January 6, 2012

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

RE: File No. 4-637, Comments on Petition for Rulemaking on Corporate Political Spending, Submitted by 21 Civic Organizations and Individuals

These comments are submitted by the following organizations – 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 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 – in response to the Petition for Rulemaking (File No. 4-637), requesting the Securities and Exchange Commission (SEC) to initiate a rulemaking project to regulate corporate political spending by publicly-held corporations.

Our organizations encourage the SEC to carry through with the rulemaking project and develop regulations mandating disclosure to investors, shareholders and the public of corporate political expenditures above a *de minimis* threshold, including contributions to third party entities for political purposes, and ensuring that shareholders have the right to use company proxy statements to propose and adopt by-laws requiring shareholder approval of overall corporate political budgets.

Responsible Corporate Governance in Political Spending Decisions

American corporations have long been major financial players in the political process, by raising and spending campaign funds in federal elections through political action committees (PACs) and lobbying federal and state governments. Until very recently, most of this corporate political spending had been subject to regulation and disclosure requirements of campaign finance laws and lobbying disclosure laws.

Corporate funds generally were not allowed to be used to pay for express advocacy campaign ads (independent expenditures) at the federal level or in state and judicial elections of 24 states;

nor could corporate treasury funds be used to pay for "electioneering communications" in federal elections and a small handful of other states since passage of the Bipartisan Campaign Reform Act (BCRA) of 2002.[1]

As a result, corporate governance procedures guiding corporate decisions to make direct political expenditures out of treasury funds were not really needed and had not been an issue addressed by the Securities and Exchange Commission (SEC).

All that changed on January 21, 2010, when the U.S. Supreme Court radically changed federal and state campaign finance laws in the *Citizens United v. Federal Election Commission* decision.[2] The Court dramatically reversed earlier precedent and ruled that corporations and unions now have the right to use general treasury funds to pay for unlimited independent expenditures and electioneering communications supporting or attacking federal, state or judicial candidates. Literally overnight, the Court opened up new pathways for unlimited political expenditures by corporations – pathways that largely fall outside current corporate governance rules and procedures. As a result, the SEC must now assume primary responsibility in developing responsible corporate governance procedures for addressing this new environment of corporate political spending.

Comparative Regulation of Corporate Political Activity in the United Kingdom and the United States

The United Kingdom has long allowed corporate financing of electoral activity. Because of this history, laws have been on the books in the United Kingdom as early as the 1960s to provide guidance for corporate political spending. Largely out of concern that the absence of regulations

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[1] Prior to the *Citizens United* decision, 24 states either prohibited or limited corporate or union spending in state and local elections. [For a listing of states that restrict corporate spending, go to: http://www.citizen.org/documents/Corporate_spending_on_state_candidates.pdf]. In addition, the decision potentially unleashed direct corporate financing of judicial campaigns in the 39 states that allow for election of judges. [For a listing of state judicial selection processes, go to: http://www.citizen.org/documents/Judicial_selection_chart.pdf]

[2] The "electioneering communications" provision of BCRA is an expansion of the class of advertisements defined as campaign ads rather than issue ads, and thus subject to regulation. In addition to the express advocacy standard of campaign ads, any broadcast ad that refers to a clearly identified federal candidate within 60 days of a general election, or 30 days of a primary election, and which targets that candidate's constituency, is also classified as an "electioneering communication." An ad is considered targeted to a candidate's constituency if it can be received by 50,000 or more persons in the candidate's district (as determined by the Federal Communications Commission). "Broadcast ad" includes television, radio, cable or satellite advertisements, but not Internet advertisements. Prior to two recent Supreme Court decision, FEC v. Wisconsin Right to Life, 551 U.S. 449 (2007) and Citizens United v. FEC, 588 U.S. 50 (2010), the electioneering communications provision provided a bright line standard distinguishing "campaign ads" from "issue ads," subject to disclosure and the restrictions against funding from corporate or union treasuries. The Court did not strike down the electioneering communications provision, but it did allow corporate and union funding of such ads. Today, following those court rulings, only the disclosure requirement for electioneering communications remains.

and guidance would permit CEOs or a small group of corporate officers to tap into the corporate treasury without consulting with, or even informing, shareholders and spend that money on partisan elections – which may or may not be in the benefit of the company and shareholders – the United Kingdom adopted the Companies Act of 1967.

