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Transparency for Corporate Political Spending: A Federal Solution

By David Earley and Ian Vandewalker

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I. INTRODUCTION

American elections are awash in cash as never before. Spending in the 2012 presidential election will shatter all historic records, as will spending in Congressional races. But the most significant money won't be in the candidates' campaign coffers. The money transforming contemporary elections is that flowing into — and being spent by — outside groups that are legally independent of the candidates. Many of these outside groups are able to raise funds in unlimited amounts from wealthy individuals, unions, and corporations.

As the law stands today, corporations and unions can spend unlimited amounts of money in order to influence the outcome of elections. If individuals, unions, or corporations choose to spend political money directly — by producing television advertising and buying air time, for example — they must publicly disclose the expenditures and their contributors. But it is easy to evade such disclosure by simply routing political contributions through intermediary groups that purchase the ad time. The end result is that wealthy individuals, corporations, and unions can spend millions on political advertising to influence voters' choices at the ballot box, without disclosing this spending to the public.

After the Supreme Court decided *Citizens United v. FEC*,¹ Americans were outraged at the invitation extended to corporations to spend unlimited sums to influence elections. But in addition to expanding corporations' ability to make political expenditures, *Citizens United* strongly approved of disclosure requirements. The court emphasized the importance of such disclosure, explaining that through it “[s]hareholders 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.”²

Unfortunately, a disclosure regime that would accomplish these goals did not exist at the time *Citizens United* was decided. Nor does it exist now: more than two years after *Citizens United*, Congress has done nothing to improve our nation’s disclosure laws. The DISCLOSE Act of 2012, which would have required groups spending more than \$10,000 during an election cycle to identify donors of more than \$10,000, was filibustered in the Senate.

But the failure of Congress to act does not necessarily mean that Americans' calls for accountability in political spending must go unanswered. Instead, the Securities and Exchange Commission (“SEC”) can take action, having both the authority and the responsibility to protect shareholders and the public by mandating the disclosure of political expenditures by publicly-traded corporations. Indeed, one of the SEC commissioners, Luis Aguilar, recently came forward in support of disclosure rules and urged the full Commission to act.³ The rest of the Commission should follow his lead.

This report marshals arguments and evidence in favor of SEC regulation to shed light on corporate political spending. After describing the pressure on corporations to spend on elections and the ways such spending can be kept secret, the report details the benefits a robust disclosure regime would have for the relationship between shareholders and the corporations they own, as well as the health of American democracy. Finally, this report explains the legal considerations surrounding such an SEC regulation in our federalist system, showing not only that it is constitutional, but also that it is a superior policy to analogous state regulation.

II. THE PRESSURE ON CORPORATE DECISION MAKERS TO ENGAGE IN POLITICAL SPENDING HAS RISEN WITH THE INCREASING COST OF AMERICAN ELECTIONS

The Supreme Court's 2010 decision in *Citizens United v. FEC* ushered in a new era of spending in our nation's elections. The Court opened the door for unions and corporations to spend unlimited amounts to influence the outcomes of elections.⁴ While *Citizens United* enabled companies to spend treasury funds on political advertisements, lower court decisions expanded the ruling to strike down contribution limits on outside groups that exist solely to air political advertisements. Most significant was a decision by the United States Court of Appeals for the D.C. Circuit, *SpeechNow.org v. FEC*,⁵ which permitted individuals, corporations, and unions to give unlimited amounts to groups called independent-expenditure-only committees, more commonly known as "super PACs." Super PACs can accept unlimited contributions and spend unlimited sums on political advertisements.

The capacity to raise and spend unlimited sums on elections has ratcheted up the demand for political dollars — and political fundraisers have increasingly targeted corporate managers. In a 2010 Zogby International poll of business leaders, almost half of respondents said that pressure has increased to give to politicians since 2008.⁶ Seventy-two percent of respondents explained that their businesses gave money to either "gain access to influence the legislative process (55 percent) or to avoid adverse legislative consequences (17 percent)."⁷ Indeed, "members of the business community . . . face 'shake downs' for political contributions" from aggressive politicians.⁸

For example, in a 2010 meeting with 80 corporate PAC leaders, one Republican Party official candidly put these leaders on notice by stating, "we're evaluating giving patterns." He admitted that he tells corporate donors, "I understand you have to give money to Democrats. But I want to be back in the majority. You don't have to give [this Democrat] \$5,000. Give them \$2,000. You can give \$3,000 elsewhere. Now let me show you some open seats where you can make an investment" in a suitable candidate.⁹

Businesses face real pressure from politicians to make political expenditures, a problem made worse by *Citizens United*.

