



September 2, 2014

Via electronic mail: rules-comment@sec.gov

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

Re: Comment on Rule Making Petition 4-637

Dear Ms. Murphy:

On behalf of Demos we respectfully submit this comment supporting the petition requesting a rulemaking to require public companies to disclose to shareholders the use of corporate resources for political activities. Demos is a public policy organization that works at the intersection of political and economic inequality. Demos has extensive legal and policy expertise on the subject of transparency and accountability for the use of money in politics, and has written extensively regarding its necessity, utility, and constitutionality.¹

It is the responsibility of the SEC to act to prevent further failure of regulatory responsiveness to the changed circumstances brought about by the Supreme Court's 2010 decision in *Citizens United v FEC*. Millions of dollars from publicly traded companies have already been spent in federal and state elections; this is known as a result of both voluntary and inadvertent disclosures. More than \$300 million was spent in the 2012 elections by dark money groups who hide the identity of their donors, evading transparency and shirking accountability. Many millions of dollars in undisclosed corporate money may have already been spent on politics.²

The Commission has the authority and responsibility to move forward in promulgating a rule to require disclosure of corporate political spending by public companies to protect investors and the market from risky secret corporate political spending and to vindicate investors' right to

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information necessary to exercise accountability in this arena. We urge the Commission to do so for the reasons set forth in the petition and in the one million comments the Commission has received supporting the rule.

I. Introduction

One of the enduring lessons of the Great Depression and the Great Recession is that the most effective capital market in the world cannot function without appropriate oversight.

Regulating in the public interest and to protect investors is at the core of the mission of the Securities and Exchange Commission. The Securities and Exchange Commission (SEC) was given broad authority to protect the integrity of the markets and its participants, and it has clear statutory authority to determine what information companies must disclose to their shareholders.

“We note, first, that Congress, in the 1933 and 1934 Acts, has seen fit to delegate broad rulemaking authority to the SEC. . . . The SEC, charged with swiftly and effectively implementing this national policy, was necessarily given very broad discretion to promulgate rules governing corporate disclosure. The degree of discretion accorded the Commission is evident from the language in the various statutory grants of rulemaking authority.” *Natural Res. Def. Council, Inc. v. Sec. & Exch. Comm'n*, 606 F.2d 1031, 1050 (D.C. Cir. 1979).

Section 14(a) of the Securities Exchange Act of 1934 empowers the SEC to prohibit the solicitation of proxies “in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.” 15 U.S.C. Sec. 78n. Courts have found that “[t]he Commission is given complete discretion . . . to require in corporate reports only such information as it deems necessary or appropriate in the public interest or to protect investors.” *Natural Res. Def. Council, Inc.*, 606 F.2d at 1051 (quoting S.Rep.No. 792, 73d Cong., 2d Sess. 10 (1934)).

In *Citizens United v FEC* the Supreme Court allowed business corporations to spend money from their general treasuries to support or oppose political candidates, which had been previously banned. But the Supreme Court assumed that all newly allowed political spending by publicly traded corporations from their corporate treasuries would be disclosed to shareholders and the public. In his decision, Justice Anthony Kennedy wrote:

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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.”³

In other words, Justice Kennedy relied on transparency for corporate political spending to assuage concerns about oversight and accountability for corporate political spending. Yet there are currently no federal rules that require a publicly traded corporation to disclose their use of shareholder money for political activities.

In 2011, a bi-partisan committee of law professors, The Committee on Disclosure of Corporate Political Spending, filed a petition calling on the SEC to require public companies to disclose their corporate political activities. They wrote “[s]hareholders need to receive such information for markets and the procedures of corporate democracy to ensure that such spending is in shareholders’ interest,”⁴ but noted that “[m]ost political spending remains opaque to investors in most publicly traded companies.”⁵

In 2012, the SEC indicated on its 2013 regulatory agenda that the Division of Corporation Finance was considering “whether to recommend that the Commission issue a proposed rule to require that public companies provide disclosure to shareholders regarding the use of corporate resources for political activities.”⁶ But the Commission failed to include the rulemaking on its 2013 agenda without any formal explanation, amid reports of fierce political pressure to ignore the issue despite its merits.⁷

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II. A Political Disclosure Rule Falls Well Within the Commission’s Authority and History

A. The Commission has the Authority to Require Disclosure of Corporate Political Spending

The Commission has broad authority to regulate the information contained in proxy statements and other corporate disclosures when doing so is in the public interest or in the interest of investors. As one appellate court has observed, Section 14(a) “embodies a policy of broad disclosure designed to protect the basic right of corporate suffrage.” *Allen v. Lloyd's of London*, 94 F.3d 923, 931 (4th Cir.1996) (citing *J.I. Case Co. v. Borak*, 377 U.S. 426, 431-32 (1964)). Fundamental to the right of corporate suffrage is disclosure of information concerning how corporate funds are being expended, particularly when, as in the case of political spending, the expenditures are not directly related to the corporation’s business activities.

