

July 18, 2016

Mary Jo White  
Chair, Securities and Exchange Commission

Keith Higgins  
Director, Corporate Finance Division, Securities and Exchange Commission

Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549  
Re: Disclosure Effectiveness Review

Dear Chair White and Director Higgins:

We, the undersigned organizations, welcome the opportunity to comment on the concept release on regulation S-K disclosure requirements for U.S. public companies. The Securities and Exchange Commission's (SEC) review was performed as a part of its ongoing assessment of disclosure undertaken to benefit investors and registrants. We agree with the objective of the disclosure review (hereinafter, "the review")—to improve disclosure --and appreciate the agency's focus on providing critical information concerning public companies to investors via required disclosures.

The Corporate Reform Coalition is a group of more than 85 organizations including institutional and retail investors, corporate governance experts, securities attorneys, civil society organizations, and more. As a group we are focused on the evolving need of investors to more fully understand the political activities (and the risks those activities present) of companies they invest in.

Undisclosed corporate political spending can encourage behavior that poses legal, reputational and operational risks to companies and systemic risks to the economy. It is from that viewpoint that some of our members and allies offer our perspective on a subset of the questions raised by the Corporation Finance division in the concept release. Our coalition has a particular focus on the questions raised about materiality, emerging issues, and potential new disclosures which investors have widely requested.

The opportunity to weigh in on and help improve the effectiveness of the disclosure system is an important one for both investors and the public. The outcomes of the review and the guidance and rulemaking processes that begin as a result of it should result in clear recommendations reflective of the broad-based demands of investors occurring due to the changing environment around corporate political spending and other risk-related topics.

The resources of the SEC are required to write numerous rules, police the markets, and react to changes in company structure. In order to oblige its mandate to protect investors the SEC must require material disclosures of critical business information for investors, and this includes being able to react quickly to the changing practices and priorities of public companies.

#### Materiality

The concept of materiality is used throughout the federal securities laws. The Supreme Court has defined materiality as information where there is a substantial likelihood that a reasonable investor would consider the information important in deciding how to vote or make an investment decision.

As the concept release notes on page 47, commenters to the agency shared their perspective that the investor community is diverse, and so quite obviously what is material to some may not be material to all.

**In the concept release, question 16 stated:**

**Commenters have suggested that disclosure should be written for a more sophisticated investor than current disclosure appears to contemplate, and that tailoring disclosure to less sophisticated investors contributes to excessive disclosure. Should our disclosure requirements be revised to address these views? If so, how could we revise our disclosure requirements, and which requirements should we revise, to encourage more appropriately targeted of information required or whether the optimum should be achieved on a mandatory or voluntary basis. The Sommer Report also stated that market forces alone are insufficient to cause all material information to be disclosed. Other studies have noted the limitations of the efficient market theory.**

**If we revised our disclosure requirements to address these views, would there be any harm or costs to investors?**

It is our opinion that being inclusive in required disclosures gets us closer to the SEC's mandate of providing the necessary and "important information for investment decisions" as described by the court, to all investors. We do not think that tailoring disclosures for a more sophisticated investor should be a priority focus for an agency tasked with protecting and advising the gamut of the investing community, nor do we think that "excessive disclosure" is prevalent. As was stated by the American Federation of Labor and Congress of Industrial Organizations in their comment--when information is useful to retail investors but not useful to institutional investors or vice versa, disclosure should still be required. No segment of the investor community is more or less entitled to access to all the information they deem necessary and material, and the materiality standard must be applied to every group of investors, inclusive of larger and smaller entities and interests. Broad based disclosure requirements improve transparency and builds public trust, confidence and understanding of capital markets by all investors.

One obvious example of an emerging material issue and disclosure need can be found in our coalition's focus—corporate political activity. Due to activity in the area the information has become increasingly relevant to investors. Professor Michael Hadani's study of the materiality of political spending concluded, "that firms' political spending, in particular contributions to policy makers, at best has an insubstantial impact on their bottom line and more often results in a negative effect on financial performance. Such an eventuality warrants action from the SEC to require increased transparency, oversight and shareholder say over funds' political expenditures."<sup>1</sup>

The Hadani paper includes empirical analysis of the materiality of political spending disclosures to the investing public. Specifically, the analysis includes both politically and non-politically active firms and corrects for possible reverse causality issues—that is the possibility that firm's prior performance and other firm characteristics explain corporate political expenditures. The data includes approximately 1110 small-, mid-and large cap S&P firms, both politically and non-politically active, with data covering 1997 to 2008, comparing firms' PAC contributions, among

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<sup>1</sup> Professor Michael Hadani, SEC comment to file 4-637 submitted 10/13/2011, <https://www.sec.gov/comments/4-637/4637-8.pdf>.