The original Companies Act required disclosure to shareholders of corporate political spending in U.K. elections above a *de minimis* threshold. The Act was amended through the decades. Finally, the U.K. adopted the Political Parties, Elections and Referendums Act in 2000 that not only enhances shareholder disclosure of direct corporate spending and contributions to parties and candidates, it also requires annual shareholder approval of each company's overall political budget. The Act was amended again in 2006, requiring that directors are jointly and severally liable for unauthorized corporate political expenditures.[3]

Due to the abrupt dictates of the *Citizens United* decision, little comparable guidance for corporate political spending exists in the United States. Neither the Internal Revenue Code, the Securities Exchange Act nor SEC regulations establish clear procedures on how decisions are made to effectuate corporate political expenditures. While it is the case that corporate directors have fiduciary duties that they owe to the well-being of their companies, fiduciary obligations are usually governed by state laws, subject to judicial interpretation, and frequently are not uniformly agreed upon or enforced.[4] Unless a company's internal policies deem otherwise, a CEO in the United States may simply spend money directly from the company treasury promoting or attacking favored candidates, even without receiving the informed consent of directors or shareholders.

Several very notable efforts are being made in the United States to encourage corporations *voluntarily* to disclose their political spending to shareholders, in lieu of the absence of such corporate transparency requirements.

New York City Public Advocate Bill de Blasio is running a pledge drive urging companies to state publicly that they will not spend corporate treasury money in elections. De Blasio has pledges from about a dozen major corporations, including Citigroup, General Electric and Goldman Sachs, not to spend corporate treasury money in elections. The NYC Public Advocate is maintaining a web page listing those companies that have agreed to the pledge, those that have refused the pledge and those that have not developed a clear policy on the issue.[5]

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[3] For further reading on the effort in the United Kingdom to regulate corporate expenditures and contributions to parties and candidates, see Ciara Torres-Spelliscy and Kathy Fogel, "Shareholder-Authorized Corporate Political Spending in the United Kingdom," *University of San Francisco Law Review* (Spring 2012) at 479.

[4] The Conference Board, **CORPORATE GOVERNANCE HANDBOOK**, 3rd ed. (2009) at 14-17.

[5] The New York City Public Advocate web page listing the companies that have and have not agreed to the pledge not to spend corporate money in elections is available at: http://advocate.nyc.gov/corporate-spending

The campaign for voluntary disclosure by the Center for Political Accountability (CPA) is perhaps the most widely known and successful thus far. CPA has been reaching out to most major corporations in the United States, encouraging companies to adopt internal rules establishing board oversight of political spending decisions as well as transparency to shareholders of how the companies are spending campaign dollars. CPA even provides a model code of conduct for corporate political spending decisions.

Judging from surveys of companies that have adopted internal policies governing political spending decisions, CPA concludes that most of America's largest publicly traded companies are voluntarily moving to disclose their corporate spending on politics. The group's often cited CPA-Zicklin Index, a joint project with the Carol and Lawrence Zicklin Center for Business Ethics Research, suggests that 57 companies among the largest S&P 100 now disclose on web sites their direct political spending and have adopted some element of board oversight. One third of the S&P 100 have instituted policies restricting political expenditures, with two major companies – Colgate-Palmolive and IBM -- prohibiting direct political spending altogether. Forty-three companies reportedly disclose some information about indirect political spending through trade associations or other tax-exempt groups, and 24 companies have pledged not to make independent expenditures.[6]

Though encouraging, the results of the CPA-Zicklin Index may well be over-stated.

In a similar but more comprehensive analysis of the S&P 500 companies, the nonprofit Investor Responsibility Research Center (IRRC) found that while more companies are indeed adopting internal policies for oversight and disclosure of political spending, problems abound. First of all, the number of large companies not adopting such policies remains very troubling and uneven across industrial sectors. Voluntary company disclosure of political spending remains limited and only 20 percent of S&P 500 companies report on how they spent shareowners' money. Two-thirds of the companies that appear to spend from their treasuries do not report to investors on this spending. The least transparent are Telecommunications and Financials firms; by contrast over 40 percent of Health Care companies explain where the money goes.[7]

Similarly, IRRC found that more than 75 percent of S&P companies have no policies on indirect political spending through trade associations or tax-exempt groups. Only 26 companies in the

[6] Center for Political Accountability, *The CPA-Zicklin Index of Corporate Political Disclosure and Accountability: How Leading U.S. Companies Navigate Political Spending in the Wake of Citizens United* (Oct. 28, 2011), available at: http://www.politicalaccountability.net/index.php?ht=d/sp/i/5848/pid/5848

[7] Heidi Welsh and Robin Young, *Corporate Governance of Political Expenditures: 2011Benchmark Report on S&P 500 Companies*, IRRC Institute (Nov. 2011), available at: http://www.irrcinstitute.org/pdf/Political_Spending_Report_Nov_10_2011.pdf

entire S&P index acknowledge any relationship with 501(c)(4) social welfare organizations that are playing a key role in funding electioneering ads, despite evidence that these groups are receiving more money for their political activities than ever before. Furthermore, the largest companies spend the most on politics, with the top two revenue quintile companies responsible for spending $915 million on federal and state electioneering and lobbying activities in 2011 alone.[8]