Under the Securities Laws, the public interest is a consideration equal to the interest of investors, and when considering regulations concerning corporate disclosure, the Commission must take seriously its obligation to regulate in the public interest. Under Section 14(a) of the Securities Exchange Act of 1934 (the “Exchange Act”), for example, the Commission may issue regulations governing the form and content of proxy statements that, in the judgment of the Commission, are “necessary or appropriate in the public interest or for the protection of investors.” 15 U.S.C. § 78n(a). Other provisions of the Exchange Act, the Securities Act of 1933 (the “Securities Act,” and together with the Exchange Act, the “Securities Laws”), and other statutes providing regulatory authority to the Commission also require the Commission to consider the public interest when regulating in the area of corporate disclosure. The mandate to regulate in the public interest requires the Commission to consider the social and economic context in which the Securities Laws were passed. In bringing about the Great Depression, market manipulation and a lack of corporate transparency impacted more than the corporations themselves and their shareholders – they also impacted the economic fortunes of a broad swath of the nation’s population, from workers to small business owners. When Congress mandated that the Commission regulate in the public interest, it gave the Commission the power to mitigate these collateral effects of corporate self-dealing, as well as direct harm to shareholders.⁸

More recent amendments to the Securities Laws require the Commission to consider, under the heading of the public interest, the promotion of “efficiency, competition, and capital

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formation” as part of its regulatory process. See 15 U.S.C. § 78c(f); 15 U.S.C. § 77b(b). While this requirement is often understood to oblige the SEC to engage in a cost-benefit analysis of regulations it proposes, *e.g.*, *Nat’l Resources Defense Council v. SEC*, 606 F.2d 1031, 1051 (D.C. Cir. 1979), the interests reflected in these provisions are broader than that. The Commission’s mandate to promote competition in its regulatory activities, for example, requires the Commission to take into account the impact of its rules not merely on the regulated entity or its shareholders, but on the large economic environment in which they operate. *Friedman v. Salomon/Smith Barney, Inc.*, 313 F.3d 796, 800 (2d Cir. 2002) (explaining that 15 U.S.C. § 78c(f) gives the SEC authority to regulate in the area of antitrust). A political disclosure rule will further both the rights of shareholders and the public interest more broadly.

B. The Commission has a History of Regulating Political Spending

1. The SEC has long recognized its role as the agency responsible for regulating the nexus between political spending and market protection

The SEC has been exercising jurisdiction in this area for forty years. The Commission has acted in the past to protect the integrity of the market where it intersected with campaign finance and political spending in several other areas, and it should do so now to address the new threat of secret corporate political spending. These examples illustrate the actions taken by the Commission to protect investors and the market from the vicissitudes of political spending by corporate actors.

a. Addressing the Corporate Campaign Finance Scandal of Watergate and the FCPA

Watergate led to a major corporate campaign finance scandal, and it caused the SEC to play a leading role in regulating political spending by market actors. When the SEC looked into the corporate treasury funds that had been illegally directed to President Nixon’s 1972 reelection campaign, it found that hundreds of American companies had made illegal payments to both of the major American political parties as well as to politicians abroad. These payments were made from secret political slush funds, described by then-SEC Commissioner A.A. Sommer, Jr. as “substantial pools of money that had been sucked out of the corporate accountability process.”⁹

Transparency and better reporting was one of the necessary solutions, and the SEC was instrumental in requiring more corporate transparency with regard to payments to politicians. As

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a result, hundreds of companies disclosed the existence of their secret political funds and questionable foreign and domestic political payments. These efforts led to the passage of the Foreign Corrupt Practices Act (FCPA), which in addition to banning domestic corporations from bribing foreign officials or making political contributions abroad with corrupt motives, also amended the Securities Exchange Act of 1934 to require registered issuers to keep detailed and accurate books and accounts to record corporate transactions. 15 U.S.C. § 78m(b) (2010).
Banning Pay to Play in the Municipal Bond Market

In the 1990s, the SEC found that contracts in the profitable municipal bond market were being awarded to investment companies that made contributions to the state and local officials responsible for the contract placement decisions. The SEC stepped in to stop this practice of pay to play through the Municipal Securities Rulemaking Board’s Rule G-37, which restricts municipal broker-dealers from doing business with an issuer if they have made more than a de minimis contribution to the issuer.¹⁰

The SEC exercised its authority because rigging the awarding of government contracts compromised the integrity of the bond market. As described by Professor Ciara Torres-Spelliscy, the SEC’s then-Chair Arthur Levitt Jr. “was gravely troubled that the municipal bond market wasn’t functioning as a normal market. Rather, the award of lucrative underwriting contracts seemed to flow not necessarily to the best talent, but rather to the most politically connected.”¹¹ She quotes former Counsel to the SEC Jon B. Jordan explaining that “dealers and underwriters use political contributions to the campaigns of elected officials in order to solicit municipal bond business for their firms. These contributions are specifically directed to the campaigns of elected officials who will in turn favor those firms that contributed to them when it is time to select dealers for municipal bond work.”¹² These practices created market inefficiencies; academics found the misallocated contracts had “statistically significant and economically large” higher fees, and interpreted “these higher fees as the quid pro quo for political campaign contributions.”¹³

