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"CORPORATE GOVERNANCE AFTER CITIZENS UNITED"

Chairman Kanjorski, Ranking Member Garrett, and Fellow Congressmen:

Introduction

I am pleased and honored to be invited to testify here today. My message is simple: Congress cannot successfully fight the Supreme Court over the scope of the First Amendment, but it can and should increase the transparency and accountability surrounding corporate involvement in the political process. To accomplish this, Congress can use its unquestioned power over the federal securities laws (and particularly the federal proxy rules). The goal of such efforts would not be to prevent all corporate contributions (which would be constitutionally suspect after Citizens United v. Federal Election Commission, 130 S. Ct. 876 (2010)), but rather to (1) increase managerial accountability to shareholders in a very low visibility context where managerial and shareholder interests are not well aligned, and (2) spread the sunlight of full disclosure over the very opaque process by which corporations today indirectly subsidize electioneering expenses. Sunlight is the best disinfectant, but today corporations typically avoid disclosure by making contributions through "conduit" organizations (chiefly trade associations and not for profit organizations), which in turn directly make the contribution or underwrite the electioneering expense. Interestingly, both the majority decision and Justice Scalia's concurring opinion in Citizen United assume and state that shareholders have the power to curb and restrict the use of corporate funds for political or electioneering purposes.

That assumption is too facile, because shareholders are actually very constrained in what they can do. Today, shareholders of public companies lack an effective means by which to control managerial behavior in this area. Nor do they receive adequate information (without which they have little incentive to take action). The most obvious and effective reform is not litigation against officers and directors (which would probably be futile in any event), but enhanced shareholder control through shareholder bylaw amendments. Shareholder-adopted bylaw amendments could restrict, limit, condition or even prohibit corporate expenditures on (or the use of corporate property or services for) political electioneering (including both candidate elections and referenda on issues). The most likely such bylaw amendments would (1) mandate that all electioneering payments or contributions (including contributions to conduit organizations for unspecified purposes) receive prior approval from a committee of independent directors and (2) require that such payments or contributions (and the justifications therefor) be reported to the shareholders.

Realistically, it is not necessary that such proposed bylaw amendments actually be adopted by shareholders for them to be effective. Merely the fact that they can be proposed brings management and/or the board to the bargaining table for serious negotiations. But, if action cannot even be proposed, shareholders are silenced.

Today, any shareholder effort to adopt bylaw amendments or take other collective action (such as simply seeking information) faces serious obstacles on two levels: (1) state law limits bylaw amendments by shareholders; and (2) SEC indifference and/or hostility prevents shareholder proxy proposals from even raising issues or seeking information. First, on the state law level, shareholders traditionally possessed broad power under corporate law to "adopt, amend or repeal bylaws," and bylaws were permitted to address all aspects of the corporation's business and affairs. But now comes the surprise: a 2008 decision of the Delaware Supreme Court has significantly curbed shareholder power to amend the bylaws, at least when those amended bylaws would restrict the board of directors in non-procedural ways. See CA, Inc. v. AFSCME Emples. Pension Plan, 953 A.2d 227 (Del. 2008) (discussed below). As a result, at least in Delaware (where over 50% of major U.S. public corporations are incorporated), it is unlikely that shareholders can substantively restrict direct or indirect political contributions to "conduit" organizations through bylaw amendments because such amendments would be seen as impermissibly restricting the authority of the board of directors. Outside of Delaware, the law is both sparse and uncertain, although a few decisions have more broadly upheld the scope of shareholder-adopted bylaws.[1] Because there is a need for uniformity, I will urge (in Part IV below) that Congress enact a modest amendment to the Securities Exchange Act of 1934 that would clarify and restore shareholder power to adopt and amend corporate bylaws relating to corporate political activities (which bylaws could not then be repealed or otherwise modified, except by later majority shareholder action). This proposed amendment need not address all shareholder proxy proposals all or bylaw amendments, but would focus exclusively on shareholder proposals addressing corporate activities and expenditures, both direct and indirect, in connection with political elections, campaigns or referenda.