A second problem uncovered by IRRC is gaping inconsistencies between stated corporate governance policies of corporations regarding political spending and their actual behavior. The overall number of companies that assert they do not spend money in politics has grown to 57, up from 40 a year ago. But a comparison of spending records and policy prohibitions shows that only 23 companies with 'no spending' policies actually did not give any money to political committees, parties or candidates in 2010 (though they may still lobby). *Only 17 of these firms avoided all forms of political spending, including lobbying*.[9] The same is true when it comes to stated disclosure policies. Apparently there is a large discrepancy between what is said and what is done. Companies have various conceptions on what constitute political expenditures subject to disclosure. Heidi Welsh, the lead author of the report, noted: "It's a complicated landscape. On the one hand, there's been a real movement toward disclosure, but on the other, a huge part of the picture remains obscured."[10]

Campaign Finance Laws Regulating Corporate Money in Elections

At the turn of the last century, substantial corporate financing of elections first became readily apparent in the 1896 presidential election.[11] Corporate funding of campaigns soon thereafter became an all-out scandal in the 1904 presidential election when the losing candidate, Alton Parker, publicly accused Theodore Roosevelt of secretly financing his campaign with contributions from life insurance companies, a charge that was later supported in an investigation by the state of New York.[12] Public outrage ensued as it became evident that the insurance companies were simultaneously seeking legislation from the federal government that would limit the ability of policyholders to sue the companies.

President Roosevelt sought to assuage the furor in his 1905 State of the Union address when he urged Congress to prohibit all corporate contributions to campaigns. Roosevelt proclaimed:

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[8] Id, at 2.

[9] Id, at 1.

[10] Kenneth Doyle, "New Study Finds Corporate Disclosure of Political Money Up but Still Minimal," *BNA Money and Politics Report* (Nov. 14, 2011).

[11] Matthew Josephson, **THE POLITICOS, 1865-1896** (1938) at 699.

[12] Adam Winkler, "Other People's Money: Corporations, Agency Costs and Campaign Finance Law," *Georgetown University Law Journal*, 92:871 (2004) at 886.

> *"The fortunes amassed through corporate organization are now so large, and vest such power in those that wield them, as to make it a matter of necessity to give to the sovereign – that is, to the Government, which represents the people as a whole – some effective power of supervision over their corporate use."*[13]

Congress has a long history of carefully deliberating over the proper role of corporate money in U.S. elections. Following Roosevelt's scandal, Congress responded in 1907 by passing the Tillman Act. Introduced by Sen. Ben "Pitchfork" Tillman (D-S.C.),[14] the Act specifically banned "mak[ing] a money contribution in connection with any election to any political office." The Tillman Act's ban on corporate contributions in federal elections was eventually subsumed under the Federal Corrupt Practices Act of 1925. In 1943, Congress temporarily extended the ban on corporate contributions to labor unions as well under the War Labor Disputes Act. Large labor unions responded to the War Labor Disputes Act by diverting money to independent expenditures (rather than contributions) on behalf of their favored candidates. In order to close this loophole, Congress enacted the Taft-Hartley Act of 1947 to clarify that both campaign contributions and expenditures by corporations and unions were prohibited by law.[15] The Federal Election Campaign Act of 1971 (FECA) incorporated the Taft-Hartley Act's long-standing provision against corporate and union campaign contributions and expenditures. More importantly, subsequent FECA amendments created an independent agency – the Federal Election Commission – charged with monitoring and enforcing compliance to the law. Corporate and union money began once again to trickle back into federal elections in the mid-1980s in the form of 'soft money," ostensibly for the limited purposes of paying for party-building activities and so-called issue ads. When it became clear that the trickle of soft money turned into a flood of corporate and union money to pay for electioneering activities, Congress passed the Bipartisan Campaign Reform Act of 2002 to turn off the spigot of soft money.[16]

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[13] Theodore Roosevelt, State of the Union address (Dec. 5, 1905), available at: www.thoedore-roosevelt.com/sotu5.html.

[14] Sen. Tillman kicked off the 1896 presidential campaign with a rousing speech on the Senate floor in which he challenged sitting President Grover Cleveland for doing very little to address the economic depression. Tillman made several references to pitchforks and threatened to go to the White House and "poke old Grover with a pitchfork" to prod him into action. Afterward, the Senator was known as "Pitchfork" Ben.

[15] The legislative history indicates that Congress believed both contributions and expenditures were already prohibited by the Federal Corrupt Practices Act. As Sen. Robert Taft (R-Ohio) explained: "[T]he previous law prohibited any contribution, direct or indirect, in connection with any election," and the new legislation "only makes it clear that an expenditure … is the same as an indirect contribution, which, in my opinion, has always been unlawful." Sen. Taft, Congressional statement, 93 **CONGRESSIONAL RECORD** 6594 (1947).