Given these increased pressures on corporate leaders, it is unsurprising that corporate political spending is growing along with the costs of elections. In recent years, spending in federal elections has exploded. Contributions to federal candidates have more than doubled from \$781 million in 1998 to an astounding \$1.9 billion in 2010.¹⁰ As a result of *Citizens United* in particular, outside spending in the 2010 federal elections quadrupled relative to the last midterm elections held in 2006.¹¹

In 2012, outside spending is on track to break all records, and corporations have helped fuel this spending by giving vast amounts of money to super PACs and other outside groups. By May, super PAC spending was over three times the amount that all outside groups had spent at the same point in the 2008 election.¹² Months away from the 2012 general election, numerous corporations have already donated more than \$1 million to super PACs; many more have made valuable, albeit lesser, contributions.¹³ As of March, for

example, Rooney Holdings — which has a \$53 million federal contract through a subsidiary business — had already donated \$1 million to the super PAC supporting Mitt Romney.¹⁴ In June, “[n]early 200 companies gave \$8.6 million to super PACs” — the highest monthly total yet this year — including “many repeat givers who have given a total of \$18 million.”¹⁵ The Sunlight Foundation recently estimated that businesses have contributed more than \$33 million to super PACs so far in the 2012 election cycle.¹⁶

Yet, as detailed below, corporate contributions to super PACs are just the tip of the iceberg. Substantially more corporate money is routed through non-profit “social welfare” groups and trade associations like the U.S. Chamber of Commerce, which spend millions of dollars on electioneering but don’t reveal their donors. As the *New York Times* recently reported, secretive tax-exempt groups outspent super PACs by a 3-to-2 margin in 2010, and “such groups have accounted for two-thirds of the political advertising bought by the biggest outside spenders so far in the 2012 election cycle.”¹⁷

III. LOOPHOLES IN CORPORATE DISCLOSURE LAW

Even though the cash flowing into elections after *Citizens United* has the potential to determine winners and losers at the polls, Americans are often in the dark about who controls the spigot. Current law offers various avenues by which corporations can engage in political spending without public disclosure. Closing these loopholes, and bringing transparency to corporate political activities, would yield benefits to shareholders, investors, and voters.

There are several ways under current law for corporations to engage in political electioneering without revealing their donors. *First*, although super PACs must report their donors, donations can be veiled by shunting them through shell corporations.¹⁸ For example, journalists investigating two corporations that each gave \$1 million to the super PAC supporting Mitt Romney discovered that the corporations had the same address, but neither seemed to actually have an office there, and neither appeared to engage in any business.¹⁹ Both companies were tied to a Utah multimillionaire, Steven Lund, who later acknowledged using them to donate in support of Romney.²⁰

Second, corporations can pass their political spending through nonprofit “social welfare” groups organized under section 501(c)(4) of the tax code. Many of these organizations are spending large sums on elections, and there is no requirement that they publicly disclose their donors.²¹ At least some of these groups appear to have little social purpose aside from spending to influence elections. One 501(c)(4), Crossroads GPS, has spent tens of millions of dollars on television ads in swing states attacking President Obama: it announced a \$25 million ad campaign in May and another \$25 million blitz in July.²² Among its donations, Crossroads GPS has reported two valued at \$10 million each, but the group did not publicly disclose the source of either donation.²³

Third, corporations underwrite substantial amounts of political advertising by routing donations through nonprofit trade organizations organized under section 501(c)(6) of the tax code. One of the largest 501(c)(6) spenders on elections is the U.S. Chamber of Commerce.²⁴ Corporations donate millions to the Chamber, which is not required to report the identities of its donors.²⁵ The Chamber is then able to leverage huge sums of corporate money to influence electoral outcomes, and intends to spend more \$100 million in the 2012

elections.²⁶ After a court decision required the disclosure of donors who support the type of political ad on which the Chamber has historically relied,²⁷ the organization announced that it would no longer sponsor that type of advertising and would switch to another that allows it to keep its donors secret.²⁸

IV. DISCLOSURE OF CORPORATE POLITICAL SPENDING BENEFITS INVESTORS, SHAREHOLDERS, AND DEMOCRACY

Disclosure of corporate political spending protects both shareholders and the proper functioning of American democracy. Corporate managers are currently largely free to make political expenditures according to their own interests because shareholders have little or no control over such spending; without disclosure, shareholders don't know about political spending, and so are unable to use corporate democracy to rein it in.

Half of American households own shares in major corporations — many through mutual funds, pensions, 401(k) accounts, and the like.²⁹ An increase in oversight of corporate political spending by shareholders, as well as the sunshine of public disclosure, would act as a democratizing influence on that spending. It would give a larger and more diverse portion of Americans influence over the financing of elections. That oversight cannot be exercised without information about spending.

The appetite for transparency in corporate spending on elections has been increasing in recent years among shareholders, citizens, and academics. A measure of shareholder interest is the increase in shareholder proposals concerning political spending. In 2011, 23% of shareholder proposals concerning social and environmental issues sought disclosure of political spending, and in 2012, the rate has increased to 31%.³⁰ Half of the S&P 100 companies that did not voluntarily disclose political spending saw shareholder proposals concerning political spending in 2011.³¹ During the 2012 shareholder meeting season, several corporations faced protests by shareholders and others demanding greater disclosure of political spending — some even going so far as to call for an end to all political spending by corporations.³²

The interest of shareholders and citizens generally can be seen in the reaction to a petition to the Securities and Exchange Commission seeking rules requiring disclosure of corporate political spending. The petition has received well over a quarter of a million comments — more comments than any petition in SEC history.³³ An analysis found that all but eight of these comments support mandatory disclosure, and all of the comments that have been submitted by institutional investors and government officials regarding the petition are in support.³⁴ One letter in support came from a group of mutual fund and institutional asset managers that manage more than \$690 billion.³⁵

