to hold corporations and elected officials accountable for their positions and supporters. Shareholders can determine whether their corporation's political speech advances the corporation's interest in making profits, and citizens can see whether elected officials are "'in the pocket' of so-called moneyed interests." The First Amendment protects political speech; and disclosure permits citizens and shareholders to react to the speech of corporate entities in a proper way. **This transparency enables the electorate to make informed decisions and give proper weight to different speakers and messages**.

130 S. Ct. at 916. The Court's reference to disclosure rules adopted as part of the "campaign finance system" makes clear that it was not endorsing a disclosure rule targeting only public companies.

In sum, although the petition frames its proposal by referring to "transparency" and "disclosure," there should be no confusion about the ultimate effect of any rule adopted by the Commission—burdening, and in some cases preventing, corporations' participation in the political process, which will hurt corporations and their shareholders.

3. The Costs Of Any Rule Would Far Outweigh The Benefits.

The governing legal standard requires the Commission to base its rulemaking decisions on "a rational connection between the facts found and the choices made," including an assessment of the proposed rule's costs and benefits.[64] The rule sought by the petition cannot possibly satisfy that standard:

- The Commission could not rationally find a reason for mandating disclosure in this context: engaging in political and lobbying activity is plainly in the interest of public companies and there is no basis for finding that the normal risk management processes of public companies, in particular board oversight, are ineffective in ensuring that the corporation makes these decisions in the interests of its shareholders—particularly when we rely on those processes in a wide variety of other contexts involving greater risks to the corporation.

- The Commission could not rationally find that the benefits of such a rule—which have never been identified (and, as discussed above, do not exist)—could outweigh the huge costs, including the reduced ability of public companies to participate effectively in the public policy process in order to protect shareholder interests.

The conclusion of the Court of Appeals for the District of Columbia Circuit in invalidating the proxy access rules—"[i]n view of the admittedly (and at best) 'mixed' empirical evidence, we think the Commission has not sufficiently supported its conclusion that increasing the potential for election of directors nominated by shareholders will result in improved board and company performance and shareholder value"[65]—is even more clearly applicable here. The Commission should not embark upon a rulemaking proceeding that will consume large amounts of scarce resources when the evidence makes clear that a rule could never be lawfully promulgated.

B. The Commission Lacks Statutory Authority To Promulgate the Proposed Rule.

The petition takes the position that Section 14(a) authorizes the Commission to require the inclusion in proxies of any information, even if the information is immaterial, as long as some shareholders have evidenced an interest in the information.[66] That is plainly wrong. The Commission has repeatedly referenced materiality in this context—a standard that cannot be satisfied here.

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[64] *See Business Roundtable*, 647 F.3d at 1148, 1152 (quotation marks omitted).

[65] *Id*. at 1151 (citation omitted).

[66] Petition at 2 & nn.2-3.

To begin with, the petition's reliance on *Natural Resources Defense Council v. SEC,* 606 F.2d 1031 (D.C. Cir. 1979), is entirely misplaced. That case rejected a challenge to the Commission's decision *not to require* the disclosure of certain environmental and employment information; the court accordingly had no occasion to address the limits on the Commission's authority to *require* disclosures. The language in the opinion cited by the petition refers to the Commission's "broad discretion" in this area and does not state or in any way indicate that the Commission's discretion is wholly unbounded.

In each of the risk disclosure rules referenced in the petition, the Commission specifically limited the disclosure requirement to material information.[67] And in its determination refusing to require disclosure of environmental and employment information—the determination upheld in *Natural Resources Defense Council*—the Commission observed that "it is generally not authorized to consider the promotion of social goals unrelated to the objectives of the federal securities laws"[68] and expressly noted that materiality is a "limitation" on what types of information corporations will be required to disclose.[69]

The Commission has thus recognized that materiality is an important threshold requirement in mandating disclosure under Section 14(a). That limitation on the Commission's authority accords with basic common sense: why would Congress have authorized the Commission to require companies to disclose immaterial information?