The second obstacle to increased shareholder accountability lies in the SEC's skeptical attitude toward shareholder proposals, including bylaw amendments, relating to corporate political activities. To adopt a bylaw amendment (or to take any other action at a shareholders meeting), shareholders need as a practical matter to rely on SEC Rule 14a-8, which allows them to place a shareholder proposal on the corporation's own proxy

[1] See Int'l Bd of Teamsters Gen. Fund v. Fleming Cos., Inc., 975 P.2d 907, 909 (Okla. 1999) (upholding bylaw amendment restricting use of "poison pill").

statement for a shareholder vote. But Rule 14a-8 contains a number of broad and ambiguous exceptions under which the SEC can permit corporations to exclude shareholder proposals from their proxy statements. Recently (as discussed below), the SEC has advised several public corporations that they may exclude shareholder proposals calling for the corporation to prepare a report to its shareholders on its electioneering and lobbying activities. The SEC has given a variety of justifications for permitting the exclusion of such shareholder proposals, but the bottom line is that shareholder proposals, even ones requesting only an informational report, face an uncertain fate (and probably an uphill battle) at the SEC. Thus, if shareholder accountability is to be achieved in this area, Congress needs to prod the SEC to revisit this field.

Finally, shareholders cannot be assumed to be eager to take any form of collective action, all of which involve costs to them. The reality is that shareholders will remain rationally passive unless and until they become aware of corporate payments for purposes that appear unrelated to shareholder profit. Today, shareholders receive little information, and substantial corporate payments can be masked as contributions for unspecified purposes to trade associations or other "conduits" (even though management knows or foresees the likelihood that some or all the payment will be used for political purposes). At a minimum, greater disclosure is needed before shareholder accountability will become feasible. The standard vehicles for disclosures to shareholders and the market by a public corporation are its proxy statement and its Annual Report on Form 10-K. Thus, I will recommend (in Part VI below) that Congress instruct the SEC to require at least annual disclosure (and possibly quarterly disclosure) of all payments, loans, contributions of property or services, to a candidate, a campaign organization, or a "conduit" organization where (in the last case) it is foreseeable to the corporation's managers that some or all of such amounts or contributions will be used for electioneering purposes.

One final prefatory comment is necessary: those who wish to minimize any Congressional response to Citizens United will argue that the appropriate answer is simply to rely upon greater board oversight. Certainly, increased board oversight is desirable, and groups such as the Center for Political Accountability have done much to foster improved board oversight. But exclusive reliance should not be placed on the board alone. Boards respond to shareholder objections with greater alacrity when shareholders have a potential remedy if the board were to ignore them. Subjecting corporate managers only to greater board oversight is analogous to throwing Brer Rabbit into the Briar Patch. If a given board of directors is willing to tolerate covert political actions by management, shareholders need a right to challenge them. Bylaw amendments do not need to be adopted to be effective; rather, they need only to secure a significant shareholder vote (say 20% or more) to awaken the board to shareholder concerns and thereby bring the corporation to the negotiating table. But to begin this process, the federal proxy rules and the SEC's continuous disclosure system need the disclosure revisions hereafter discussed.

II. An Overview of the Conduit System

Generally, public corporations are reluctant to directly fund political advertisements and similar activities themselves (even though they have been accorded Constitutional protection to do so since the Supreme Court's decision in Federal Election Commission v. Wisconsin Right to Life, Inc., 551 U.S. 449 (2006)). Expenditures for political purposes, particularly high profile advertisements, are likely to antagonize some portion of the corporation's shareholders, consumers or employees.

As a result, corporations prefer to make contributions through conduit organizations. Such organizations include both political entities (known in the parlance as "Section 527" organizations[2]) and trade associations and other tax exempt organizations.[3] The scale of such funding is growing, and one recent study noted that in 2004 over $100 million was spent on "political spending" (as defined by the Internal Revenue Code) by just six trade associations.[4] Although a corporation is under no general statutory obligation to disclose its political contributions, the Bipartisan Campaign Reform Act of 2002 ("BCRA") does require any person who spends more than $10,000 on electioneering communications within a calendar year to file a disclosure statement with the Federal Election Commission ("FEC"). Thus, the conduit organization that actually makes the electioneering contribution must file such a statement and disclose the names of certain contributors who have specifically paid for the communication (see 2 U.S.C. § 434(f)(2)). As a result, the practice has developed under which corporate contributions to these conduit organizations are not specifically earmarked for any purpose, in order that specific identification of the donor is not required by the conduit organization. Revealingly, a growing proportion of the expenditures for political "issue" advertising by nonprofit groups are not allocated to any donor. According to a recent New York Times story, prior to the Wisconsin Right to Life