[16] In the 2000 election cycle, national and congressional party committees broke all previous records in soft money fundraising. National Republican party committees raised $249.9 million and spent $252.8 million in soft money, while national Democratic party committees raised $245.2 million in soft money and spent $244.8 million. More than half of this soft money was transferred to state parties and used to pay for television advertisements. Overall, 77% of party-sponsored television commercials relating to federal elections in the 2000 election were paid for by

There are two key pillars of the Bipartisan Campaign Reform Act that have fundamentally transformed campaign finance law. First, the Act prohibited raising and spending "soft money" by federal officeholders and candidates and by the national parties, and severely restricts the use of soft money by state and local parties in relation to federal election activities. Second, the Act redefined what constitutes a campaign advertisement. It imposed a bright-line standard in which any broadcast advertisement that depicts a candidate within 30 days of a primary election or 60 days of a general election, and is targeted to the voting constituency of that candidate, constitutes an "electioneering communication," subject to federal campaign finance regulations and disclosure requirements.

The electioneering communications section of the law was limited to candidate-specific broadcast, cable and satellite communications to targeted audiences in close proximity to primary and general elections. Its purpose was to extend the existing prohibition on corporate and union expenditures on express advocacy to what had become its functional equivalent. BCRA left untouched the many avenues for campaigning and lobbying available to corporations and unions not covered by the bright-line test for electioneering (or by the ban on party soft money).

Avenues for corporate and union involvement in politics that remained open included, for example, genuine issue advocacy, lobbying activity, partisan political communications among their shareholders and memberships, contributions and independent expenditures through political action committees, sponsoring candidate and party appearances at forums and conventions, and providing nonpartisan registration and mobilization of voters among the general public.

The *Citizens United* decision largely reversed this century of legislative efforts to rein in corporate money in federal elections. Though it left intact the definition of "electioneering communications" and the disclosure laws that apply to independent expenditures and electioneering communications, these campaign expenditures could now be financed directly from corporate treasuries. Corporations and unions are still prohibited from making direct campaign contributions to federal candidates and parties, since the contribution ban was not challenged in the *Citizens United* case, but corporations and unions can now make unlimited

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state parties. The national party committees and federal congressional committees combined purchased about 23% of the party ads that addressed federal elections. Not surprisingly, most of this state party spending activity took place in the most competitive states in the presidential election: Florida, Pennsylvania, California, Michigan, Washington, and Ohio. In other words, the national parties found a way to tap into corporate and union money and use that money for television advertising on behalf of federal candidates, particularly for the presidential candidates. Craig Holman, *The End of Limits on Money in Politics: Soft Money Now Comprises the Largest Share of Party Spending on Television Ads in Federal Elections*, NYU's Brennan Center for Justice (2001), available at: http://brennan.3cdn.net/f1b070cbd490336610_08m6bpvsf.pdf expenditures for or against candidates as long as those expenditures are not coordinated with the candidates.

Not long after the *Citizens United* decision allowed unlimited corporate political expenditures, lower courts and the FEC expanded the ruling to also allow unlimited corporate contributions to entities that make independent campaign expenditures. In *SpeechNow.org v. Federal Election Commission*, SpeechNow, a section 527 group formed to make only independent expenditures, challenged the constitutionality of the $5,000 contribution limit on contributions from individuals to their group as well as the political committee registration and disclosure requirements. The D.C. Circuit Court of Appeals held that limits on contributions made by individuals to independent expenditure groups such as SpeechNow are indeed unconstitutional in light of the Supreme Court's decision in *Citizens United*. The FEC then took this decision a step further and issued an advisory opinion stating that the *Citizens United* decision exempted independent expenditure-only committees from the prohibitions on *corporate* and *union* contributions as well as individual contributions.[17]

In a matter of just a few short years since January 21, 2010, the campaign finance laws restricting corporate financing of elections have gone nearly full circle – back to the turn of the last century.

Transparency of Corporate Political Spending Is Constitutional, But Not Reality

While the Court has returned us to the era of unlimited corporate spending in elections, there remains one aspect of modern campaign finance law that the Court has steadfastly upheld – disclosure.

Eight justices of the Supreme Court upheld the disclosure and disclaimer requirements of federal campaign finance laws in both the 2003 *McConnell v. FEC* decision that originally upheld most aspects of BCRA[18] and the 2010 *Citizens United* decision. Justice Anthony Kennedy, the principal author of *Citizens United*, wrote extensively about the value of disclosure, especially in the new regime of unlimited corporate spending. But Justice Kennedy and the Court were, at best, naïve about the quality of disclosure under today's campaign finance system. While it is indeed the case that the campaign finance statutes call for full disclosure of donors behind independent expenditures and electioneering communications, the Federal Election Commission in 2007 began dismantling the law's disclosure requirements through hostile regulations.