The issue of transparency in corporate political spending is a hot topic among those who study corporations as well. Late in 2011, three major reports on corporate political spending and patterns of disclosure were released: the Robert Zicklin Center for Corporate Integrity at Baruch College released the Baruch Index of Corporate Political Disclosure;³⁶ the Center for Political Accountability and the Carol and Lawrence Zicklin Center for Business Ethics Research at the Wharton School of the University of Pennsylvania introduced the CPA-Zicklin Index of Corporate Political Accountability and Disclosure;³⁷ and the Sustainable Investments Institute released *Corporate Governance of Political Expenditures: 2011 Benchmark Report on S&P 500 Companies*.³⁸

Moreover, these reports reveal that many corporations are willing to answer the call for greater transparency. The CPA-Zicklin index concluded that disclosure of political spending is common among the largest publicly traded companies: fifty-seven of the S&P 100 companies disclose their political spending and impose board oversight or prohibit spending corporate money on politics altogether. The Sustainable Investments Institute report found that disclosure of political spending in the S&P 500 is not as common as in the S&P 100, although those that do disclose trend toward more expansive transparency, including transparency about who makes decisions regarding political spending and how much political spending companies do indirectly through trade associations. This research shows that disclosure of corporate political spending is both feasible and increasingly popular, although there is still great room for improvement.

A. Corporate Transparency Benefits Investors and Shareholders

Corporate disclosure of political expenditures presents a number of benefits, both to investors and to the market broadly. As an example of the latter, it can shed light on companies' practice of securing market advantages by cashing in on elected officials' gratitude for donations. This practice distorts the operation of the marketplace and can create a suboptimal distribution of capital because advantage is gained through political influence rather than genuine market value. Disclosure can also help to ensure that corporations do not violate campaign finance laws; violations would be far easier to detect if details about companies' spending were publicly available.

In addition to these broader benefits, disclosure of political expenditures by corporations would directly protect investors in two ways: (1) empowering investors' oversight concerning political spending and its effect on profits, and (2) allowing shareholders to ensure their money is not used to support candidates or causes that conflict with their personal beliefs. Both issues are clearly relevant to those who own stock in a given company, who have various ways to react to actions by corporate management, including voting against retention of the board and divesting their shares. But these issues also matter to *potential* investors who are deciding whether to buy stock in a particular company and seek to make an informed decision. Responsible investors learn about the companies whose stock they are considering buying as they attempt to ensure a return on their investment.

As an initial matter, transparency in political spending by corporations allows current and potential shareholders to monitor whether spending choices by corporate managers benefit a firm's bottom line. An example involving News Corporation illustrates how this dynamic plays out. In June 2010, News Corporation — which owns Fox News among many other media entities — donated \$1 million to the Republican Governors Association.³⁹ Rupert Murdoch, the founder, chairman, and CEO of the company, at first explained: “It had nothing to do with Fox News. The RGA [gift] was actually [a result of] my friendship with John Kasich.”⁴⁰ Kasich had previously hosted his own program on Fox News and, at the time, was a Republican candidate for governor of Ohio; Kasich went on to narrowly defeat Democratic incumbent Ted Strickland by a two point margin. Murdoch later explained that the donation was “in the interest of the country and of all the shareholders” and that his previous explanation was a “foolish throwaway line.”⁴¹ When asked whether shareholders might be permitted to be involved in the process of choosing political expenditures, Murdoch dismissed the possibility, saying: “No. Sorry, you have the right to vote us off the board if you don't like that.”⁴²

News Corporation's conduct is a glaring example of a manager acting in his own interest rather than the company's. Managers have considerable decision-making power regarding how to spend money, and shareholders have an interest in decisions about spending being made in the pursuit of corporate returns. Some political scientists have concluded that companies that spend money on elections have lower returns, and that their returns decrease as political spending rises.⁴⁵ Corporations making political donations may come close to—or venture over—the lines demarcating violations of campaign finance laws or prohibited pay-to-play activities. Criminal liability would obviously affect profits. In order to make well-informed decisions, investors must have information about actions by corporate management so they can assess whether a corporation's political spending helps or hurts the company's bottom line.

Distinct from their financial interest in the company's profit, shareholders also have a political or expressive interest in refraining from financially supporting political activities with which they disagree. Robust disclosure of corporate political spending gives shareholders the tools to ensure they invest only in companies with whose political spending they agree. In 2010, Target Corporation contributed \$150,000 to MN Forward, a PAC “that backs pro-business candidates in [Minnesota] statewide races, including a candidate for governor who opposes same-sex marriage.”⁴⁴ As a result of the contribution, Target was the subject of boycotts and extensive negative publicity. Beyond having concern with how political expenditures could harm Target's corporate image and profitability, shareholders asked the company to consider when contributing to political candidates “whether a candidate espouses policies that conflict with the company's values.”⁴⁵ At least one Target shareholder, a foundation that funds groups fighting against prejudice against gay, lesbian, bisexual, and transgender people, liquidated its stock in protest.⁴⁶ As Target Chairman, President, and CEO Gregg Steinhafel later explained in an apology letter to “Target Leaders,” he was “genuinely sorry” because the “decision affected many . . . in a way [he] did not anticipate.”⁴⁷ At the 2011 annual shareholder meeting, Steinhafel was so exasperated from receiving questions about Target's political contributions that he said, “Does anybody have a question relating to our business that is unrelated to political giving? I would love to hear any question related to something else.”⁴⁸