[2] "Section 527" refers to 26 U.S. Code § 527 (a provision of the Internal Revenue Code) which permits political committees and political entities to receive unlimited corporate contributions. The Democratic and Republican Governors Associations would be examples of Section 527 organizations.
[3] Trade associations and civic leagues are permitted by the Internal Revenue Code to engage in political campaign activities so long as such activity does not constitute the group's primary activity. See 26 U.S.C. §501(c)(6). Among the most politically active of these trade organizations are: the U.S. Chamber of Commerce, the National Association of Manufacturers, the Business Roundtable, and the American Tort Reform Association. Corporations are not required today to disclose their contributions to such organizations.
[4] See Center for Political Accountability, HIDDEN RIVERS: How Trade Associations Conceal Corporate Political Spending, Its Threat to Companies, and What Shareholders Can Do (2008) at 1.

decision, in 2006, virtually all of the $98.7 million in "electioneering communications" by nonprofit groups in the 2004 election cycle did identify the donor. But, during the 2008 election cycle (after the Wisconsin Right to Life decision in 2006), over one-third of the $116.5 million reported by nonprofit groups as expended on "electioneering communications" was not accompanied by donor identification.[5] Predictably, this unidentified donor percentage will grow in the wake of Citizens United, as corporations, now free to contribute generously, elect to use conduits and make unrestricted contributions in order to avoid the need to have their donations disclosed.

Finally, the interests of shareholders and managers do not appear to be well aligned with respect to political contributions. The Center for Political Accountability has released a series of reports showing that managers have regularly used corporate funds to subsidize political causes or issues having no obvious relationship to their corporation's interests.[6] Thus, although it is certainly understandable that a pharmaceutical company would wish to lobby on the issue of health care reform, it is less clear why it should seek to influence issues such as abortion or single sex marriage. But the evidence is clear that public companies do seek to influence these issues.

III. Shareholder Power to Restrict Corporate Political Activities Under State and Federal Law

It is simplest to cover the shareholders' ability to restrict corporate political spending under state law and then turn to federal law. I will not cover the possibility of derivative litigation against corporate officers and directors because, in the case at least of a public corporation, the legal necessity for a shareholder to make a demand on the board

[5] See Griff Palmer, "Decision Could Allow Anonymous Political Contributions by Businesses," N.Y. Times, February 28, 2010 at p. 25.
[6] For one such study, see Hidden Rivers, supra note 4.

before commencing suit is deemed to acknowledge the applicability of the business judgment rule and thereby becomes an insurmountable barrier for all practice purposes.

A. State Law

Under Section 109 of the Delaware General Corporation Law (and similar statutes in other jurisdictions), shareholders may "adopt, amend or repeal" the bylaws, and under Section 109(b), the bylaws "may contain any provision, not inconsistent with law or with the certificate of incorporation, relating to the business of the corporation, the conduct of its affairs, and its rights or powers, or the rights and powers of its stockholders, directors, officers, or employees." On its face, this language seems to cover the waterfront. But Section 141(a) of the Delaware General Corporation Law provides equally universally that "[t]he business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors, except as may be otherwise provided in this chapter or in its certificate of incorporation." Thus, there is an obvious tension, and if a bylaw restricts the authority or discretion of the board, it was not self-evident which provision – Section 109 or Section 141 – took precedence.

In 2008, the Delaware Supreme Court resolved this tension in C.A. Inc. v. AFSCME Employees Pension Plan, 953 A.2d 227 (Del. 2008). In that case, AFSCME, a large union pension plan, proposed a bylaw amendment to be included on C.A. Inc.'s proxy statement that would compel the corporation to reimburse a stockholder, or group of stockholders, for reasonable expenses incurred in a proxy fight so long as the insurgent group elected at least one director. C.A. Inc. asked the SEC to permit it to exclude this proposed bylaw under Rule 14a-8 on several grounds, including that it was not a "proper subject" for shareholder action under Delaware law because it contravened Del. Gen.