Significant similar concerns arise in the context of secret corporate political spending. When the D.C. Circuit Court of Appeals upheld the constitutionality of Rule G-37 it explained the parallel between the government’s interest in defending the integrity of the market and the political system, saying that while “here the effort is to safeguard a commercial marketplace. . . . [i]n every case where a quid in the electoral process is being exchanged for a quo in a particular market where the government deals, the corruption in the market is simply the flipside of the

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electoral corruption.”¹⁴ The Court further underlined the link between regulating political spending and promoting a free market, noting that “the link between eliminating pay-to-play practices and the Commission’s goals of ‘perfecting the mechanism of a free and open market’ and promoting ‘just and equitable principles of trade’ is self-evident.”¹⁵

c. Banning Pay to Play in Pension Fund Management

As recently as 2010, the SEC acted to stop pay to play in the public pension fund market by promulgating Rule 206(4)-5, which restricts campaign contributions from investment advisers to the public officials responsible for making investment decisions for public pensions.¹⁶ Several elected officials were jailed as a result of pay-to-play scandals, including NY Comptroller Alan Hevesi. These schemes involved fraud on both the political system and the market, since the success of these investment advisers was due not to their skill but their political spending. The Director of the SEC’s Division of Investment Management explained that the SEC rule was needed because “[p]ay-to-play serves the interests of advisers to public pension plans rather than the interests of the millions of pension plan beneficiaries who rely on their advice. The rule . . . help[s] ensure advisory contracts are awarded on professional competence, not political influence.”¹⁷

Then-Chair Mary Schapiro explained the pernicious systemic effects of pay-to-play corruption, saying, “An unspoken, but entrenched and well-understood practice, pay to play can also favor large advisers over smaller competitors, reward political connections rather than management skill, and — as a number of recent enforcement cases have shown — pave the way to outright fraud and corruption. . . . Pay to play practices are corrupt and corrupting. They run counter to the fiduciary principles by which funds held in trust should be managed. They harm beneficiaries, municipalities and honest advisers. And they breed criminal behavior.”¹⁸

Recognizing that campaign spending can have a distorting impact on the markets, the Commission was right to act to protect the integrity of the market by promulgating the Rule 206(4)-5. The Commission should take similar action to mandate disclosure of direct and indirect political spending, because secret corporate political spending is a threat to investors, the market, and the public, and transparency for corporate political spending is in their interest.

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III. Requiring Disclosure of Corporate Political Spending Is in the Interest of Investors, the Markets, and the Economy.

In *Citizens United* the Supreme Court noted that disclosure of corporate political expenditures “can provide shareholders . . . with the information needed to hold corporations . . . accountable for their positions.” 558 U.S. at 370. Disclosure, according to the Court, would allow shareholders to “determine whether their corporation’s political speech advances the corporation’s interest in making profits.” *Id.* Currently, however, shareholders cannot meaningfully exercise this most fundamental right of corporate democracy with regard to political spending because the information needed to hold corporate management accountable is not required to be disclosed.

A. Investors Have a Right to Know and It Is In Their Interest for Corporations to Disclose Information About Their Corporate Political Spending.

It is a basic precept in American securities law that shareholders should be given the information they need to evaluate the companies in which they invest.¹⁹ Shareholders have a right to know how the executives entrusted with their investment dollars are spending corporate funds so that they can make informed investment decisions and effectively exercise their right of corporate suffrage. In the absence of a rule requiring disclosure of corporate political spending, however, there is no comprehensive or consistent requirement that companies disclose their political spending, and thus, this principal of corporate democracy continues to be frustrated.

According to proxy advisory service Glass Lewis, political donations “have the potential to negatively affect the company.”²⁰ Undisclosed political activity is material for a number of reasons, most importantly because it subjects investors to a range of unknown risks. Glass Lewis writes that “we believe that companies should disclose as much relevant information as possible to help shareholders assess whether political spending activities are aligned with a company’s policy and best interests and that companies should carefully consider the inherent reputational risks associated with supporting candidates or trade associations whose social positions can be interpreted as contrary to company values.”²¹

The lack of information on corporate political spending can harm investors in a number of ways, and the Commission can and should alleviate these harms by adopting a political disclosure rule.

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First, lack of disclosure of corporate political activity creates asymmetries in information—a micro-level form of market failure—which increases agency problems, creating opportunities for executives to engage in political activity that serves their own interests at shareholder expense. Shareholders—and often directors—are unable to hold executives accountable for their political activities if these activities remain hidden to them. Disclosure of corporate political spending would help to mitigate this inherent moral hazard by diminishing the monitoring costs for investors.²²

The principal-agent problem is exacerbated in the context of corporate political spending, where the interests of management and shareholders may very well not be aligned. Companies frequently don't even have an internal policy regarding risk assessment or a requirement for board approval for using corporate resources for political activities.²³ A recent study found that poor corporate governance is correlated with larger political donations, suggesting that political donations are “symptomatic of agency problems within firms.”²⁴ Another report found that companies that contribute more money in politics are less likely to disclose.²⁵ Without transparency and accountability, management is free to distribute company resources for political ends according to its own personal proclivities. There is a risk that political spending will advance the interests of an individual manager rather than the company, or executives at the expense of shareholders (for example, funding lobbying against changes to corporate governance laws that currently shield executive conduct, including political activity, from shareholder scrutiny).