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[67] *Proxy Disclosure Enhancements*, 74 Fed. Reg. 68334, 68335-37 (2009) (disclosure limited to risks "reasonably likely to have a material adverse effect on the company"); *Proxy Disclosure and Solicitation Enhancements*, 74 Fed. Reg. 35076, 35078 (2009) ("[D]isclosure [of compensation policies] under the proposed rule amendment would only be required if the materiality threshold is triggered."). *Executive Compensation Disclosure*, 57 Fed. Reg. 29582, 29584 (1992) (limiting disclosure to "material pay-related information"). The compensation disclosure rules referenced in the petition are premised on the very reasonable conclusion that the amounts and methods of compensation are material to shareholders because they make clear the monetary incentives of high-level corporate officials in exercising their duties.

[68] Securities Act Release No. 5627 (Oct. 16, 1975), 40 Fed. Reg. 51656 (1975).

[69] *Id.* at 51660. The Commission explained:

> Whether particular disclosure requirements are necessary to permit the Commission to discharge its obligations under the Securities Act and the Securities Exchange Act or are necessary or appropriate in the public interest or for the protection of investors involves a balancing of competing factors. . . . In administering the disclosure process under the Securities Act and the Securities Exchange Act, the Commission has generally resolved these various competing considerations by requiring disclosure only of such information as the Commission believes is important to the reasonable investor—*material information*. 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.

Id. at 51659-60 (emphasis added; quotation marks and citations omitted).

The petition does not even attempt to demonstrate that political and lobbying expenditures constitute material information. Certainly the amounts of money would not come close to triggering the 5% materiality threshold.[70] And there is no basis for finding this information material on a qualitative basis—as we have discussed, the petition has failed to present any rational reason why shareholders would find this information material. Rather, the result of such a disclosure requirement would be to harm shareholders' interests by opening the door to attacks on public companies that would reduce shareholder value.

C. A Disclosure Targeting Public Companies Would Violate The First Amendment.

There is no question that public companies' political and lobbying activities are protected by the First Amendment.[71] The disclosure rule sought by the petition would single out these activities for special requirements not applicable to other speakers. That discrimination violates the First Amendment.

Government measures that discriminate among speakers present serious First Amendment concerns.[72] Discrimination among speakers is not only troubling in its own right, it also may be a surrogate for viewpoint discrimination—which is why discrimination among speakers is often subject to the most exacting First Amendment scrutiny, and are often invalidated.[73]

"The inherent worth of the speech . . . does not depend upon the identity of its source, whether corporation, association, union, or individual."[74] That is why the American Civil Liberties Union, and many other organizations, have opposed federal legislation that would have

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[70] *See* Staff Accounting Bulletin No. 99, 64 Fed. Reg. 45150 (Aug. 19, 1999).

[71] *E.g., Citizens United*, *supra*; *First Nat'l Bank v. Bellotti*, 435 U.S. 765 (1978).

[72] *Bellotti*, 435 U.S. at 776-77.

[73] *See, e.g.*, *Sorrell v. IMS Health Inc.*, 131 S. Ct. 2653, 2762 (2011) (striking down Vermont statute restricting the use of prescription information by marketers but not by researchers); *City of Cincinnati v. Discovery Network, Inc.*, 507 U.S. 410, 430-31 (1993) (striking down Cincinatti, Ohio ordinance banning commercial handbill newsracks but not newspaper newsracks); *Bellotti*, 435 U.S. at 784 (striking down Massachusetts law that barred corporations, but not other entities, from making contributions or expenditures to influence the outcome of a vote on any question submitted to voters other than questions materially affecting the property, business or assets of the corporation); *see also Regan v. Taxation with Representation of Washington*, 461 U.S. 540, 548 (1983) (rejecting First Amendment challenge to differential tax treatment of veterans groups and other charitable organizations, but noting that the case would be different were there any "indication that the statute was intended to suppress any ideas or any demonstration that it has had that effect").

[74] *Bellotti*, 435 U.S. at 777.

imposed different disclosure regimes on different categories of political speakers, while exempting some speakers from any disclosure requirement at all.[75]

The Supreme Court has recognized that disclosure requirements can chill the exercise of First Amendment rights, and invalidated such requirements in a variety of contexts.[76] The disclosure requirements that the Court has upheld have applied even-handedly, and have not carried the possibility of viewpoint discrimination.[77]

The petition seeks to single out for regulation only public companies' political activity, conduct that is at the very core of the First Amendment. "Regulation of the corporate processes that produce corporate speech is still speech regulation even if it sails under the corporate governance flag."[78] There would be no similar disclosure obligations for other entities. That is a textbook case of the very sort of discrimination that the First Amendment prohibits. "Given corporations' inherent nature as mechanisms for earning profits from employing capital in pursuit of business opportunities, regulating speech by these entities can be viewed as directed at a specific type of activity."[79] Additional support for the conclusion that such a rule would constitute impermissible viewpoint discrimination is provided by the fact that the impetus for the rule comes largely from entities advocating policy views that are the opposite of those held by most public companies.