Target was not the only company to receive negative feedback as a result of its political activities. Replacements, Ltd., a North Carolina company that sells china, silver, and glassware, lobbied legislators, made monetary contributions, and even sold T-shirts in its showroom in an effort to oppose the state's Amendment One, which would ban same-sex marriage. Numerous customers expressed disagreement with the company's actions and vowed to conduct no further business with the company.⁴⁹ As this example shows, harm to a company's bottom line can occur for engaging in any political activity, regardless of the viewpoint expressed.

Disagreement with the Target and Replacements, Ltd. contributions went beyond shareholders, and some of the Target shareholders were no doubt more concerned with the financial effect on the company of negative publicity and boycotts than with their own political views. Nevertheless, the situations illustrate what can occur when corporate activities and shareholder ideals collide. Had Target's expenditures not been disclosed, shareholders would not have been aware that the company they owned was acting contrary to their personal beliefs. Some shareholders may want to divest from a company that supports candidates or causes they disagree with, and some may want to exercise control over management to prevent such expenditures. Neither is possible without disclosure.

B. Corporate Transparency Benefits Democracy

Disclosure of political expenditures also promotes other goals that are not specific to investors. In the landmark case *Buckley v. Valeo*,⁵⁰ the U.S. Supreme Court affirmed the constitutionality of disclosure requirements for candidates and political committees on the basis of three specific interests: the voters' interest in information about the source of political spending, the interest in deterring and revealing corruption, and the interest in preventing circumvention of the law through loopholes. There is also a due process interest in disclosure in the context of judicial elections.

The informational interest. As the Supreme Court noted, voters have an interest in knowing “where political campaign money comes from and how it is spent by the candidate in order to aid the voters in evaluating those who seek . . . office.”⁵¹ Knowing who is speaking allows voters to better understand the messages they receive and “to place each candidate in the political spectrum more precisely than is often possible solely on the basis of party labels and campaign speeches.”⁵²

Outside political spenders have a storied history of hiding behind deceptive organization names to obfuscate the true source of funds. A few years ago in Colorado, an organization named “‘Littleton Neighbors Voting No’ spent \$170,000 to defeat a restriction that would have prevented Wal-Mart from coming to town.”⁵³ While the name of this organization might evoke images of a grassroots group of people coming together in the small Colorado town of about 41,000 people, it was later revealed that the organization was funded exclusively by Wal-Mart.⁵⁴ Indeed, this is just one of the latest examples in a long line of misleading monikers that has been extensively documented, including by the Supreme Court. In rejecting an earlier challenge to a disclosure law, the Court explained:

Curiously, Plaintiffs want to preserve the ability to run these advertisements while hiding behind dubious and misleading names like: ‘The Coalition—Americans Working for Real Change’ (funded by business organizations opposed to organized labor) [and] ‘Citizens for Better Medicare’ (funded by the pharmaceutical industry) Given these tactics, Plaintiffs never satisfactorily answer the question of how ‘uninhibited, robust, and wide-open’ speech can occur when organizations hide themselves from the scrutiny of the voting public.⁵⁵

Disclosure prevents companies from masking their spending, allowing the public to know the sources of electoral advertising.

The anti-corruption interest. “[D]isclosure requirements deter actual corruption and avoid the appearance of corruption by exposing large contributions and expenditures to the light of publicity,” making them harder to hide.⁵⁶ As the Supreme Court put it in *Buckley*, “[p]ublicity is justly commended as a remedy for social and industrial diseases. Sunlight is said to be the best of disinfectants”⁵⁷

For example, some corporations engage in the practice of “bet hedging,” where a corporation gives comparable amounts of funding to competing candidates or parties.⁵⁸ Rather than supporting a particular candidate and his or her policies, such expenses seem only to be intended to secure a post-election benefit “whatever the outcome of the election.”⁵⁹ “[I]f a donor hedges its bets, it is presumptively engaging in a *quid*

pro quo transaction: contributions now, benefits later.”⁶⁰ Furthermore, it is sometimes elected officials who seek to extort corporations. Decision makers may threaten to give a government contract to a competitor or refuse to advance legislation if a corporation refuses a politician’s demands for contributions. As the Supreme Court explained in its (since partially overruled) *McConnell* opinion, “Particularly telling is the fact that, in 1996 and 2000, more than half of the top 50 soft-money donors gave substantial sums to *both* major national parties, leaving room for no other conclusion but that these donors were seeking influence, or avoiding retaliation, rather than promoting any particular ideology.”⁶¹

The anti-circumvention interest. The third interest is the anti-circumvention interest in ensuring that contribution limits are not evaded through the exploitation of loopholes. Entities that are forbidden from making contributions should not be permitted to launder contributions by passing them through organizations that can make such contributions. Disclosure of the source of the spending assists in preventing this.