Corp. L. §141 by invading the authority of the board of directors. The SEC certified this question of whether it was a "proper subject" to the Delaware Supreme Court. The Court found that, although a proxy expense reimbursement bylaw was a proper subject for shareholder action, the specific bylaw, as drafted, violated Section 141 by attempting to curb the right and ability of the board to manage the corporation's business and affairs. Specifically, it said that the proposed bylaw "would violate the prohibition, which our decisions have derived from Section 141(a), against contractual arrangements that commit the board of directors to a course of action that would preclude them from fully discharging their fiduciary duties to the corporation and its shareholders."[7] For the board to have acceded to this restriction, it added, would have breached their fiduciary duties.[8]

For the future, the key impact of the C.A., Inc. decision is that although it considers procedural bylaws as appropriate for shareholder action, it views skeptically bylaws that "encroach upon the board's managerial authority under Section 141(a)."[9] Much academic and practitioner commentary has focused on this decision,[10] and most have concluded that a proposed shareholder bylaw amendment will be invalid if it attempts to curb the substantive power of the board. Possibly, some argue, a shareholder bylaw amendment would remain a proper subject for shareholder action if it contained a "fiduciary out" that permitted the board to ignore the amendment if it believes that its fiduciary duties require it to do so. Thus, a shareholder bylaw proposed bylaw that precluded "soft money" contributions to a Section 527 organization or to a trade

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[7] Id. at 240.
[8] Id. at 238, 240.
[9] Id. at 235 fn. 15-16.
[10] For the view that the decision will preclude most substantive bylaw amendments by shareholders, see Note, Delaware to the Rescue, 3 Brooklyn J. Corp. Fin. & Com. L. 431 (2009); Robert Thompson, Delaware's Disclosure: Moving the Line on Federal-State Corporate Regulation, 2009 U. Ill. L. Rev. 167, 188-189.

association would be presumptively invalid unless it contained a "fiduciary out" clause that permitted the board to disregard the bylaw if it believed that doing so was in the best interests of shareholders. To say the least, the value and effect of such a bylaw amendment is highly questionable.

In fairness, C.A., Inc. will probably not be the last word that Delaware courts write on shareholder sponsored bylaw amendments. Historically, the Delaware corporate law decisions have twisted and turned, as new nuances emerge, times change, and the personnel on the court shifts. But in the meantime, it is clear that the SEC will likely rule that shareholder bylaws impinging on the board's substantive powers are not a "proper subject" for shareholder action under SEC Rule 14a-8(i)(1) and so will permit such proposed amendments to be excluded. Indeed, shareholder activists do not appear currently to be seeking to adopt bylaw amendments. Today, shareholder activists are disdaining the formal bylaw amendment approach and instead requesting the board pursuant to SEC Rule 14a-8 to prepare a report on the corporation's political contributions and expenditures. As discussed below, this approach has also met with mixed results, as the SEC's staff has sometimes read Rule 14a-8 not to authorize such a request.

Thus, the bottom line is that under Delaware law shareholders have little practical ability to limit or restrict political contributions by mandatory shareholder action. Outside of Delaware, the law is sparse, but the strong tendency in another jurisdiction has been for their courts to follow Delaware on issues of corporate law.

B. Federal Law

Under SEC Rule 14a-3, corporations are required to prepare and distribute proxy statements in connection with their solicitation of proxies. Under SEC Rule 14a-8,[11] a shareholder may require the corporation under defined circumstances to include a proposal submitted by the shareholder in its proxy statement for a vote by all shareholders. This rule greatly economizes on the costs that a shareholder would otherwise face if the shareholder had to conduct his or her own proxy solicitation. Thus, for several decades, corporate activists and reformers have relied on Rule 14a-8 to enable them to place issues of concern to them on the agenda for the corporation's annual meeting. Originally, these issues primarily related to corporate ethics and morality (e.g., apartheid, discrimination, environmental issues, etc.), but more recently the focus has moved to economic issues (poison pills, takeover defenses, board structure, etc.). Rule 14a-8 has, however, some important substantive limits, which the SEC has inconsistently interpreted over the years:

> First, Rule 14a-8(i)(1) permits the corporation to exclude the proposal if it "is not a proper subject for action by shareholders under the laws of the jurisdiction of the company's organization."
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> Second, Rule 14a-8(i)(7) permits the corporation to exclude if "the proposal deals with a matter relating to the company's ordinary business operations."
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> Third, Rule 14a-8(i)(5) permits exclusion if the proposal is deemed economically insignificant because it "relates to operations which account for less than 5 percent of the company's total assets . . . and for less than 5% of its net

[11] See 17 CFR §240.14a-8.

earnings and gross sales for its most recent fiscal year and is not otherwise significantly related to the company's business."

Although there are numerous other restrictions, these three are most important. Because Rule 14a-8(i)(1) conditions the eligibility of the shareholder proposal on whether it is a "proper subject" under state law, it follows that the C.A., Inc. v. AFSCME Employees Pension Plan decision discussed above has undercut the ability of shareholders to use Rule 14a-8 to propose a bylaw amendment that restricts the board's substantive power to make political contributions. As a consequence, shareholders have recently instead sought to use Rule 14a-8 to request the corporation to prepare a report describing its political contributions and related political or lobbying activities. The premise here is that such a request is more procedural in character so that the C.A., Inc. decision is not an obstacle.

Nonetheless, even in the case of these more modest requests, the SEC's Staff has recently resisted. Last year, both Bristol-Myers Squibb Company and Abbott Laboratories received shareholder proposals submitted by the AFL-CIO Reserve Fund requesting them to prepare reports on their lobbying activities and expenses with respect to specific political issues during a specific time period. In both cases, the SEC Staff ruled in no-action letters that the proposals could be excluded as relating to "ordinary business operations." See Bristol-Myers Squibb Company, 2009 SEC No-Act. LEXIS 590 (Feb. 17, 2009); Abbott Laboratories, 2009 SEC No-Act. LEXIS 133 (Feb. 11, 2009). Similarly, the SEC's Staff permitted Exxon Mobil Corporation to exclude a shareholder proposal submitted by a nonprofit foundation requiring Exxon Mobil to provide a report disclosing Exxon Mobil's "policies and procedures for political contributions and expenditures." See Exxon Mobil Corporation, 2009 SEC No-Act. LEXIS 347 (March 23, 2009) (permitting proposal to be excluded under Rule 14a-8(i)(10) on the ground that Exxon Mobil had already "substantially implemented" a similar proposal).

In overview, the SEC's Staff has long read the "ordinary business operations" exclusion under Rule 14a-8(i)(7) broadly in the belief that "it is impracticable for shareholders to decide how to solve such problems at an annual shareholders meeting." See "Amendments to Rules on Shareholder Proposals," Securities Exchange Act Release No. 40018 (May 21, 1998). In so doing, the Staff has sometimes embarrassed the Commission. Not so long ago, the SEC Staff permitted Cracker Barrel Old Country Store Inc. to exclude shareholder proposals asking Cracker Barrel to reconsider its position that it would not hire or retain gay employees. This decision was challenged in court. See New York City Employees Ret. Sys. v. SEC, 45 F.3d 7 (2d Cir. 1995). Ultimately, under pressure from all sides, the SEC reversed course and decided that discriminatory employment policies were not a matter of "ordinary business operations." See Securities Exchange Act Release No. 40018 (May 21, 1998). Nonetheless, over the last twenty odd years, a fair generalization of the SEC Staff's reading of Rule 14a-8(i)(7) would be that it has consistently read this exemption broadly to protect managements from any obligation to provide detailed data or respond to shareholder pressures – until such time as the Staff's policy became so controversial as to embarrass the Commission. Only a decade ago, all proposals relating to executive compensation were similarly excluded as matters of "ordinary business."

In short, recent experience has shown that the SEC will exclude even shareholder proposals seeking only disclosure of corporate policies and procedures relating to political contributions or lobbying expenses as normally outside the permissible scope of Rule 14a-8. Against this background, it is well to reconsider an assumption made by the Court's majority in Citizens United. There, the majority wrote:

> "Shareholder objections raised through the procedures of corporate democracy . . . can be more effective today because modern technology makes disclosures rapid and informative."