The First Amendment also requires that disclosure requirements not "discourage[] participation" in the political process "without sufficient cause."[80] The disclosure requirements sought by petitioners are specifically intended to discourage corporate participation in the political process, and have no justification in the purposes of the federal securities laws.

Finally, a disclosure rule is invalid if it subjects a speaker to a "reasonable probability" of "threats, harassment, or reprisals."[81] A rule of the sort advocated in the petition would create such a reasonable probability, further weakening its validity.[82] Indeed, such retribution against

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[75] Letter re: S. 3628–The Democracy is Strengthened by Casting Light on Spending in Elections (DISCLOSE) Act at 3 (July 23, 2010), *available at* http://www.aclu.org/files/assets/-Ltr_to_Senate_re_ACLU_opposes_DISCLOSE_Act.pdf.

[76] *Buckley v. Am. Constitutional Law Found., Inc.*, 525 U.S. 182 (1999); *McIntyre v. Ohio Elections Comm'n*, 514 U.S. 334, 338 & n.3 (1995); *Talley v. Cal.*, 362 U.S. 60 (1960); *NAACP v. Ala. ex rel. Patterson*, 357 U.S. 449 (1958).

[77] *E.g.*, *Buckley v. Valeo*, 424 U.S. 1 (1976) (per curiam).

[78] Ribstein, *supra*, at 1022.

[79] *Id*. at 1027.

[80] *Am. Constitutional Law Found.*, 525 U.S. at 200.

[81] *Doe v. Reed*, 130 S. Ct. 2811, 2820 (2010) (quoting *Buckley*, 424 U.S. at 74).

[82] *See, e.g.*, D. Sunshine Hillygus, *Are Consumers Motivated by Politics?*, YouGov, http://today.yougov.com/news/2012/04/30/are-consumers-motivated-politics/ (Apr. 30, 2012) (describing a recent YouGov.com poll finding that "consumer boycotting" was "more common than many other types of political activity"); Brad Smith, *The Problematic Nature of Secondary Boycotts on Political Speech*,

corporations is not only a reasonably probable outcome of the disclosure rule sought by petitioners, it is the very goal of the petition's principal supporters.

D. Even If Adoption of Such A Disclosure Rule Were Legally Permissible, There Are Additional Reasons Why The Petition Should Be Denied.

There are several additional reasons—apart from the Commission's obvious lack of legal authority to adopt the type of disclosure rule sought in the petition—that require denial of the petition.

1. Disclosure Standards Regarding Political Activity Should Be Established By Congress, And Should Be Even-Handed.

Political and lobbying activities are already subject to very substantial disclosure regimes. At the federal level, Congress has enacted detailed legislation governing disclosure of political expenditures, which has been implemented in even more detailed regulations issued by the Federal Election Commission.[83] Similar disclosure obligations are in place at the state level.[84]

The same is true with respect to lobbying. Indeed, Congress recently enacted the Honest Leadership and Open Government Act of 2007, which significantly expands federal lobbying disclosure.[85]

These existing federal regulatory systems reflect two fundamental principles.

First, federal disclosure standards are adopted by Congress, and by administrative agencies only at Congress's express direction. Indeed, it is significant that the rulemaking petition asks the Commission to adopt disclosure rules with respect to public companies ***that Congress has considered and specifically declined to enact***.[86] This end-run around the legislative process would be improper in any context; it is especially improper given Congress' established practice of addressing these issues itself and the Commission's lack of expertise in the area of political and lobbying expenditures.

Second, disclosure regarding political activities has long been governed by the basic principle that disclosure standards must be drafted so that they apply even-handedly and are not gerrymandered to advantage, or disadvantage, one side or the other in policy debates. That even-handedness is of course required by the First Amendment (as we discussed above), and serves the important goal of ensuring that all sides play by the same rules.