other forms of political expenditures (such as lobbying or having politically tied board directors) to those who did not have such spending and the impact of such contributions on firms' financial outcomes, which include firms' annual market value and firms' return on sales. This analysis has the advantage of reviewing a larger sample than other studies which focused on either the S&P 100 or the S&P 500. As such, this analysis captures the largest publicly traded firms in the U.S. The analysis also compares firms' annual spending on political activities to their cumulative (or repeated) political spending over the 11 years of data and the impact these two patterns of spending have on firms' financial outcomes. The paper's regression analysis reveals that PAC expenditures and cumulative PAC expenditures have a statistically significant negative affect on firms' market value, both when examining their year to year PAC expenditures and also when examining their cumulative, 11 years, PAC expenditures. At the same time, PAC and cumulative PAC expenditures have no statistically significant effect on firms' return on sales.

***Taken together, the large scale analysis results indicate that firms' donations to politicians are not effective in promoting firms' outcomes and indeed may harm them***

### ESG Disclosure

The concept release discusses at length the potential need for new environmental and social disclosures. The release notes that in 1975 the Commission concluded that it would require such disclosure relating to social and environmental performance "only if such information...is important to the reasonable investor – material information." As stated above in our discussion of materiality, our view is that it is better to be more inclusive when it comes to required disclosures, and to err on the side of providing information if a segment of investors strongly requires it, even if not all will use it.

Using that rubric, the issue of political spending disclosure has already passed a clear threshold of significant demand by investors through the volume and diversity of the demand for the information. In addition to the 1.2 million comments received to the petition calling for this rulemaking, as is noted on page 208 of this concept release, the agency received many letters to the disclosure effectiveness review process recommending that the Commission adopt a rule requiring disclosure of political spending.

***Of the 102 non-form comments received to the disclosure effectiveness review process, 84% of them (86) call for the agency to work on this rule.*** There are an additional 9718 form comments which do the same. Such a high volume should not be ignored and the issue should be given serious consideration and effort by the agency.<sup>2</sup> The agency is currently allowed to do work on this rulemaking, though it cannot move it to finalization until the next budget cycle due to a rider attached to the FY16 omnibus budget package. The preliminary work on this rule should begin now.<sup>3</sup>

As the Commission notes in the concept release, the role of sustainability and public policy information in investors' voting and investment decisions is evolving, and many investors are increasingly engaging on ESG matters. Political spending and lobbying disclosure are issues that investors consistently choose to engage on, either through petitioning the SEC or dialoging with

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<sup>2</sup>Comments to the record assessed on 5/3/16. <https://www.sec.gov/comments/disclosure-effectiveness/disclosureeffectiveness.shtml>.

<sup>3</sup> Professor John Coates, Harvard University, 12/17/2015, <http://www.uspirg.org/sites/pirg/files/resources/SEC%20Rider%20Legal%20Opinion%202015-12-17.pdf>.

individual companies through the shareholder resolution process. We'll discuss this engagement further below in answer to another set of agency questions.

**The agency requested input on the issue of requiring more disclosure in the following manner in the concept release, question 216 states:**

**Are there specific sustainability or public policy issues that are important to informed voting and investment decisions? If so, what are they? If we were to adopt specific disclosure requirements involving sustainability or public policy issues, how could our rules elicit meaningful disclosure on such issues? How could we create a disclosure framework that would be flexible enough to address such issues as they evolve over time? Alternatively, what additional Commission or staff guidance, if any, would be necessary to elicit meaningful disclosure on such issues?**

**217. Would line-item requirements for disclosure about sustainability or public policy issues cause registrants to disclose information that is not material to investors? Would these disclosures obscure information that is important to an understanding of a registrant's business and financial condition? Why or why not?**

**218. Some registrants already provide information about ESG matters in sustainability or corporate social responsibility reports or on their websites. Corporate sustainability reports may also be available in databases aggregating such reports. Why do some registrants choose to provide sustainability information outside of their Commission filings? Is the information provided on company websites sufficient to address investor needs? What are the advantages and disadvantages of registrants providing such disclosure on their websites? How important to investors is integrated reporting, as opposed to separate financial and sustainability reporting? If we permitted registrants to use information on their websites to satisfy any ESG disclosure requirement, how would this affect the comparability and consistency of the disclosure?**

As mentioned, we believe that the specific policy issue of corporate political spending is an ESG topic with which the agency should move forward. We believe that a successful agency is one that is flexible to react to a changing environment and to new demands by investors.

Our organizations have a keen interest in the agency proceeding with rulemaking requiring disclosure of political spending information from public companies. Reflecting the intense investor interest in enhanced political spending disclosure, the rulemaking petition filed at the Commission on political spending disclosure by 10 prominent securities law professors has attracted a record level of support for SEC rulemaking. As mentioned above, 1.2 million comment letters have been submitted to support the rule, with the vast majority in support of increased disclosure. Those in favor go far beyond retail investors to include institutional investors, State Treasurers, Members of Congress, Former SEC Chairs and Commissioners, the founder of the major mutual fund-Vanguard Corporation, major endowed foundations, public pension funds, and more.