The law itself is quite clear that the sources of funds behind campaign ads are subject to disclosure. Section 201 of BCRA, for example, lays out the disclosure requirements for groups funding electioneering communications. BCRA clearly states that all major donors to the person making the electioneering communication must be disclosed, not just those who contributed for a

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[17] Diana Dwyer, *After Citizens United and SpeechNow.org Decisions: Considering the Consequences of New Campaign Finance Rules*, paper presented before the 2011 annual meeting of the American Political Science Association, Seattle, Washington (Sep. 1-4, 2011).

[18] McConnell v. Federal Election Commission, 540 U.S. 93 (2003).

campaign ad. The provision reads in part: "Every person who makes a disbursement for the direct costs of producing and airing electioneering communications in an aggregate amount in excess of $10,000 during any calendar year shall, within 24 hours of each disclosure date, file with the Commission a statement containing . . . the names and addresses of all contributors who contributed an aggregate amount of $1,000 or more to the person making the disbursement during the period beginning on the first day of the preceding calendar year and ending on the disclosure date."

After the Supreme Court's 2007 *Wisconsin Right to Life* decision created a broad exemption to BCRA's ban on independent electioneering communications close to elections – the case permitted corporations and unions to fund any ad that could be interpreted as something other than an appeal to support or oppose a candidate – the FEC modified its regulations implementing the disclosure requirements.

The agency altered its disclosure regulation at the end of 2007 requiring a corporation or labor organization that makes electioneering communications to disclose "the name and address of each person who made a donation aggregating $1,000 or more to the corporation or labor organization, aggregating since the first day of the preceding calendar year, which was *made for the purpose of furthering electioneering communications*."[19] BCRA makes no such exception.

As a result, this language has recently been interpreted by a growing number of outside groups to mean that only those donors who specifically "earmark" funds for a campaign ad need be disclosed. FEC staff has periodically requested full donor disclosure from outside groups financing independent ads, but the Commission itself has deadlocked on taking any actions against those declining compliance. More and more of these groups are now refusing to disclose the major donors funding their campaign ads, claiming that none of their funders earmarked the money for electioneering activity. This refusal to disclose donors is also expanding among groups funding other independent expenditures, not just electioneering communications.

On August 18, 2010, the Republican bloc of FEC commissioners further weakened the disclosure requirements when it blocked a case alleging that an organization called Freedom's Watch failed to comply with the disclosure rule.[20]

Freedom's Watch, a conservative nonprofit corporation, sponsored television ads in the 2008 elections that reportedly were funded by roughly $30 million from a single donor. A New York Times article quoted an unnamed Republican operative saying that the group's $30 million for ad spending "came almost entirely from casino mogul Sheldon G. Adelson," who has "insisted on parceling out his money project by project, as opposed to setting an overall budget, limiting the group's ability to plan and be nimble…."[21]

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[19] 11 CFR 104.20(c)(9). Emphasis added.

[20] Statement of Reasons for Chairman Matthew S. Petersen and Commissioners Caroline C. Hunter and Donald F. McGahn, Freedom's Watch, Inc., MUR 6002 (Aug. 13, 2010), available at: http://eqs.sdrdc.com/eqsdocsMUR/10044274536.pdf

[21] Michael Luo, "Great Expectations for a Conservative Group Seem All But Dashed," *The New York Times* (April 12, 2008).

Substantial evidence showed that Mr. Adelson earmarked contributions for Freedom's Watch's electioneering communications budget. But in a written "statement of reasons," the three Republican commissioners announced a new, even higher bar for requiring disclosure: Not only must funds be earmarked for electioneering communications; they must be earmarked for a specific campaign ad.

The impact of this deregulation of the campaign finance disclosure requirement has been dramatic. In terms of electioneering communications by outside groups, the percentage of groups disclosing the financiers of their ads fell from nearly 100 percent before Wisconsin Right to Life to less than 50 percent in 2008, and to just over a third in the recently completed election cycle. In terms of independent expenditures by outside groups, donor disclosure fell from 96.7 percent in 2006 to 83.3 percent in 2008 and down to 70 percent in 2010. Combined this means that overall disclosure of the sources of funds behind campaign ads by outside groups has fallen from near full disclosure in 2004 and 2006 to about half of all sources of funds by outside electioneering groups being disclosed in 2010.[22] If left unaddressed, the percentage of disclosed funds in the 2012 elections and beyond will likely fall much, much lower.

Through deregulation and lack of enforcement, very little is left of what by all rights should be a very robust transparency law.