Center for Competitive Politics, http://www.campaignfreedom.org/2012/04/20/the-problematic-nature-of-secondary-boycotts-on-political-speech/ (Apr. 20, 2012) (noting the recent rise in secondary boycotts).

[83] *E.g.*, 2 U.S.C. §§ 431-434; Code of Federal Regulations, title 11.

[84] http://www.ncsl.org/legislatures-elections/elections/campaign-finance-an-overview.aspx.

[85] Lobbying Disclosure Act, 2 U.S.C. §§ 1601 *et seq.*; http://www.ncsl.org/legislatures-elections.aspx?tabs=1116,84,211 (collecting state lobbying disclosure requirements).

[86] *E.g.*, Shareholder Protection Act of 2011, H.R. 2517, 112th Cong. (2011); Shareholder Protection Act of 2011, S. 1360, 112th Cong. (2011).

The rule sought by the petition would violate this fundamental principle by imposing disclosure requirements on public companies that do not apply to others who participate in political activities. Thus, entities that often oppose public companies in policy debates—such as lawyers, law firms, "public interest" entities, unions,[87] closely-held businesses, and many others—would be permitted to conceal political and lobbying expenditures that public companies alone would be required to disclose. That discriminatory regulation would have significant consequences for public policy debates, as we discuss below.[88]

2. Shareholders Have Overwhelmingly Rejected Proposals Requiring Disclosure Of Political And Lobbying Expenditures Beyond What Is Mandated By Existing Law.

The petition argues that the number of shareholder proposals filed regarding disclosure of political and lobbying activity demonstrates a level of shareholder interest that justifies the promulgation of a rule requiring disclosure by all companies.[89] That contention is wrong as a matter of law—the Commission still would be obligated to satisfy the statutory standard for issuance of a rule, and as we have explained the disclosure rule sought by the petition cannot meet that test. But the metric invoked by the petition must be rejected on its own terms, because it provides no evidence whatever of the level of general shareholder interest in this topic.

While it certainly is true that a number of such shareholder proposals have been filed, the proposals have come from particular categories of shareholders—union pension funds, liberal-oriented social investment funds, and government pension funds controlled by elected officials. All of these groups (or the individuals or entities that control them) share one characteristic—frequent opposition to the positions taken by most public companies on a large number of policy issues. Their filing of these proposals therefore is as likely, and perhaps more likely, to be motivated by their desire to burden companies' ability to participate in public policy activities, as discussed above, rather than by their position as shareholders.

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[87] The broad categories covered by the petition reach far beyond the disclosures that labor unions are required to make under the Labor Management Reporting and Disclosure Act. For example, contributions to associations and other entities that may be used by those entities for political purposes are not separately disclosed by labor unions, but the petition appears to target such expenditures. S*ee* Petition at 10 & n.29.

[88] The petition attempts to soften its obvious attempt to impose discriminatory rules on public companies by suggesting that it is difficult to access information already required to be disclosed by generally-applicable law, and that public companies should provide this information for their shareholders. Petition at 8. In fact, this information is online and easily accessible—at the federal level through the websites of the Congress (for lobbying expenditures) and the Federal Election Commission (for political expenditures), and at state and local levels through websites maintained by the relevant regulatory bodies.

Moreover, the petition candidly admits that disclosures required by existing law are not really its focus, claiming that "a substantial amount of the public-company resources spent on politics are currently not disclosed in any public filing" and that "shareholders will need more information than is publicly available." Petition at 8. The petition thus plainly seeks to impose a disclosure requirement on public companies that is both unique and reaches much more broadly than any current law.

[89] Petition at 3-6.

In its recent *Business Roundtable & U.S. Chamber of Commerce* decision, the U.S. Court of Appeals for the District of Columbia Circuit recognized the dual interests of these shareholders and criticized the Commission for failing to address that issue in its analysis of the costs of benefits of the rule at issue in that case:

> [T]here is good reason to believe institutional investors with special interests will be able to use the rule and, as more than one commenter noted, "public and union pension funds" are the institutional investors "most likely to make use of proxy access." Nonetheless, the Commission failed to respond to comments arguing 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.[90]

Here, these "investors with special interests" are the principal advocates of political and lobbying expenditure disclosure requirements, as demonstrated by the fact that they sponsor the overwhelming percentage of shareholder proposals on that topic[91] and that they are the source of the positive comments that have been filed in this docket.[92] Because these shareholders' "special

[90] 647 F.3d at 1152 (citations omitted).