Second, investors are unable to make informed investment decisions when corporations may be publicly professing support for one set of policies or values, while secretly supporting a different position. Companies may make public statements on one side of an issue while secretly lobbying and spending to support public policy on the opposite side of the issue. Such corporate double-dealing is not uncommon. For example, a 2012 study by the Union of Concerned Scientists of 28 publicly traded companies' public statements and political activities concerning climate change found that “companies are more likely to express commitment or concern about climate change in venues directed at the general public, such as their corporate websites, and that companies are more likely to misrepresent climate science through their funding of outside organizations or in venues directed at the federal government, such as corporate comments in response to[EPA regulatory activity].”²⁶ Individuals investing in such companies on the basis of

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their public statements thus may not be getting what they are bargaining for, and, as explained below, they are taking on risks that have not been disclosed.

Third, information concerning corporate political activity is material to investors regardless of the dollar amount of political spending.²⁷ The Commission has long held that qualitative, as well as quantitative, information may be material for disclosure purposes.²⁸ For example, the Commission has required disclosure of corporate policies related to diversity considerations in the selection of board members. With regard to political spending, a company that advocates one position in its internal policies and public relations activity and another in its political activity risks suffering reputational harm that adversely affects investors when the political activity becomes known.

Indeed, the SEC has already implicitly recognized the materiality of information concerning political spending. When managers and directors at several corporations have sought to block shareholder proposals calling for disclosure of such spending by arguing that under Rule 14a-8, the proposals either (i) are vague or (ii) are ordinary business decisions that shareholders do not need to be involved in,²⁹ the SEC has rejected both arguments. In a series of “no-action” letters, the SEC has indicated that shareholders cannot be denied the opportunity to indicate their views on a corporation’s political spending and has made clear that corporate political activity is not an ordinary business decision.³⁰

Fourth, from a quantitative perspective, information on political activity is material because it is far from certain that political spending in fact enhances shareholder value.³¹ A number of studies have shown that increased corporate political activity is negatively correlated to shareholder value and economic growth. Information that would show whether shareholder funds are being expended on activities that may be of little value to shareholders is material. Economists Russell Sobel and Rachel Graefe-Anderson find “there is little evidence that companies’ lobbying expenditures or political contributions lead to greater profits” but that “company executives appear to be the main beneficiaries of strong political connections between firms and the federal government, capturing dollars which do not flow to the rest of the firm or its shareholders.”³² A new study from the Mercatus Center at George Mason University finds that political activity, including lobbying, has no significant impact on improving the corporate bottom line. A study from Harvard Law Professor John Coates finds that, “in the period 1998-2004 shareholder-friendly governance was consistently and strongly negatively related to observable political activity before and after controlling for established correlates of that activity,

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even in a firm fixed effects model. Political activity, in turn, is strongly negatively correlated with firm value.”³³

B. Disclosure of Secret Corporate Political Spending Is Good for Markets.

One of the Commission’s primary functions is to ensure the smooth and efficient functioning of the financial markets. It does so by eliminating the inefficiencies that develop when market players are left without appropriate oversight. Disclosure will help the markets distinguish between companies that compete and win through superior products and services, and those, such as Enron, that merely appear to do so due to superior access to lawmakers, which allows them to win policies that increase their short-term profits out of proportion to any value their activities add to the real economy.

One of the most dangerous forms of market failure that arise when businesses engage in political activity is that companies will divert their resources to rent-seeking rather than putting them to productive use in the economy. Those who oppose requiring transparency for political spending assert that executives use political spending to advocate policies that benefit investors. But when the political activity amounts to rent-seeking, while it may enhance short-term returns to investors, it distorts the financial markets by causing capital to be allocated to those who have political influence rather than those who are creating value in the wider economy. When political activity is secret, it is much more likely that it will be devoted to rent-seeking.³⁴ Mandating disclosure of corporate political spending will increase efficiency in the markets, and will help ensure that capital is devoted to productive ends.

C. Disclosure of Secret Corporate Political Spending is Good for the Economy and the Public Interest.

In addition to protecting the interests of investors and the integrity of the capital markets, the Commission’s disclosure regulations serve the public interest more generally. A rule requiring disclosure of corporate political activity will serve the public interest by promoting more robust competition, increasing corporate accountability for political activities, and encouraging businesses to act as responsible actors in society.

Section 3(f) of the Exchange Act expressly requires the Commission to consider whether its regulations promote competition. Corporate political spending can be directed to reduce

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competition in the economy; the classic example of such activity is lobbying by members of a competitive industry for trade protections. Such protections by definition decrease foreign competition, allowing domestic industry freer rein to charge customers higher prices for the same or lower quality products. Corporations also seek political influence to secure competitive advantages vis-à-vis their domestic competitors. For example, Amazon for many years lobbied politicians to oppose sales taxes on internet transactions to gain a competitive advantage in relation to large brick-and-mortar retailers.³⁵ More recently, it has reversed its position and spent to support sales taxes on e-commerce transactions because such taxes will give it a competitive advantage in relation to smaller online retailers, which are now its most significant competitors. Direct lobbying can be relatively transparent, but it demonstrates the anticompetitive ways in which corporations wield their political influence. Undisclosed political activities are, if anything, likely to pursue even more anti-competitive and possibly predatory ends.