See Citizens United v. Federal Election Commission, 130 S. Ct. 876, 175 L. Ed. 2d 753, 802 (2010).

In reality, however, the deck seems stacked against shareholders who seek either to challenge political contributions by management or to obtain fuller disclosure from the corporation. In all likelihood, such a shareholder will be unable to secure a bylaw amendment (or even to propose it to other shareholders under Rule 14a-8) or to obtain a report from the corporation disclosing its specific policies and practices regarding corporate contributions or lobbying activities.

IV. Empowering Shareholders to Address Corporate Political Contributions and Related Activities

Because there is a need for uniformity, the simplest, most direct route to assuring accountability to shareholders is to amend the Securities Exchange Act of 1934 to authorize shareholders both to adopt bylaw amendments addressing corporate political activities and to require corporate reports to shareholders on corporate political activities, contributions and donations.

For example, a new section could be added to Section 14 (which covers proxies and their solicitation) of the Securities Exchange Act, which could provide along the following lines:

<u>Proposed Section 14(i)</u>:

> "(i) It shall be unlawful for any issuer of a class of equity securities registered pursuant to Section 12(b) or 12(g) of this title, or required to file reports pursuant to Section 15(d) of this title, to solicit any proxy, consent, or authorization without permitting shareholders to submit shareholder proposals, in accordance with rules and procedures prescribed by the Commission, to be voted upon by the shareholders at the same time as the vote, consent, or authorization sought by the issuer, where such proposal relates to political contributions, loans, or expenditures or electioneering expenses, including direct contributions of services or property by the issuer or indirect contributions, loans, or other payments by the issuer to conduit organizations (as defined) that may use all or some portion of such contributions, loans or expenditures for political or electioneering expenses. Notwithstanding any contrary provision of state or federal law, a vote by a majority of the shareholders represented at a shareholder meeting at which a quorum was present, or a vote by a majority of all shares outstanding in the case of a shareholder consent, in favor of a shareholder proposal made in accordance with Commission rules and relating to corporate political activities, contributions, or payments (i) shall bind the issuer to the same extent as if the proposal were set forth in the issuer's certification of incorporation or similar charter document, (ii) may not be cancelled or modified by its board of directors or any similar body, and (iii) may be modified or repealed only by a majority vote of the shareholders at a subsequent shareholder meeting or by a subsequent shareholder consent executed by a majority of all the shareholders."

This language is intended to be illustrative, and it would require some additional definitions for terms such as "electioneering expense" and "conduit organization," but those terms would be broadly defined.

The impact of this provision would be threefold: (1) shareholder bylaw amendments would be valid in all states, but only with respect to the subject of the corporation's involvement in political and electioneering expenses; (2) the directors could not cancel, repeal or modify any shareholder bylaw with a board-passed bylaw; (3) a majority of the shareholders could always modify or repeal the earlier policy (thus preventing a supermajority provision to be inserted that might require, for example, an 80% shareholder vote to modify or repeal the initial policy). Pursuant to this procedure, shareholders could pass bylaws, create special committees of directors to monitor the corporation's involvement in politics, or require reports or studies to be prepared for the shareholders.

The prospects for abuse of this new power seem small because shareholders cannot easily be persuaded to vote for any radical or prophylactic proposal. The real likelihood is that the board and shareholder groups will bargain "in the shadow of the law" and reach agreement on new policies in order to forestall the need for resort to the bylaw amendment process. Today, the board has less need to negotiate because insurgent shareholders cannot typically resort either to a bylaw amendment under state law or a shareholder proposal under SEC Rule 14a-8. In effect, once shareholders are empowered, more realistic and meaningful negotiations can begin.

Some would urge Congress to go further and preclude the corporation from making political contributions or incurring "electioneering expenses," directly or indirectly, unless it had first obtained shareholder authorization for such payments. This would place the burden on the corporation to obtain shareholder consent as a prerequisite. The problem with this more radical approach is that (1) it could conceivably be seen as an unconstitutional prior restraint, and (2) it would likely produce only broad blanket authorizations supported by management, which shareholders might approve for fear that the corporation would otherwise be silenced or rendered unable to pursue its legitimate interests. Placing the burden on shareholders to obtain a majority approval for a shareholder proposal is the more cautious and conservative course, and it will likely produce negotiation and consensus.