[91] *See* Proxy Monitor, *Shedding Light on the Influence of Shareholder Proposals in Corporations*, http://proxymonitor.org/ScoreCard2012.aspx (listing proposals and sponsoring shareholders).

[92] Virtually all of the substantive comments in favor of initiating a rulemaking have been filed by these special interest shareholders and other groups that generally oppose corporations' public policy positions. *See, e.g.*, Comments on Rulemaking Petition 4-637 by Alice O'Brien, Jason Walta, and Zachary Ista, Office of General Counsel, National Education Association, *available at* http://www.sec.gov/comments/4-637/4637-1150.pdf (Nov. 8, 2012); Lisa Gilbert, Director, Public Citizen's Congress Watch, *available at* http://www.sec.gov/comments/4-637/4637-1156.pdf (Oct. 25, 2012); American Federation of State, County and Municipal Employees (AFSME), Citizens for Responsibility and Ethics in Washington, Coalition for Accountability in Political Spending, CREDO Action, Government Accountability Project, Health Care for America Now, Mercy Investment Services, Inc., New Progressive Alliance, NorthStar Asset Management, Inc., OMB Watch, Sunlight Foundation, U.S. PIRG, West Virginia Citizen Action Group, *available at* http://www.sec.gov/comments/4-637/4637-534.pdf (July 16, 2012); Kate Coyne-McCoy, Executive Director, Coalition for Accountability in Political Spending, *available at* http://www.sec.gov/comments/4-637/4637-490.pdf (Mar. 2, 2012); Gerald W. McEntee, President, American Federation of State, County and Municipal Employees, *available at* http://www.sec.gov/comments/4-637/4637-175.pdf (Feb. 1, 2012); Janet Cowell, State Treasurer, North Carolina; Tom DiNapoli, State Comptroller, New York; Bill Lockyer, State Treasurer, California; Rob McCord, State Treasurer, Pennsylvania; Bill de Blasio, Public Advocate, New York City; Representative William A. Current, Sr., North Carolina House of Representatives; Representative James Pilliod, New Hampshire House of Representatives; and Toni Pappas, County Commissioner, Hillsborough County, New Hampshire, *available at* http://www.sec.gov/comments/4-637/4637-84.pdf (Jan. 19, 2012); Daniel Pedrotty, Director, Office of Investment, AFL-CIO, *available at* http://www.sec.gov/comments/4-637/4637-25.pdf (Jan. 18, 2012); Americans for Campaign Reform, Catholic Foreign Mission Society of America-Maryknoll Fathers and Brothers, Center for Media and Democracy, Citizens for Responsibility and Ethics in Washington (CREW), Citizen Works, Coalition for

interests" are clear with respect to the disclosure issue, the Commission cannot gauge shareholder interest on the basis of these shareholders' activities.

The only accurate way to gauge shareholder interest is to examine the votes that these proposals actually received. An independent evaluation of proxy resolutions at Fortune 200 companies found that the average shareholder vote in favor of proposals relating to disclosure of political and lobbying activities in recent years has ranged around the 20% level; but "[o]verall, in 2012, Fortune 200 shareholder proposals relating to political spending or lobbying received only 17 percent support. This is the lowest level of any year in the Proxy Monitor database."[93]

Moreover, "shareholder votes across all classes of political-spending proposals generally declined [from 2011 to 2012], including among the more limited class of political-spending-disclosure proposals advocated by the Center for Political Accountability, for which shareholder support across the Fortune 200 fell from 26.6 percent in 2011 to 22.7 percent in 2012."[94] "[V]ote totals across the broader Fortune 500" showed "a similar decrease in shareholder support, from 28.6 percent in 2011 to 25.2 percent in 2012 for CPA-type proposals."[95]

Even though the total number of political disclosure proposals at Fortune 200 companies increased—and there is often increased media attention on the issue—***support by actual shareholders is declining***. There simply is no basis for the Commission to conclude that there is significant shareholder support, outside the limited category of self-interested shareholders, for mandatory disclosure rules in this area.