Corporate political activity can present broad concerns to the general public and significant risks to our economy. For example, a study conducted by the International Monetary Fund, drew a link between banks' political spending and heavy involvement in risky sub-prime mortgages.³⁶ Further, eighty-six percent of Americans agree that prompt disclosure of political spending would help voters, customers, and shareholders hold companies accountable for political behavior; 87 percent of Republicans, 86 percent of Independents, and 92% of Democrats agreed.³⁷ But “in order for the governance mechanisms the Supreme Court has relied upon to work effectively” this political disclosure rulemaking is necessary.³⁸

IV. The Benefits of Disclosure to Investors, the Markets, and the Economy Far Outweigh the Costs.

Under Section 3(f) of the Exchange Act, the Commission must consider the economic consequences of any proposed rule. This provision has been held to require that the Commission conduct a cost-benefit analysis of each proposed rule. In the case of a rule requiring disclosure of corporate political activity, the benefits to shareholders, the financial markets, and the broader economy are great, while the cost to companies of providing this information will be minimal, particularly when compared to the current costs to investors of gathering information about corporate political spending from existing sources—when it is even available at any cost.

As outlined in detail above, a political disclosure rule would benefit investors by reducing the potential for agency problems in relation to political activity, increasing investor understanding

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of the risks of their investments, and allowing more informed investment decisions. It would benefit the financial markets by reducing rent-seeking and enhancing the efficient allocation of capital to productive uses. It would benefit the economy by increasing competition, promoting corporate accountability, and advancing responsible corporate behavior. Moreover, “[e]xisting evidence . . . indicate that the range of potential benefits of corporate political spending disclosure – to shareholders and the market—vastly outweigh the possible costs of compliance to public corporations.”³⁹ Thus cost-benefit considerations suggest that the corporation, rather than individual investors or members of the public, is in the best position to assemble and report information concerning its political spending.

As Dr. Susan Holmberg finds, in a comprehensive report on the costs of political spending disclosure,

“it is indisputable that an SEC rule requiring companies to disclose their corporate political spending would result in only a nominal set of compliance costs to corporations engaged in political activities while creating a wide range of benefits to the economy, particularly by: generating positive externalities for corporations that are already in compliance, offsetting the large monitoring costs from a lack of transparency in corporate political spending borne by existing shareholders, providing potential investors with key information with which to make rational investment decisions, and creating incentives for self-interested corporate managers to more effectively maximize shareholder wealth.”

A. Benefits for Investors of Disclosure of Corporate Political Spending are High

Shareholders have demonstrated a strong interest in disclosure of information concerning corporate political activities. The vast majority of the over 750,000 comments submitted to the Commission in relation to this petition by individual or institutional investors, support a rule requiring disclosure. The rulemaking petition’s supporters also include six state treasurers writing as fiduciaries, John Bogle, the founder and former CEO of Vanguard, the Council of Institutional Investors and a global coalition of investors managing more than \$690 billion in assets.

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Many companies are facing shareholder demands for increased transparency around corporate political spending, which was the most frequently filed shareholder resolution in 2014 and 2013.⁴⁰ In 2013, there were 125 shareholder resolutions pertaining to political spending filed, with an average support level of 32 percent. Two of the resolutions garnered a majority vote, and 29 were withdrawn after negotiations with the company.⁴¹ Support for these proposals by mutual funds reached a new high in 2013, and levels of opposition have fallen. According to a ten-year analysis by the Center for Political Accountability, “forty large U.S. mutual fund families voted in favor of corporate political spending disclosure an unprecedented 39% of the time, on average.”⁴²

B. Costs for Companies of Disclosure of Political Spending are Low

1. Companies Already Collect Information about Corporate Political Spending

Companies must already collect information about their political spending in order to file accurate tax returns.⁴³ The proposed rule requiring disclosure would just require the further step of reporting, with minimal further costs. The petition invites the SEC to use its authority to design the disclosure rule to sit within current reporting regulations. For example, the SEC can choose to mirror the categories that the IRS lists as non-deductible political expenditures under IRC § 162(e), which companies already track. The SEC can further choose to add this disclosure to an existing reporting requirement such as those made on Form 10-K or Form 10-Q, which would mean minimal additional costs for production and distribution for companies.⁴⁴

2. Some Companies Already Disclose Information about Corporate Political Spending

Increasingly, companies are recognizing the benefits of disclosure. They’ve responded to shareholder demand and adopted policies that provide disclosure for corporate political spending. More than 118 major companies have a meaningful level of disclosure of political spending. The Center for Political Accountability found that 78 percent of companies studied improved their political spending disclosure in 2013. The CEO of Aflac has said “I want to be as transparent as possible” and Qualcomm’s CEO recognized that “increased transparency for election-related

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activities by corporations is very beneficial.” Microsoft has been disclosing its political activity since 2007, and executive Dan Bross said that “by not being transparent and open, we’d be increasing the risk to the corporation,” and a Merck executive noted that “publicizing contributions has established a sense of discipline at Merck.”⁴⁵