Lack of Transparency Poses Particular Problems for Corporate Political Spending

Justice Anthony Kennedy justified permitting corporate electioneering in large part on the expectation that the corporate funders of the ads would be disclosed, thereby enabling shareholders and the public to hold corporations accountable. Kennedy highlighted this point when he wrote in *Citizens United*:

> *"A campaign finance system that pairs corporate independent expenditures with effective disclosure has not existed before today. 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…. 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."*[23]

Without adequate disclosure of corporate political spending, shareholders and investors have little means to hold corporate directors accountable and to safeguard their investments. This is a major concern of shareholders. Even before the *Citizens United* decision, a large majority (85

[22] Public Citizen, *Disclosure Eclipse* (Nov. 18, 2010), available at: http://www.citizen.org/documents/Eclipsed-Disclosure11182010.pdf

[23] Citizens United v. Federal Election Commission, 558 U.S. 50 (2010)

percent) of American shareholders surveyed in 2006 felt that there is a "lack of transparency surrounding corporate political activity" and that this "lack of transparency and oversight in corporate political activity encourages behavior" that threatens shareholder value. [24] A full 94 percent of shareholders surveyed supported disclosure and 84 percent supported board oversight and approval of any "direct and indirect" corporate political spending.

But even corporations themselves may find this new world of unlimited and undisclosed political spending not in their best interests.

The Committee for Economic Development (CED), a nonprofit and nonpartisan association of some 200 senior corporate executives and academic leaders, has hosted numerous conferences and sponsored studies highlighting the potential problems for the business community caused by the *Citizens United* decision.

> *"CED is deeply concerned about the changes taking place in political finance. Current fundraising practices promote a pay-to-play mentality that encourages political giving as a means of influencing legislative decisionmaking…. We believe this demand for campaign dollars impairs the economic development and the fiscal health of the nation by promoting behavior that is not conducive to sustained value creation…. Corporate resources that might be better spent investing in an enterprise or otherwise building shareholder value would then be diverted to political activities."*[25]

CED bolsters its argument with a 2010 survey of major CEOs across the business community conducted by Zogby International. Six in ten of the 301 business leaders surveyed say there is pressure to contribute to political campaigns. Seventy-seven percent believe that corporations should disclose all of their direct and indirect political expenditures, including money provided to third party organizations to be spent on campaign ads. The poll also found that ninety-three percent of business leaders believe that corporate boards should be informed of the beneficiaries and purposes of the company's direct and indirect political spending. Two-thirds polled agreed with the statement: "the lack of transparency and oversight in corporate political activity encourages behavior that puts corporations at legal risk and endangers corporate reputations."[26]

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[24] Center for Political Accountability, "Corporate Political Spending: A Survey of American Shareholders," Mason-Dixon Polling & Research (2006), available at: http://www.politicalaccountability.net/index.php?ht=a/GetDocumentAction/i/918

[25] Committee for Economic Development, "After Citizens United: Improving Accountability in Political Finance," *Executive Summary* (2011).

[26] Committee for Economic Development, "New Business Poll Shows Discontent with Undisclosed Campaign Expenditures Following Citizens United Decision," Press Release (Oct. 28, 2010).

There is a growing body of empirical evidence that unlimited and undisclosed corporate political spending may indeed undermine overall corporate value, or at the very least, may not provide shareholders with any discernible benefits. Rather, corporate political activity overall often reflects the interests of the managers of the companies, or on a risk-adjusted basis, is less beneficial than other purposes to which shareholder funds could be put.

John Coates, for example, found that, both before and after *Citizens United*, corporate political activity was associated with lower corporate value. Specifically, among the S&P 500 – which accounts for 75 percent of the market capitalization of publicly traded companies in the U.S. – firms active in politics, whether through company-controlled political action committees, registered lobbying, or both, had lower price/book ratios than industry peers that were not politically active. This was true in every election cycle from 1998 to 2004.[27]

This negative trend between corporate political activity and value became even more pronounced after the *Citizens United* decision, in the 2010 elections, when politically active firms had, on average, a 24 percent lower price/book ratio than their industry peers.[28] This difference can be found before and after controlling for other factors that have previously been found to affect firm value, including recent profits, sales growth, leverage, and size. In addition, while political activity generally correlates negatively with general measures of shareholder rights and power, it continues to be associated with lower shareholder value even after controlling for shareholder rights of a general nature. That is, even among companies with poor shareholder rights, firms that are more politically active tend to have lower valuations than less active firms.

In an unrelated study, Rajesh Aggarwal and co-authors found that companies that made soft money donations to parties or donations to Section 527 committees from 1991 to 2004 (accounting for roughly 11 percent of the universe of U.S. publicly traded firms) tended to be large, slowly growing firms that had more free cash than other firms but spent less on research and development or business investments. Their donations were negatively correlated with long-term firm-specific stock market performance.[29]

Aggarwal et al. also found that better corporate governance – including better board structure, lower CEO compensation, and the presence of large shareholders to monitor corporate behavior – tended to be associated with less political activity. But, as with Coates's research, the negative relationship between political activity and shareholder returns persisted even after controlling for more general corporate governance factors, suggesting that policies limiting or disclosing political activity could further improve shareholder value.