Finally, the number of comments filed with the Commission do not support a different conclusion. More than 99.7 percent of those comments are "astro-turf" form letters generated by the same group of organizations that have spawned the shareholder proposals on this issue. And there is no evidence at all that any of the individuals filing those form letters are actually shareholders. The comments filed by self-identified shareholders all come from the same subset of shareholders as the shareholder proposals discussed above. They too accordingly provide no basis for finding ***shareholder*** support, as opposed to support from politically-motivated

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Accountability in Political Spending (CAPS), Democracy 21, Democracy for America, Democracy North Carolina, Free Speech for the People, Maryknoll Office for Global Concerns, Michigan Campaign Finance Network, Nell Minow, N.C. Center for Voter Education, Ohio Citizen Action, Public Campaign, Public Citizen, Sunlight Foundation, U.S. Chamber Watch, U.S. PIRG, and Wisconsin Democracy Campaign, *available at* http://www.sec.gov/comments/4-637/4637-21.pdf (Jan. 6, 2012).

[93] James R. Copland, *A Report on Corporate Governance and Shareholder Activism,* at 19 (Fall 2012), *available at* http://proxymonitor.org/Forms/pmr_04.aspx.

[94] *Id*. The report notes that the Center for Political Accountability "claims higher vote totals for its shareholder proposals by inflating its figures. It counts not the percentage of shareholder support (among all shareholders present in person or by proxy and entitled to vote at a shareholder meeting), but rather the percentage of support among shareholders voting For or Against"—even if the company's bylaws provide that support should be assessed based on the former measure. The Proxy Monitor data cited in the text properly "assess[es] vote shares according to companies' own bylaws." *Id*. at n.64.

[95] *Id*.

organizations that stand to gain in policy debates if the Commission places discriminatory burdens on public companies' political and lobbying activities.

3. The Proposal's Disclosure Requirements Are Not Corporate "Best Practices"—The Overwhelming Majority Of Public Companies Have Not Adopted Them.

The petition also claims that public companies have voluntarily adopted disclosure practices of the type sought in the petition, and that this supposed fact supports adoption of a rule. But the premise of this assertion is entirely incorrect—there is no factual support for the contention that large numbers public companies have voluntarily agreed to disclosure in addition to what is required by generally-applicable political activity and lobbying laws.

The claim in the petition is based on disclosure information compiled by the Center for Political Accountability ("CPA"), which is hardly an independent source. It is the leading advocate for disclosure of the sort sought by the petition and the CPA's analysis, embodied in the "the CPA-Zicklin Index" is prepared by CPA and structured to provide back-up for CPA's claims.[96]

Moreover, even CPA's own 2012 analysis—updated from the one cited in the petition—fails to support the petition's claims. The report shows that fewer than 15 of 196 companies are disclosing political expenditures that are not already required to be disclosed by the applicable political contribution laws.[97] Thus, only a small minority of companies are disclosing more than

[96] The report is copyrighted by CPA and the authors are all CPA employees. *See The 2012 CPA-Zicklin Index of Corporate Political Accountability and Disclosure*, at 2, 4 (Sept. 2012), *available at* http://politicalaccountability-.net/index.php?ht=a/GetDocumentAction/i/6903 ("*2012 CPA Report*"). Thus, although the report cover bears the logo of the University of Pennsylvania's Wharton School, and of the Carol and Lawrence Zicklin Center for Business Ethics Research, the CPA in fact appears to produce the entire report.

[97] CPA's report claims that 79 companies either fully or partially comply with its standards regarding disclosure of payments to tax-exempt organizations or trade associations that may be used for political purposes. *2012 CPA Report* at 23-29. But that is a gross overstatement. To begin with, even CPA asserts that *only one company* (and that company only partially) discloses the amounts and recipients of payments made by tax-exempt organizations or trade associations to which the company donates funds. In addition, review of the policies of the entities listed as disclosing payments to trade associations that may be used for political purposes reveals that the overwhelming majority of those entities do not disclose the amounts of those payments—they simply disclose the existence of payments and, in some cases, that they have requested the amounts used for political purposes and the trade association has not supplied that information. Other companies disclose total contributions to trade associations but do not break them down by association. A few companies disclose the information provided by trade associations regarding the amount of payments that are not tax-deductible, but that amount is vastly overinclusive because it includes sums expended by the trade association for lobbying and other non-deductible activities. With respect to contributions to other organizations, some companies listed by CPA as disclosing in fact have a policy against making contributions, or make such contributions only to organizations that are required by law to disclose their contributors. And other companies follow the same approach as for trade associations, listing total contributions but not identifying specific organizations, or report that the organizations declined to identify the amounts used for political purposes.

what the law requires—a far cry from the petition's claim of a corporate groundswell in favor of its one-sided disclosure requirements.