The due process interest. Political spending in at least one type of election — those involving the election of state and local judges — implicates an additional, fourth interest: the due process rights of litigants. The Supreme Court has held that due process requires the recusal of an elected state supreme court justice who was elected with the help of large sums of money from one of the parties to a lawsuit.⁶² Although the Court specifically declined to determine whether the judge involved in the case was in fact biased,⁶³ it held that the “probability of actual bias on the part of the judge . . . [was] too high to be constitutionally tolerable” and required recusal.⁶⁴ Given this ruling, a litigant who does not know if his or her opponent spent significant sums of money to elect the judge hearing his or her case lacks the information needed to assess whether the court in question is truly an impartial tribunal. Ensuring that any political spending by corporate litigants is disclosed, therefore, helps to protect the due process rights of parties engaged in legal disputes with such companies.

V. REQUIRING DISCLOSURE OF CORPORATE POLITICAL SPENDING FURTHERS IMPORTANT CONSTITUTIONAL VALUES

While *Citizens United* led to a dramatic increase in spending in elections, the opinion had a less mentioned, but very important second half. By an 8-1 vote, the *Citizens United* Court strongly approved of mandatory disclosure of political expenditures. Citing the voters’ interest in knowing who is speaking about candidates, the Court upheld the constitutionality of the disclosure and disclaimer provisions of the law before it.⁶⁵ The Court went on to specifically address disclosure of corporate political activity:

[P]rompt 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.⁶⁶

Citizens United reaffirmed a long line of Supreme Court decisions upholding disclosure requirements designed to provide voters with the facts they need to make informed choices, and these decisions clearly establish that requiring disclosure of corporate political expenditures does not violate the First Amendment.⁶⁷ In fact, First Amendment values are furthered by disclosure, since it allows citizens and shareholders to determine the weight they should give to different speakers and messages by considering the sources of their funding. Lower court decisions since *Citizens United* have recognized these values and have consistently upheld campaign finance disclosure laws, showing that their constitutionality is beyond question.⁶⁸ *Citizens United* emphasized the individual rights of corporations, but recognized that the owners of the corporations should have some control over how their money is spent. In order to exercise such control, shareholders must have knowledge about corporate activities.

VI. HOW TO ACHIEVE DISCLOSURE OF CORPORATE POLITICAL SPENDING

Requiring disclosure of corporate political spending would produce numerous benefits for the investor community and the body politic. *How* to achieve full transparency around corporate political spending, however, presents a separate question. Various solutions are available at least in theory: disclosure policies could be adopted by companies voluntarily, through regulation by the states, or through federal regulation. Federal regulation is the superior option because of the nationwide application that federal rules would have and the uniformity they would bring to a system of disclosure. Because the problems with the other two possibilities help illustrate the strengths of the federal solution, they are discussed first.

A. Company-by-Company Disclosure

As noted above, recent years have seen greater numbers of corporations voluntarily disclosing their political spending. And this year's shareholder meeting season has seen a number of proposals that would add to that number, if adopted. Although this is an encouraging sign, it does not meaningfully address the interests just discussed. For one thing, a corporation that reports voluntarily can always stop reporting. And without external oversight, there is no guarantee that the disclosure will be as robust as it should be. Each business that chooses to disclose its political spending may define political spending slightly differently, making it hard for investors to compare. For example, Boeing did not include in its voluntary disclosures an in-kind donation of advertising worth \$200,000 to a group opposing a ballot initiative.⁶⁹ When the donation came to light, the company argued that it did not qualify as a "political contribution." Other companies would classify this expenditure differently. Finally, such a decentralized system of disclosure creates logistical obstacles for those who want to access the information. Companies may release the information in different formats, preventing apples-to-apples comparisons.

B. State-by-State Disclosure

There are two different strategies a state government might utilize to achieve disclosure of corporate political expenditures. The first strategy is regulation through election laws, which would require all entities, corporate and otherwise, to disclose whether they make political expenditures in elections within the state. The second

strategy is regulation through corporate laws, by requiring all corporations within the power of the state to regulate to disclose their political expenditures. Both of these options present difficulties.

First, states could use election law to require disclosure of corporate political spending. Election-based disclosure is premised on a state's broad power to conduct and regulate elections. One facet of that power is the state's ability to require the disclosure of political expenditures in order to further the interests discussed above. This power is circumscribed, however, by the restriction that states can regulate state and local elections, but not federal elections. Federal elections are those that involve the selection of federal officials, such as the President of the United States and members of Congress. State elections, on the other hand, involve elections to select officials such as the Governor and members of the state legislature, and local elections may involve posts such as mayor or school board member. The elections clause in the United States Constitution provides that the states can regulate federal elections, "but the Congress may at any time by Law make or alter such Regulations."⁷⁰ Congress has chosen to extensively regulate in the area of federal elections and has expressly preempted state regulation,⁷¹ meaning the federal government has forbidden the state governments from regulating federal elections. Therefore, any attempt by states to require disclosure in federal elections will fail, absent action by Congress. Hence, states can only regulate state and local elections; they cannot rely on their election-regulating authority to require disclosure of corporate spending in federal elections.