[27] John C. Coates IV, "Corporate Governance and Corporate Political Activity: What Effect Will Citizens United Have on Shareholder Wealth?" Harvard Law and Economics Discussion Paper No. 684, 2010. Available at http://ssrn.com/abstract=1680861.

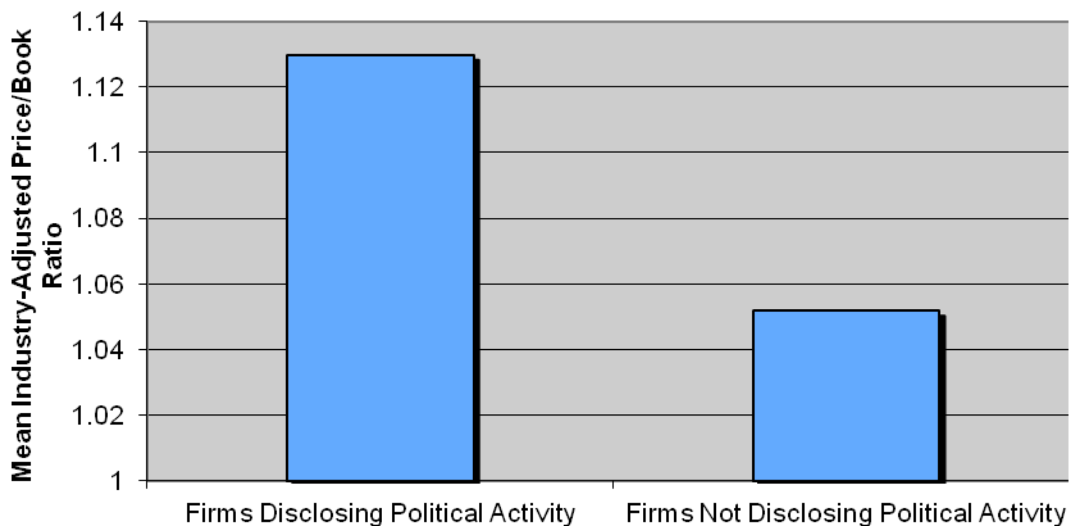
[28] John C. Coates IV, "Corporate Political Activity, Corporate Governance and Corporate Value Before and After Citizens United" (2011). Working paper available from the author.

[29] Rajesh K. Aggarwal, Felix Meshke, and Tracy Wang, "Corporate Political Donations: Investment or Agency?" (January 2011). Working Paper. Available at http://ssrn.com/abstract=972670.

What about disclosure? Is it true that companies that disclose their political activities are worse off for doing so? To answer this question, Coates and Taylor Lincoln[30] conducted a study analyzing the market valuations and other financial aspects of 80 S&P 500 companies that have adopted policies calling for disclosure of their electioneering activities.[31] In particular, Coates and Lincoln compared the price/book ratios of those companies with similarly sized S&P 500 companies in the same industries. (Price/book ratios are commonly used valuation metrics that are more stable than year-to-year earnings. Price/book ratios reflect the market's evaluation of whether a company as currently managed is using shareholder resources well, compared to similar firms.)

Because many factors influence price/book ratios, Coates and Lincoln controlled for company size, leverage, research-and-development activities, and three-year sales growth, as well as whether the companies had PACs that made donations in 2010. The final variable, whether companies had active PACs, is necessary because companies without active PACs do not tend to have political disclosure policies. Coates and Lincoln found that politically inactive companies tend to have higher price/book valuations than companies that are politically active. Therefore a non-disclosing politically inactive firm could be expected to have a higher valuation than a disclosing politically active firm.

Coates and Lincoln found that companies with policies calling for political disclosure had a 7.5 percent higher industry-adjusted price/book ratio than other firms as of year-end 2010. The Figure below depicts the findings.



[30] John Coates and Taylor Lincoln, *Fulfilling Kennedy's Promise: Why the SEC Should Mandate Disclosure of Corporate Political Activity* (September 2011), available at: http://www.citizen.org/documents/Fulfilling-Kennedys-Promise.pdf

[31] About 85 companies have adopted some variation of a policy provided by the Center for Political Accountability in which they have pledged to disclose electioneering activities. Available at http://www.politicalaccountability.net/index.php?ht=d/sp/i/869/pid/869.

