Institutional Investors Demand Disclosure on Companies' Political Spending

06 Jun 2012 - Katie Gilbert

On January 21, 2010, the day the Supreme Court delivered its landmark decision on Citizens United vs. Federal Election Commission that it would overturn most of a century's worth of regulations on corporate political spending, the $140 billion New York State Common Retirement Fund corporate governance department happened to be meeting to discuss the problem of untraceable political spending by companies in its portfolio. Patrick Doherty, the fund's director of corporate governance, was making the pitch to New York State Comptroller Thomas DiNapoli that the political spending issue should be a central focus of New York Common's corporate governance campaign for the coming year.

The overlap was coincidental; before the court's final decision on Citizens United, the case hadn't attracted too much attention in the comptroller's office or among most of the general public. That changed after January 21. Despite New York Common's pre-Citizens United efforts to improve disclosure around corporate political spending — which primarily consisted of a concerted support of any shareholder resolution pushing the issue — the fund's leaders hadn't heard constituents express their opinions on the topic. But they spoke up after the decision on Citizens United, says DiNapoli.

"Since Citizens United, many folks expressed concern," he says, adding that New York Common changed tack after the court's January 2010 decision, too. "We've always put a priority on the transparency and accountability of a company's operations, but all that was obviously heightened by the Supreme Court decision and a sense that some corporations were going to embark on an even more aggressive pattern of engaging in corporate spending for political campaigns."

The court's decision on Citizens United cleared the way for an avalanche of corporate money to fall into the political process by striking down constraints on political spending from companies' corporate treasuries as a violation of the freedom of speech protected by the First Amendment. (The law still prohibits direct corporate contributions to federal candidates, but otherwise, companies face no restrictions as to the amount, recipient or timing of their political contributions.)

The consequences of the court's decision came into sharp relief right away. According to data from

Public Citizen's Congress Watch division, spending by outside groups between the 2006 and 2010 midterm elections jumped from about $50 million to $275 million. This year's presidential, state and local races are expected to set records as far and away history's priciest; in April alone, Barack Obama and the Democratic National Committee took in $43.6 million, and Republican candidate Mitt Romney's campaign and the Republican National Committee raised $40.1 million.

The Supreme Court never specified that any of this limitless corporate spending should be exercised anonymously. On the contrary, it appeared explicitly opposed to the idea of nontransparent spending: The court's majority opinion, penned by Justice Kennedy, states that "disclosure permits citizens and shareholders to react to the speech of corporate entities in a proper way." However, opaque corporate political spending has become the reality anyway, as companies have opted to make their donations through organizations formed under section 501(c)(4) of the U.S. tax code (reserved for "social welfare groups") and section 501(c)(6) (for business associations, like the Chamber of Commerce) which don't require the public disclosure of their funders. From the perspective of institutional investors like New York Common, this introduces more than a note of unquantifiable risk into the portfolio, and several major investors have mobilized behind the mission to wipe their portfolios clean of anonymous corporate political spending.

"We see this as an area of risk in terms of a possible impact on shareholder value," DiNapoli says. "You've seen some situations where companies have made decisions about political spending that have come back to hurt the bottom line for the company."

DiNapoli points to last summer's firestorm around Minneapolis-based retailer Target to illustrate. In July 2010, newly freed from political spending constraints, the company made a $150,000 donation to MN Forward, a nonprofit that soon thereafter ran a television ad for Tom Emmer, a Minnesota gubernatorial candidate and a loud opponent of gay marriage. (It remains unclear whether Target knew that MN Forward would be required by state law to disclose its contributors.) Boycotts, protests and in-store sit-ins followed at Target stores nationwide. Shareholders deserve to know, DiNapoli says, when companies have exposed themselves to that kind of reputational risk.

About a month after the Citizens United decision, New York Common joined the California Public Employees' Retirement System, the New Jersey State Investment Council, the Connecticut State Treasurer and others on a campaign organized by the Center for Political Responsibility and the Council of Institutional Investors to write letters to the 427 companies in the S&P 500 that lacked disclosure policies on corporate political spending. New York Common filed its first shareholder proposal on the issue with AIG for the company's fall 2010 general meeting.

This year, New York Common filed 17 such proposals — more than any other U.S. investor — and so far it has reached agreements on disclosure policies with seven of them, including PG&E, Safeway and Kroger. Research by the Sustainable Investments Institute found that the 2012 proxy season has seen a record 125 shareholder resolutions focused on political disclosure.

Last summer, California Treasurer Bill Lockyer sent a letter to the two biggest public pension funds in his state and in the U.S. — the $238 billion California Public Employees' Retirement System (CalPERS) and the $153 billion California State Teachers' Retirement System (CalSTRS) — entreating both to develop a formal policy of their own on the issue of political spending by portfolio companies.