C. It is Overly Burdensome, if not Impossible, for Investors to Collect Information on Corporate Political Spending Independently

Shareholders are subjected to insurmountable monitoring costs where there is no mandatory requirement that a publicly traded corporation disclose its political spending. Mandatory disclosure for all public companies would diminish the monitoring costs for shareholders. According to Glass Lewis, “[s]hareholders often must search through numerous campaign finance reports and detailed tax documents to ascertain even limited information.”⁴⁶ Moreover, corporations frequently use trade associations as vehicles for political action,⁴⁷ and these indirect avenues for political spending are not required to disclose the identity of their financial contributors. A substantial amount of corporate money spent on politics is not disclosed in any public filing and would thus be hidden even from an investor who attempted to put together all the publicly available information on a company’s political spending.

D. Transparency is a Necessary Condition for Private Ordering

Many opponents of mandatory disclosure of corporate political activity contend that whether and to what extent corporations engage in such activity should be left to private ordering by shareholders and the corporations. Without disclosure of corporate political activity, however, private ordering cannot effectively regulate it. It is precisely the role of government to create the conditions—to reduce the transaction costs and set the rules of the marketplace—in which private ordering can lead to efficient and socially beneficial outcomes. Leaving it to corporations themselves to decide how much of their corporate political activity to disclose keeps transaction costs high for investors and will not promote efficient outcomes.

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Even when companies sign agreements with shareholders to disclose their political spending, it can be difficult for individual investors to enforce accountability. In a recently released report, “The Myth of Corporate Political Disclosure Exposed” the Center for Responsibility and Ethics in Washington (CREW) exposed the failure of many public companies to keep their promises on political spending disclosure.⁴⁸ They compared political spending reports from 60 companies to contributions disclosed on tax forms filed by section 527 political organizations and found significant discrepancies for more than one-third of the companies, including: Microsoft omitted nearly \$1 million in political contributions to 527 organizations from 2011-2013; Pfizer had approximately \$395,000 in discrepancies between what the company voluntarily disclosed and what 527 organizations reported in contributions; Prudential had approximately \$211,000 in discrepancies between its disclosed contributions and those disclosed by 527 organizations.⁴⁹

In 2012, Aetna was discovered to have inadvertently disclosed more than \$7 million in contributions to political groups that it had not disclosed to shareholders, despite claiming that it provided transparency and accountability for its political activity. It had hidden more than \$3.3 million in contributions to the American Action Network, which spends 66% of its budget on political ads,⁵⁰ and nearly \$4.5 million to the U.S. Chamber of Commerce.⁵¹ Ironically, Aetna has argued it was already engaging in effective disclosure in order to persuade shareholders to vote against disclosure resolutions offered by the Service Employees International Union Master Trust in 2012 and from the Unitarian Universalist Association of Congregations in 2013.⁵² In other words, Aetna used the lack of mandatory disclosure to thwart private efforts to regulate disclosure.

Leaving shareholders to fight a lopsided battle to force transparency for corporate political spending on reluctant managers or in the face of inadequate board oversight, on a company by company basis, is a dereliction of the SEC’s duty to regulate in the public interest and the interest of investors. The SEC should hold all publicly traded companies to the same standard of disclosure. Only then will shareholders have the ability to make rational investment

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decisions and help make informed choices regarding their assessment of any corporation's political spending decisions.

V. Conclusion

The Supreme Court's Citizens United decision has transformed not only our political and electoral processes, it has transformed the securities markets by allowing public companies to devote greater resources than ever to political activities without the knowledge, oversight, or consent of their shareholders. The SEC must not sit by in the face of changes that threaten investors, the market, and the public interest. To be responsible and responsive regulators, the Commission must rebuff the self-interested protestations of those who benefit from secret political spending, and fulfill its mission to protect investors and the markets by engaging in a rulemaking to require disclosure of corporate political spending.

Sincerely,



Liz Kennedy
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¹ Testimony of Liz Kennedy, Counsel at Demos Submitted to the United States Senate Committee on Rules and Administration, “Dollars and Sense: How Undisclosed Money and Post-*McCutcheon* Campaign Finance Will Affect the 2014 Election and Beyond” (Apr. 30, 2014), *available at* http://www.demos.org/sites/default/files/publications/Kennedy_TestimonyPostMcCutcheon2.pdf; Testimony of Liz Kennedy, on behalf of Demos, Submitted to the United States Senate Committee on Rules and Administration Hearing on the DISCLOSE Act of 2012, S. 2219 (Mar. 29, 2012), *available at* http://www.demos.org/sites/default/files/publications/DISCLOSE_Testimony_SenateHearing_3_29.pdf; Liz Kennedy, *Citizens Actually United: The Overwhelming, Bi-Partisan Opposition to Corporate Political Spending And Support for Achievable Reforms*, DEMOS (2012), http://www.demos.org/sites/default/files/publications/CitizensActuallyUnited_CorporatePoliticalSpending.pdf; Brief of *Amici Curiae* Communications Workers of America *et al.* in Support Appellee, *McCutcheon v. Fed. Election Comm’n*, No. No. 12-536 (U.S. 2013) (counsel for *amici curiae*), *available at* http://www.demos.org/sites/default/files/publications/mccutcheon_sc_demos_cwa_amici_brief.pdf.