Second, states could turn to corporate law to regulate corporate political transparency. The ability of businesses to incorporate is a feature of state law, and states regulate corporations in various ways. The state has an interest in regulating the relationship between public corporations and those who own stock in them in order to ensure the well-being of shareholders. Since many corporations do business in more than one state and state laws can conflict with one another, nearly all states have adopted the "internal affairs doctrine," which states that "a corporation's internal affairs — matters peculiar to the relationships among or between the corporation and its current officers, directors, and shareholders" are regulated by "the law of the state of incorporation."⁷² A corporation's state of incorporation is the state where the corporation was initially created and registered with a state government. A corporation is known as a "domestic corporation" within the state in which it is incorporated and a "foreign corporation" everywhere else.

Each state could compel domestic corporations to disclose political expenditures at all levels: federal, state, local, and even expenditures in foreign countries. Such state corporate disclosure rules would go hand in hand with the reporting requirements of federal securities law.⁷³ As a general matter, a federal law can trump — or "preempt" — state laws that concern the same subject as the federal law. However, federal securities law expressly allows the states to regulate disclosures for domestic corporations.⁷⁴ And since it would be possible for a corporation to comply with both federal disclosure requirements and any state laws that mandated disclosure of political spending, there would be no conflict between state and federal regimes that would warrant federal preemption.⁷⁵

But because of the internal affairs doctrine, a state cannot use its corporate law to require businesses incorporated in other states to disclose their political spending. Consequently, a company incorporated in Delaware is free to anonymously spend as much as it wants (subject to other laws, such as each state's

election-based disclosure laws and contribution limits) in every state as long as Delaware chooses not to require that corporations disclose political expenditures.

Even if a state were to combine the election-based and corporation-based strategies, the state could, at most, (1) require domestic corporations — corporations incorporated in the state — to disclose all political expenditures to their shareholders, regardless of whether those expenditures are in federal, state, or local elections and (2) require all corporations, regardless of their state of incorporation, to disclose all political expenditures in state and local elections, but not federal elections. Thus, even the most robust disclosure regulation by states would leave open significant loopholes.

Furthermore, state regulation would lead to a patchwork of different disclosure schemes. Some states' laws might be stronger than others, might require fewer disclosures than others, or might be enforced with different degrees of vigor than others. And investors trying to keep track of corporate political spending would have to search as many as fifty different databases to track down all of any given company's expenditures. Moreover, some states might never even enact disclosure laws, leaving the public with incomplete information. Though state regulation would be a step in the right direction, it would be a necessarily incomplete step.

C. Federally Mandated Disclosure: The Best Solution

Federal regulation would not suffer from the same limitations as state-by-state regulation. The federal government already engages in significant oversight of publicly held corporations through federal securities laws.⁷⁶ Given the keen interest of investors and the public in the issue, the SEC clearly has the statutory authority to add political spending to the disclosures required of publicly held corporations. The Securities Exchange Act of 1934 created the SEC and gives it “complete discretion . . . to require in corporate reports . . . such information as it deems necessary or appropriate in the public interest or to protect investors.”⁷⁷ A “philosophy of full disclosure” is the “fundamental purpose” of the Securities Exchange Act; disclosure is necessary “to achieve a high standard of business ethics in the securities industry.”⁷⁸

Just as states do not have the power to regulate federal elections, Congress is limited in its ability to regulate state elections.⁷⁹ However, the federal government clearly has the power to regulate publicly held companies in order to protect investors in securities under the broad grant of power derived from the Commerce Clause of the U.S. Constitution.⁸⁰ The disclosure of political spending is a vital part of that mission. Such a rule is a far cry from the intrusions on states' regulation of the internal affairs of corporations that courts have found raise federalism concerns. In fact, courts use mandatory disclosure as a benchmark of permissible federal regulation to contrast with actions that infringe on states' power.⁸¹ Federalism concerns are greatest where federal regulation would “interfere with” or “override[]” state corporate law.⁸² But an expansion in the scope of disclosures mandated by SEC regulations would cause no interference with the states' regulation of corporations' internal affairs and could be enforced in parallel with any state-imposed disclosure requirements. Indeed, an SEC rule could exist in harmony with strong state laws requiring disclosure of corporate spending on elections, like those discussed above.

The SEC should promulgate regulations requiring public corporations to disclose all of their political expenditures on a periodic basis. As SEC Commissioner Aguilar has said, “[a]rming investors with the information they need to facilitate informed decision-making is a core responsibility of the SEC. In fact, it is one of the factors that led to the creation of the SEC.”⁸³ In particular, such disclosures should include political contributions, independent expenditures, electioneering communications, and contributions to organizations that undertake these activities. Political expenditures at all levels of government—federal, state, and local—should all be reported. Each entry should include specific information, including the identity of any candidates involved, whether the payment supports or opposes the candidate, the amount of the expenditure, and the date of the expenditure. Similar information should be collected with regard to ballot initiatives, referenda, and other issues put to a public vote.