A report addressing corporate political and lobbying activities issued by a committee of the Conference Board confirms that there is no "best practice" of voluntary disclosure of information not already required to be disclosed by law. The report states that "[e]ach corporation must confront these issues thoughtfully, consider them carefully, and arrive at an answer that is consistent with their own governance practices, business strategies and the interests of the stakeholders—including shareholders, employees, and customers."[98]

The committee specifically rejected a "check-the-box, one-size-fits-all approach," concluding that "[w]hen it comes to political spending by corporations, and the related questions of how to demonstrate accountability and how much information to disclose, there is no single right answer."[99] That is precisely the opposite of the petition's position.

In sum, a rule along the lines advocated by the petition would not codify "best practices"; rather, it would impose extraordinary requirements that only a very few companies have adopted.

4. Acceptance By The Commission Of The Unsupportable Justifications For This Rulemaking Will Produce A Flood Of Similar Disclosure Demands, Which Would Result In Disclosure Overload And Significant Destruction Of Shareholder Value.

There is another significant reason why the Commission should deny the petition. The only way the Commission could proceed would be if it endorsed the argument that disclosure should be mandated when shareholders—even a small minority of shareholders with "special interests" other than the desire to maximize shareholder value—contend that the board and management cannot be trusted to act in the interests of shareholders. That determination would have far-reaching consequences.

There are numerous other areas in which that same assertion could be made, and—once the precedent was established—demands for rules compelling disclosure of other types of information can be expected, and for precisely the same reason: to use disclosures not to inform shareholders but rather to inflict brand damage on companies to force them to change their policies. Here are just a few of the categories of information that could be demanded:

- Disclosure annually of jobs "exported" from the United States;
- Disclosure of sales in countries that the State Department has found to engage in religious persecution, or other forms of human rights violations; or
- Disclosure annually of each facility located outside the United States that (a) does not comply with U.S. environmental standards; or (b) does not comply with U.S. labor standards, whether hours or minimum pay.

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[98] Conference Board, *supra*, at 5.

[99] *Id*. at 5, 15.

All of these “disclosures” could easily be justified on the same spurious ground that the petition advances with respect to political activity—concern that the decision to engage in the conduct was not truly in shareholders’ interest and could possibly lead to brand damage. But each of these additional disclosures—like those sought in the petition—would be used to attack the company and damage its brand, and thereby hurt shareholder value. That is why these disclosures, like the disclosures sought in the petition, would be ***counterproductive*** in terms of protecting and enhancing shareholder value.

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The rule sought by the petition cannot be grounded in any rational policy justification, is beyond the Commission’s statutory authority, and would violate the First Amendment. The petition therefore should be denied.

Sincerely,

60 Plus Association
Agricultural Retailers Association
Aircraft Owners and Pilots Association
American Gaming Association
American Trucking Associations
Associated General Contractors of America
Automotive Aftermarket Industry Association
Construction Industry Round Table (CIRT)
Consumer Data Industry Association
Georgia Mining Association
Greater Springfield Chamber of Commerce
Johnson City Chamber of Commerce
Maine State Chamber of Commerce
Metals Service Center Institute
Mississippi Associated Builders & Contractors, Inc.
Missouri Insurance Coalition
Motor & Equipment Manufacturers Association
National Association of Manufacturers
National Association of Wholesaler-Distributors
National Council of Chain Restaurants
National Mining Association
National Restaurant Association
National Retail Federation
Retail Industry Leaders Association
Rocky Mountain Chapter, Associated Builders & Contractors
Schuylkill Chamber of Commerce
Small Business & Entrepreneurship Council
The Ohio Society of CPAs
United States Chamber of Commerce