"In order to accurately assess a company's sustainability, shareholders must be able to analyze whether political spending is consistent with the company's values," Lockyer wrote in the letter, "and whether it poses risks to the firm's brand, reputation or profitability." He also cites studies — one from Harvard Law School and another from the University of Minnesota School of Management — that have found negative correlations between a firm's political spending and its returns and overall value.

In November both California funds adopted policies to consistently support shareholder efforts focused on improving disclosure of political contributions.

But a company-by-company shareholder campaign is no match for the sweeping scope of the Citizens United decision. In August 2011 a coalition of prominent law professors asked the Securities and Exchange Commission to step in and exercise its power to make an overarching rule. The group of professors, called the Committee on Disclosure of Political Spending, filed a rulemaking petition asking the SEC to require that corporations publicly disclose their political contributions.

SEC commissioner Luis Aguilar has issued his strong support of the rule change. In February, in his speech at the annual SEC Speaks event, where the commission gathers to discuss its most pressing issues, Aguilar argued that the SEC should adopt the new disclosure rule.

"When it is clear that investors are in the dark and not receiving adequate disclosures, the commission should act, and act swiftly, to ensure that investors have the information they require," he said in the speech.

He added that he believed the disclosure gap was one that the Supreme Court had left the regulator to fill. The court made explicit in its decision on Citizens United, he said, that full, real-time disclosure on the new spending it allowed would be critical. And yet it offered no means to enforce such disclosure.

"Unfortunately, the court envisioned a [disclosure] mechanism that does not currently exist," Aguilar said at the SEC Speaks event. The SEC has received a record 180,000 comment letters supporting the professors' rulemaking petition.

Some investors say that requiring disclosure may not go far enough; companies need to altogether exit from political spending that's funded straight out of the corporate treasury, they insist. This proxy season, socially responsible investment firm Trillium Asset Management filed the first shareholder proposal by an institutional investor that asks a company to completely refrain from channeling funds

from the corporate treasury to political ends. The targeted company was Bank of America.

“We think money coming from the corporate treasury is the riskiest to play around with,” says Shelley Alpern, director of shareholder advocacy at Trillium. “It’s the most directly tied to the company image.”

On the resolution’s first go-round, support was low — 4.8 percent voted in favor of Trillium’s no-spending resolution at Bank of America — much lower than the average support of roughly 25 percent garnered so far this year by resolutions asking for more disclosure on political spending. Alpern says she believes that support will rise as investors come to understand that such a resolution doesn’t target lobbying or spending by corporate PACs at all — just the money that comes straight from corporate treasury coffers.

Adam Kanzer, managing director and general counsel at Domini Social Investments — a firm that has been filing shareholder resolutions and engaging companies on their political spending disclosure policies since 2003 — says that though all of the proposals Domini has filed with companies on the political spending issues have focused on disclosure, he is seriously considering going the way of Trillium and asking for a full stop to corporate-treasury contributions. “If that’s really what we want, then that’s really what we should ask for,” he says.

Beyond concerns of brand risk, is it possible that the First Amendment rights of shareholders are being impinged upon by the changes that followed Citizens United? The Supreme Court may soon have the opportunity to rule on that question, thanks to a showdown over Montana’s corporate political spending rules that has moved through district court to the state’s supreme court and has recently been appealed to the U.S.’s highest justices.

Domini is among a coalition of investors managing more than $100 billion — the roster includes Trillium Asset Management, the Interfaith Center on Corporate Responsibility, Calvert Asset Management and Walden Asset Management — that filed an amicus curiae brief in support of Montana’s effort to retain its corporate political spending ban, despite post-Citizens United challenges to that restriction.

The brief’s main argument is that a major public corporation’s political contribution violates shareholders’ First Amendment rights, since they’re obliged to "speak" through their financial ties to that contribution without their consent.

“A corporate and securities law regime that compels millions of investors to underwrite political speech to which they cannot meaningfully object may itself be unconstitutional,” states the brief.

The Supreme Court is expected to announce whether it will rule on the Montana case in June, and if it is accepted, it will be argued around Election Day. Kanzer and others hold to a careful hope that the state’s case could present the Supreme Court an opportunity to revisit its earlier decision in

Citizens United.

But in the absence of a change of heart from the Supreme Court and an overarching rule change from the SEC, institutional investors say they plan to continue chipping away at the issue by filing shareholder resolutions, one company at a time.

“The thing is, the disclosure and oversight strategy has been successful beyond everyone’s wildest dreams,” Kanzer says. He points to a recently passed milestone announced by the Center for Political Accountability, a nonprofit that has been working to help investors persuade companies to improve political spending disclosure rules: 100 companies, including half of the S&P 100, have agreed to adopt transparency policies on political contributions since the nonprofit began its efforts in 2003.

Says Kanzer: “When I first started this, I thought, ‘This is the right thing to do,’ but I didn’t think there was any chance companies were actually going to do it.”