Political expenditures should be reported quarterly on a company’s Form 10-Q filing with the SEC.⁸⁴ A central database that included all disclosures nationwide would be far easier for shareholders and voters alike to navigate than fifty separate databases maintained by the states. Reviewing disclosure forms can be an involved, labor-intensive process. While private efforts have been made to consolidate state disclosures into one central database,⁸⁵ regulation that created a nationwide database would be uniform and dependable. The SEC can easily incorporate the collection of this information into its preexisting EDGAR filing system, which already receives thousands of electronic filings daily. This information would then be freely available to shareholders and voters through the Internet, with many filings being posted on the same day they are submitted.

* * * * *

Recent legal changes have created an electoral environment fraught with new risks for shareholders and voters alike. Corporate spending on elections may impact the fiscal health of corporations and has the potential to distort the operation of the market. Shareholders may unknowingly fund activity that conflicts with their political beliefs. Voters can be kept in the dark about the sources of advertisements designed to influence their votes. Disclosure, however, would minimize these risks: shareholders would know how their companies are spending money and voters would know who is funding political speech.

While *Citizens United* prompted increased corporate spending on politics, the decision also contained the seeds of the solution. The Supreme Court strongly approved of laws requiring disclosure of political expenditures and noted the importance of well-functioning corporate democracy. As the Court succinctly put it, “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.”⁸⁶ Such prompt disclosure is not required by current law, but an SEC rule would change that. In the words of SEC Commissioner Aguilar, “Investors are not receiving adequate disclosure, and as the investors’ advocate, the Commission should act swiftly to rectify the situation by requiring transparency.”⁸⁷

ENDNOTES

¹ 130 S. Ct. 876 (2010).

² *Id.*, at 916 (internal citations and quotation marks omitted).

³ Luis A. Aguilar, Comm’r, U.S. Securities & Exchange Comm’n, Address at the Practicing Law Inst. SEC Speaks in 2012 Program (Feb. 24, 2012), *available at* <http://www.sec.gov/news/speech/2012/spch022412laa.htm> (“The Commission should provide for disclosure of corporate political expenditures that results in uniform and consistent disclosure.”).

⁴ Formally speaking, *Citizens United* permits corporations and unions to fund “independent expenditures” and “electioneering communications.” “Independent expenditures” are political expenditures that support or oppose the election of a political candidate in express terms—“vote for” or “defeat”—but are uncoordinated with any candidate. “Electioneering communications” are broadcast advertisements, made in the weeks immediately before an election that mention a candidate, without expressly advocating for the candidate’s election or defeat—“call Senator Smith and tell her to be tough on crime.” *See, e.g.*, 2 U.S.C. §§ 431(8), (17); 434(f)(3). Many states have similar definitions.

⁵ 599 F.3d 686, 698 (D.C. Cir. 2010).

⁶ COMM. FOR ECON. DEV. SUBCOMM. ON MONEY IN POLITICS, AFTER *CITIZENS UNITED*: IMPROVING ACCOUNTABILITY IN PUBLIC FINANCE 3 (2011), *available at* http://www.ced.org/images/content/events/moneyinpolitics/2011/38751_citizensunited.pdf

⁷ *Id.* at 3.

⁸ *Id.* at 2.

⁹ *Id.*

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¹⁸ *See, e.g.*, Jonathan D. Salant, *Payday Lender Political Donors Hidden in Corporate Names*, BLOOMBERG (Mar. 21, 2012), <http://www.bloomberg.com/news/2012-03-22/payday-lender-political-donors-hidden-in-corporate-names.html> (describing businesses’ use of limited liability corporations to secretly donate to super PAC supporting Romney).

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- ²³ Matea Gold, *Secret Donors Pour Millions of Dollars into Crossroads GPS*, L.A. TIMES, Apr. 18, 2012, at A5.
- ²⁴ *The Chamber of Secrets*, ECONOMIST, Apr. 21, 2012, <http://www.economist.com/node/21553020> (stating that the Chamber was the biggest spender in the 2010 elections, excepting the two political parties).
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⁵⁰ 424 U.S. 1, 66-68 (1976).

⁵¹ *Id.* at 66-67 (internal citation and quotation marks omitted).

⁵² *Id.* at 67.

⁵³ *The First Amendment and Campaign Finance Reform After Citizens United*, *Hearing Before the H. Comm. on the Judiciary*, 111th Cong. 11 (2010) (statement of Monica Youn, Counsel and Director of the Campaign Finance Project, Brennan Center for Justice), *available at* <http://judiciary.house.gov/hearings/pdf/Youn100203.pdf>.

⁵⁴ *Id.*

⁵⁵ *McConnell v. FEC*, 540 U.S. 93, 197 (2003), *overruled in part by Citizens United v. FEC*, 130 S. Ct. 876 (2010) (quoting *McConnell v. FEC*, 251 F. Supp. 2d 176, 237 (D.D.C. 2003)).

⁵⁶ *Buckley*, 424 U.S. at 67.

⁵⁷ *Id.* (quoting *LOUIS BRANDEIS, OTHER PEOPLE’S MONEY* 62 (1933)).

⁵⁸ Jason Cohen, *The Same Side of Two Coins: The Peculiar Phenomenon of Bet-Hedging in Campaign Finance*, 26 *N. ILL. U. L. REV.* 271, 274-75 & n.13 (2006).