Given data limitations, Coates and Lincoln cannot claim that disclosure policies cause the higher price/book ratios. The study only shows that they these policies are correlated in the S&P 500, and the companies that have adopted pro-disclosure policies are, on the whole, more valuable. Nevertheless, the data from 2010 are inconsistent with the idea that disclosure policies harm politically active companies as a general matter, and they are consistent with the idea that well-managed companies responsive to shareholder concerns tend to be more highly valued than other companies.

Conclusion: Require Publicly-Traded Companies to Disclose Political Spending; Give Shareholders the Right to Sign Off on Political Budgets

The Supreme Court has thrust upon us an entirely new political landscape in its *Citizens United* decision – a landscape that this nation has not been prepared to deal with both in terms of campaign finance law and responsible corporate governance. The widely-perceived dysfunctional Federal Election Commission has thus far tied the hands of the federal government when it comes to requiring transparency of campaign financing, with no resolution in sight. The FEC's failures have resulted in a startling decline of disclosure of the sources of political expenditures, especially from the largest new source of campaign money – corporations.

The new and growing role of undisclosed corporate expenditures in American elections calls upon the Securities and Exchange Commission to step up to the plate, regardless of any actions that may or may not come from the FEC. The *Citizens United* decision poses more than a campaign finance problem; it has elevated to whole new levels the problem of responsible corporate governance in the decisionmaking process of corporate political expenditures.

Shareholders have been concerned about the business sense of corporate political spending for some time – concerns that have become vastly more pronounced as the scope and nature of corporate political activity has expanded. Current and ongoing research on the effects of corporate political spending on overall value substantiate those concerns. In just the last two years, the number of shareholder resolutions calling for enhanced transparency and oversight of political spending decisions has far outpaced all previous years, reaching 62 resolutions in 2010 and 101 resolutions in 2011.

At the same time, many business executives are expressing concern over the proper role of corporations in the political arena. Surveys of top business leaders show considerable support for transparency and oversight, which is reflected in a notable trend toward voluntary policies governing political activities. These voluntary policies, however, are not a complete solution. They are often inconsistent, unenforced and disparate between economic sectors.

Congress is debating sweeping legislation that would require transparency and a shareholder vote on political budgets, based on the established model in the United Kingdom, which Congress should proceed with. But it is imperative that the SEC move forward with regulatory actions within its jurisdiction to lay the groundwork for responsible corporate governance in this new era. The Securities and Exchange Commission should issue rules that ensure comprehensive disclosure of political activities by publicly traded companies and facilitate shareholder efforts to adopt bylaws requiring that managers get their sign-off on political budgets.

- **On disclosure**. The SEC should require publicly traded companies to disclose to shareholders and the public their expenditures used for political purposes, including donations to trade associations that help finance electioneering and/or lobbying activities. The SEC rule should require companies to obtain from their trade associations an enumeration of the amount of their contributions used for non-deductible political activities (defined broadly as lobbying and electioneering) as well as details on the amount of money used specifically for electioneering. Electioneering expenditures could be calculated relatively simply by taking the amount the third party group spent on activities recognized by federal election law, such as on "independent expenditures" and "electioneering communications."

Distinguishing between electioneering and lobbying spending is important because of their distinct characters. Unlimited corporate spending has clearly strengthened the arm of corporate lobbyists, who often determine how a corporation spends its political dollars. Full disclosure of both electioneering spending and lobbying expenditures is imperative. The Supreme Court carved out a special place for disclosure of electioneering spending as well as lobbying expenditures in previous court rulings, including the *Citizens United* decision and the *United States v. Harriss* decision.[32] .

- **On shareholder sign-off**. We applaud the consistent stances of the SEC in making clear that shareholders have the right to use the company's proxy statement to propose and (if approved by a majority of shareholders) to adopt by-laws requiring that any publicly traded company's political spending budget – including electioneering and lobbying expenditures – be approved by a majority vote of all shareholders in advance of any political spending. The SEC has recognized by taking no action in cases like the proposal filed by Northstar Asset Management on the Home Depot proxy, that shareholders have the authority to adopt such procedures for overseeing corporate spending decisions. This type activity is already a well-established form of responsible corporate governance, and has been demonstrated as a workable and non-intrusive right for shareholders in the United Kingdom over the last decade.

For these reasons, we encourage the Securities and Exchange Commission to take up the Petition for Rulemaking (File No. 4-637) and promulgate reasonable corporate governance regulations addressing the new phenomenon of unlimited and undisclosed corporate political spending in American elections.

Respectfully Submitted,

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)

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[32] United States v. Harriss, 347 U.S. 612 (1954).

Citizen Works

Coalition for 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, co-author, Corporate Governance

N.C. Center for Voter Education

Ohio Citizen Action

Public Campaign

Public Citizen

Sunlight Foundation

U.S. Chamber Watch

U.S. PIRG

Wisconsin Democracy Campaign