As mentioned above, many have made the arguments for the materiality of this information to shareholder value. A 2012 study by Harvard Law Professor John C. Coates IV<sup>4</sup> found that "in most

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<sup>4</sup> *Corporate Politics, Governance, and Value Before and After Citizens United*, John C Coates, Harvard Law School, 7/6/12, Journal of Empirical Legal Studies, [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2128608](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2128608).

industries, political activity correlates negatively with measures of shareholder power, positively with signs of agency costs, and negatively with shareholder value.” Professor Coates’ findings are supported by the subsequent empirical study<sup>5</sup> mentioned above published in the *Strategic Management Journal* by Michael Hadani and Doug Shuler, which found that cumulative political investments tend to have a deleterious effect on both market and accounting performance over time.

In the years since the Supreme Court decision *Citizens United vs. FEC*, shareholders concerned about a lack transparency and the impact of secret political spending on their investments have filed hundreds of shareholder resolutions calling for companies to disclose this information. Political spending disclosure resolutions have become one of the most frequently filed type of resolution in the ESG space, with nearly 100 such resolutions filed this spring.<sup>6</sup> The votes consistently get a strong showing (in the 30-40% range) and generally receive majority winning votes when the major mutual funds (which generally abstain) are removed from the calculation.

The Supreme Court has stated that complete real-time disclosure of public company political spending should allow shareholders to “determine whether their corporation’s political speech advances the corporation’s interest in making profits.” Corporations use treasury funds to make a variety of political expenditures, including direct contributions to state-level political candidates, political parties, judicial races, ballot initiatives, and a range of tax-exempt entities such as trade associations and 527 organizations that engage in political activity. Corporations may also contribute funds to finance political advertising on public policy issues or to advocate for or against the election of particular candidates.

These activities are subject to a variety of state and federal laws. But because there are no current rules that require that companies disclose this spending to their shareholders, it is essentially impossible for an investor to obtain a full picture of any individual company’s political spending unless the company chooses to disclose. Without an SEC rule requiring full disclosure for all public companies, shareholders have no uniform means to monitor these activities, or assess the risks of corporate political spending. Voluntary disclosure has led to a patchwork of understanding which makes it impossible for investors to manage, and potentially mitigate, the full range of risks presented by corporate political spending, and to the question in the concept release, this is not a sufficient mechanism for any reasoned investor to make investment decisions. Nor would disclosures made on individual corporate websites suit the need of shareholders, as without a uniform requirement for which types of spending and how to disclose it, investors will be faced with a time consuming process and insufficient information to compare companies and make choices.

From an issuer’s perspective, a disclosure mandate would level the playing field by relieving concern that disclosing activities could disadvantage the issuer’s standing or competitiveness.

Any new disclosure requirements which come from the S-K concept release and the review should be structured to capture the evolving role of corporate money in politics, and the myriad entities that it can move through, by creating a structure that clearly defines the entities to which giving money would trigger the transparency. The rule could be easily structured to do so, and as stated

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<sup>5</sup> *In search of El Dorado: The elusive financial returns on corporate political investments*, Michael Hadani and Douglas Schuler, *Strategic Management Journal*, Volume 34, Issue 2, pages 165–181, 2/5/2013, <http://onlinelibrary.wiley.com/doi/10.1002/smj.2006/abstract>.

<sup>6</sup> *Proxy Preview*, from As You Sow, the Sustainable Investments Institute, and Proxy Impact, 2016, <http://www.proxypreview.org/>.

above, we do not believe that providing this information so-demanded by so many, would in some way obscure other disclosure data points which are already required. This information is material, and those that want to use it should be able to do so.

### Conclusion

We appreciate that the agency has opened the process around the review for comment. We call on the agency to live up to the mandate found in the agency's mission, "to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation." If the agency is true to this directive, then we have complete confidence that the eventual rulemakings and guidance that come out of the review process and the affiliated concept papers will work to provide comprehensive information on corporate political spending to investors.

Sincerely,

The Center for Media and Democracy

Citizens for Responsibility and Ethics in Washington  
(CREW)

Common Cause

Communications Workers of America (CWA)

Harrington Investments, Inc.

International Brotherhood of Teamsters (IBT)

Interfaith Center on Corporate Responsibility

New Progressive Alliance

Pax World Management, LLC

Public Citizen

Sunlight Foundation

The Sustainability Group at Loring, Wolcott, &  
Coolidge

U.S. Public Interest Research Group (U.S. PIRG)

US SIF: The Forum for Sustainable and Responsible  
Investment

Union of Concerned Scientists

Voices for Progress

Walden Asset Management

West Virginia Citizen Action Group

Women's Donors Network