² Nicholas Confessore, *S.E.C. is Asked to Require Disclosure of Donations*, N.Y. TIMES A1 (Apr. 23, 2013), *available at* <http://www.nytimes.com/2013/04/24/us/politics/sec-is-asked-to-make-companies-disclose-donations.html?pagewanted=1>

³ *Citizens United v. Fed. Election Comm’n*, 130 S. Ct. 876, 916 (2010).

⁴ Letter from the Committee on Disclosure of Corporate Political Spending to Elizabeth M. Murphy, Sec’y, U.S. Securities and Exchange Commission (Aug. 3, 2011), *at* <http://www.sec.gov/rules/petitions/2011/petn4-637.pdf>.

⁵ *Id.*

⁶ Office of Information and Regulatory Affairs, Office of Management and Budget, *Disclosure Regarding the Use of Corporate Resources for Political Activities* (Dec. 12, 2012), <http://www.reginfo.gov/public/do/eAgendaViewRule?pubId=201210&RIN=3235-AL36>.

⁷ Alec MacGillis, *Mary Jo White Doesn’t Scare Anybody*, NEW REPUBLIC (May 4, 2014), <http://www.newrepublic.com/article/117632/secs-mary-jo-white-whiffs-transparency-wall-street-dark-money>

⁸ *See, e.g., Schiller v. Tower Semiconductor Ltd.*, 449 F.3d 286, 297 (2d Cir. 2006) (SEC may issue regulations that “serve[] the public interest while at the same time leaving in place adequate investor protections”).

⁹ Ciara Torres-Spelliscy, *The SEC and Dark Political Money*, CORPORATE REFORM COALITION 8 (Jun. 18, 2013), <http://www.citizen.org/documents/sec-dark-political-money-history-report.pdf>.

¹⁰ *Self-Regulatory Organization; Municipal Securities Rulemaking Board*, SEC Release No. 34-33868; File No. SR-MSRB-94-2, 59 Fed. Reg. 17621 (Apr. 13, 1994); Torres-Spelliscy, *supra* note ix at 14; *see also*, Kathy H. Rocklen & Benjamin J. Catalano, *Overview of Restrictions on Political Activities by Investment Advisers, Broker-Dealers and Their Employees* (June 2011), PROSKAUER ROSE LLP, <http://www.proskauer.com/files/uploads/broker-dealer/Overview-Restrictions-Political-Activities-Investment-Advisers-Broker-Dealers-Their-Employees.pdf>.

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¹¹ Torres-Spelliscy, *supra* note ix at 10.

¹² *Id.* at 11 (quoting Jon B. Jordan, *The Regulation of “Pay-To-Play” and the Influence of Political Contributions in the Municipal Securities Industry*, 1999 COLUMBIA BUS. L. REV. 489, 493 (1999)).

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¹⁵ *Id.* at 945; Nicholas Reade Everett, *Kicking Back Corruption in the Public Fund Advisory Selection Process: The SEC’s Proposed Rule to Curtail Pay-to-Play Practices by Investment Advisers*, 29 REV. BANKING & FIN. L. 557, 564 (2010).

¹⁶ *Id.*

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¹⁸ Mary L. Schapiro, Speech by SEC Chairman: Opening Statement at the SEC Open Meeting (Jun. 30, 2010), <http://www.sec.gov/news/speech/2010/spch063010mls.htm>.

¹⁹ *SEC v. Ralston Purina Co.*, 346 U.S. 119 (1953) (The securities acts protect investors “by promoting full disclosure of information thought necessary to informed investment decisions.”).

²⁰ Glass Lewis, & Co., LLP, *Proxy Paper™ Guidelines: 2014 Proxy Season, An Overview of the Glass Lewis Approach to Proxy Advice* 17 (2014), http://www.glasslewis.com/assets/uploads/2013/12/2014_GUIDELINES_Shrhdr_Initvs.pdf.

²¹ *Id.*

²² Michael Hadani, *Institutional Ownership Monitoring and Corporate Political Activity: Governance Implications*, 65 J. of Bus. Res. 944, 944-50 (2012), available at <http://www.sciencedirect.com/science/article/pii/S0148296311001378>.

²³ Anthony Kammer & Liz Kennedy, *Who decides when a corporation spends money in politics?*, DEMOS, <http://www.demos.org/sites/default/files/publications/Explainer-CorporateExplainer2-4.pdf>.

²⁴ Rajesh K. Aggarwal *et al.*, *Corporate Political Donations: Investment or Agency?*, 14 Bus. & Pol. 1 (2012), available at <http://www.degruyter.com/view/j/bap.2012.14.issue-1/1469-3569.1391/1469-3569.1391.xml?format=INT>.

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²⁵ Donald H. Schepers & Naomi A. Gardberg, *Baruch Index of Corporate Political Disclosures: 2011* (2011), <http://baruch.cuny.edu/baruchindex/BIResults.pdf>.