V. SEC Rule 14a-8

In fairness, Rule 14a-8 has long imposed substantial logistical burdens on the SEC's Staff, and the Staff has interpreted the rule cautiously, often reading it very narrowly in order not to subject corporations to potential micro-management by shareholders. But the issue of corporate campaign contributions is distinctively different, in part because such payments may not be related to the corporation's business activities. Thus, it is important that the SEC revisit SEC Rule 14a-8 in light of Citizens United, which fundamentally changes the relationship between corporations and the political process. Congress should prod the SEC to re-examine its policies under Rule 14a-8 through hearings and/or letters to the Commission. Ultimately, Congress could legislate, but that may not be (and hopefully should not be) necessary. Still, at a minimum, the Commission and its Staff must recognize that political contributions and electioneering expenses are seldom matters of "ordinary business operations" but rather reflect departures from ordinary business (sometimes extraordinary departures) that shareholders reasonably want to monitor and restrain.

VI. Disclosure and Transparency

Shareholders today do not receive even minimal disclosure about corporate political contributions, donations, or electioneering expenses. As earlier noted, federal law may require the conduit organization to disclose its contributions and payments, but it does not require those corporations who make payments for unspecified purposes to a trade association or Section 527 organization to disclose these payments. Although most corporations will rarely direct that their contribution be used for political or electioneering purposes, they will be aware of such use because the trade association is required by law to inform its corporate donors of the amount of their contributions used for political purposes. Precisely because the corporation has this knowledge, it would be appropriate to require disclosure of both the total contribution to the conduit organization and the percentages allocated to political or electioneering purposes over recent years.

The appropriate medium for such disclosure is the corporation's Annual Report on Form 10-K and its proxy statement. This information would be instantly accessible to the shareholders, the market, and securities analysts. Moreover, the appropriate disclosures should cover not only the amount of such payments, but also (1) the purposes behind it and (2) the process by which it was internally approved. Did the CEO decide this on his own? Or was it overseen by a specific board committee? If so, why did they think it appropriate? False statements made in response to these disclosure requirements would be subject to potential criminal enforcement under 18 U.S.C. §1001, and the SEC could also seek civil injunctions and penalties.

Arguably, the SEC already has authority to require disclosure of corporate political activities, but clearly it has not used this power. Possibly, the Commission may feel that legitimate issues exist as to whether such information is material to investors. But the SEC should articulate its position. After Citizens United, the prospect of material corporate payments for political purposes increases exponentially, and the need for disclosure is enhanced. Disclosure deters abuse, and in the light of Citizens United, the potential for low-visibility abuse has just grown.

CONCLUSION

As a general rule, the least drastic means should be preferred when regulating the behavior of public corporations. Thus, I do not suggest or support legislation that would attempt to prohibit corporate contributions or even subject them to prior shareholder approval.

Rather, my starting point comes from Justice Brandeis:

"Sunlight is the best disinfectant; electricity, the best policeman."

That maxim has long been the rationale for the SEC. Precisely for that reason, Congress should instruct the SEC to revisit its disclosure requirements in light of Citizens United and advise Congress whether more detailed disclosures are needed. Because today SEC disclosure rules simply ignore corporate political contributions, it is hard to believe that the SEC will really tell Congress that nothing needs to be done. If the SEC believes it needs additional statutory authority, it should so advise Congress. Still, because the SEC can sometimes be a bureaucratic and slow moving body with many other crises and issues to face, a deadline should be specified for its response.

Next, the SEC must be prodded to reconsider its overbroad exemptions to Rule 14a-8 and recognize that covert political activities are not matters of "ordinary business operations." That the Staff today has repeatedly ruled requests for informational reports about corporate political activities to be simply beyond shareholder power should embarrass the Commission.

Finally, shareholders need a remedy for the case where the corporation resists. The best remedy is not litigation, but a right for the majority of the shareholders to adopt bylaws regulating and restricting corporate political activities. This right will seldom be actually employed, but its existence vastly increases shareholder leverage. Because shareholders own the corporation, it is hardly radical to urge that they be given a say in how it is run.