²⁶ http://www.ucsusa.org/assets/documents/scientific_integrity/a-climate-of-corporate-control-report.pdf

²⁷ Alison Frankel, *Why shield corporations from disclosing political spending?*, REUTERS (Dec. 16, 2013), <http://blogs.reuters.com/alison-frankel/2013/12/16/why-shield-corporations-from-disclosing-political-spending/>.

²⁸ See Lucian A. Bebchuk & Robert J. Jackson, *Responding to Objections to Shining Light on Corporate Political Spending (1): The Claim of Immateriality*, HARV. L. SCH. FORUM ON CORP. GOVERNANCE & FIN. REG. (Apr. 4, 2013, 9:26 am), <http://blogs.law.harvard.edu/corpgov/2013/04/04/responding-to-objections-to-shining-light-on-corporate-political-spending-1-the-claim-of-immateriality/>.

²⁹ While ordinary business decisions may be excluded from annual proxy statements, the SEC has indicated that a shareholder proposal that raises "significant social policy issues" and does not micromanage the company should not be excluded under the ordinary business rule. For an overview of the types of shareholder proposals that may be excluded from a company's proxy statement, see David Lynn, *Frequently Asked Questions about Shareholder Proposals and Proxy Access*, MORRISON & FORRISTER LLP (2012), <http://www.mofo.com/files/Uploads/Images/Frequently-Asked-Questions-about-Shareholder-Proposals-and-Proxy-Access.pdf>.

³⁰ See Home Depot, Inc., SEC No Action Letter, 2011 WL 291324 (Mar. 25, 2011), available at <http://www.sec.gov/divisions/corpfin/cf-noaction/14a-8/2011/northstarasset032511-14a8.pdf>; Bank of America, SEC No Action Letter (Feb. 15, 2013), <http://www.sec.gov/divisions/corpfin/cf-noaction/14a-8/2013/stephenjohnson021513-14a8.pdf>.

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³³ Coates, *supra* note xxxi.

³⁴ Hadani, *supra* note xxii.

³⁵ Kyung M. Song, *Amazon lobbies heavily for Internet sales tax*, SEATTLE TIMES (Sep. 7, 2013), available at http://seattletimes.com/html/localnews/2021778597_amazonlobbyingxml.html.

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³⁶ Deniz Igan *et al.*, *A Fistful of Dollars: Lobbying and the Financial Crisis*, (IMF Working Paper No. 09/287, Dec. 2009), available at <http://www.imf.org/external/pubs/ft/wp/2009/wp09287.pdf>.

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³⁸ Letter from the Committee on Disclosure of Corporate Political Spending, *supra* note *iv*.

³⁹ Susan Holmberg, *A Cost-Benefit Analysis of Corporate Political Spending Disclosure*, ROOSEVELT INSTITUTE (Oct. 30, 2013), http://www.rooseveltinstitute.org/sites/all/files/2013_10_30_Holmberg_Cost_Benefit.pdf

⁴⁰ See Press Release, Sustainable Inv. Inst., Corporate Political Spending, Climate Risks Are Major Focus of 2013 Shareholder Resolutions, Says New Report (Mar. 7, 2013), http://siinstitute.org/press/2013/ProxyPreview2013_pr_20130307.pdf; Press Release, Sustainable Inv. Inst., Proxy Preview 2014 Shows Record Number of Social & Environmental Shareholder Resolutions Filed in 2014 (Mar. 5, 2014), http://siinstitute.org/press/2014/ProxyPreview2014_pressrelease_20140305.pdf.

⁴¹ Contrary to the comments of some, the failure of many of these initiatives to gain majority support is not indicative of a lack of shareholder interest. Studies show that in a majority of proxy votes, most investors vote in accordance with management recommendations regardless of management's position. This is in large part the result of structural obstacles to investors' ability to register their preferences. For example, because such a large proportion of stocks owned by small investors are held through mutual funds, fund managers, rather than individual investors, vote the shares, and they nearly always side with management or abstain, regardless of the nature of the issue being voted on or the views of fund participants. See, e.g., Marla Brill, *The mystery of mutual fund proxy votes*, REUTERS (Nov 1, 2011), <http://www.reuters.com/article/2011/11/01/usa-funds-proxyvotes-idUSN1E7A01U120111101>.

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⁴⁶ Glass Lewis, *supra* note xx, at 16.

⁴⁷ *Id.*

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⁵⁰ Melanie Sloan, *Aetna responds to CREW: You're right*, CITIZENS FOR RESPONSIBILITY AND ETHICS IN WASHINGTON (Jun. 14, 2014), <http://www.citizensforethics.org/blog/entry/aetna-responds-to-crew-youre-right>.

⁵¹ Press Release, Citizens for Responsibility and Ethics in Washington, Aetna hides \$7 million in Political Spending; CREW calls for greater disclosure (Jun. 14, 2012), <http://www.citizensforethics.org/press/entry/aetna-political-spending-american-action-network-chamber-of-commerce>.

⁵² Press Release, Citizens for Responsibility and Ethics in Washington, CREW files lawsuit against Aetna for misleading proxy statements (Dec. 10, 2013), <http://www.citizensforethics.org/press/entry/crew-files-lawsuit-against-aetna-for-misleading-proxy-statements>

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