⁵⁹ *Id.* at 275.

⁶⁰ *Id.* at 306. Of course, there are reasons why a donor might hedge bets without intending to engage in a quid pro quo transaction. *See id.* at 306-15.

⁶¹ *McConnell*, 540 U.S. at 148.

⁶² *Caperton v. A.T. Massey Coal Co.*, 556 U.S. 868, 886 (2009).

⁶³ *Id.* at 882.

⁶⁴ *Id.* at 872.

⁶⁵ *Citizens United*, 130 S. Ct. at 915-16.

⁶⁶ *Id.* at 916 (internal citations and quotation marks omitted).

⁶⁷ *Id.* at 914-16.

⁶⁸ See, e.g., *Family PAC v. McKenna*, Nos. 10–35832, 10–35893, 2012 WL 266111, at *6 (9th Cir. Jan. 31, 2012) (upholding \$25 and \$100 disclosure thresholds for reporting information about contributors to political committees that support ballot measures); *Nat’l Org. for Marriage v. Daluz*, 654 F.3d 115, 118 (1st Cir. 2011) (finding that “relatively small imposition” for disclosing information about independent expenditures is related to government interest in providing electorate with key information); *Nat’l Org. for Marriage v. McKee*, 649 F.3d 34, 41 (1st Cir. 2011) (upholding Maine’s political committee financial disclosure requirements and finding that provisions “neither erect a barrier to political speech nor limit its quantity”), *aff’d* No. 11-1196, 40 (1st Cir. Jan. 31, 2012) (finding that “ballot question committee” law, like PAC laws, are constitutional and that “transparency is a compelling objective”), *cert. denied*, No. 11-559 (U.S. Feb. 27, 2012); *Human Life of Wash. Inc. v. Brumsickle*, 624 F.3d 990, 1013 (9th Cir. 2010) (upholding Washington’s political committee financial disclosure requirements and noting, “indeed, it is the Supreme Court’s decision in *Citizens United* . . . that provides the best guidance regarding the constitutionality of the Disclosure Law’s requirements.”); *SpeechNow.org v. FEC*, 599 F.3d 686, 696–97 (D.C. Cir. 2010) (upholding ongoing disclosure requirements for organizations making independent expenditures; finding “*Citizens United* upheld disclaimer and disclosure requirements for electioneering communications as applied to *Citizens United*, again citing the government’s interest in providing the electorate with information”); *Justice v. Hosemann*, 829 F.Supp.2d 504, 519 (N.D. Miss. 2011) (holding that Mississippi’s disclosure forms are not “overly intrusive” and that \$200 threshold amount is rational and substantially related to government’s important informational interest); *ProtectMarriage.com v. Bowen*, 830 F.Supp.2d 914, 936 (E.D. Cal. 2011) (finding that alleged harassment related to financial support of Proposition 8 did not warrant exception from general disclosure laws); *Nat’l Org. for Marriage, Inc. v. Roberts*, 753 F.Supp.2d 1217, 1222 (N.D. Fla. 2010) (finding that Florida disclosure requirements connected to “electioneering communications organizations” “would not prohibit [plaintiff] from engaging in its proposed speech”); *Yamada v. Kuramoto*, No. 10-00497 JMS/LEK, 2010 WL 4603936, at *1 (D. Haw. Oct. 29, 2010) (finding that “*Citizens United* also endorsed disclosure”); *Iowa Right to Life Comm., Inc. v. Smithson*, 750 F.Supp.2d 1020, 1026 (S.D. Iowa 2010) (finding “under *Citizens United*, [t]he Government may regulate corporate political speech through disclaimer and disclosure requirements” (alteration in original)); *Wis. Club for Growth, Inc. v. Myse*, No. 10-CV-427-WMC, 2010 WL 4024932, at *5 (W.D. Wis. Oct. 13, 2010) (refusing to enjoin Wisconsin’s disclosure regulations; noting “[P]laintiffs’ reliance on *FEC v. WRTL* ignores the Supreme Court’s later treatment of disclosure and disclaimer regulations in *Citizens United*”); *Ctr. for Individual Freedom v. Madigan*, 735 F. Supp. 2d 994, 1000 (N.D. Ill. 2010) (upholding Illinois’ registration, disclosure, and reporting provisions; noting “in *Citizens United*, the Supreme Court expressly rejected the contention that election-law disclosure requirements are limited to express advocacy or its functional equivalent”).

⁶⁹ Ameet Sachdev, *Political Advocacy Piques Shareholders’ Interest*, CHI. TRIB., May 18, 2012, at C1.

⁷⁰ U.S. CONST. art. I, § 4.

⁷¹ 2 U.S.C. § 453(a) (“[T]he provisions of this Act, and of rules prescribed under this Act, supersede and preempt any provision of State law with respect to election to Federal office.”).

⁷² 19 C.J.S. *Corporations* § 981 (2011).

⁷³ See, e.g., 15 U.S.C. § 78m (requiring periodic disclosures by issuers of securities).

⁷⁴ 15 U.S.C. § 77r(a)(2)(B).

⁷⁵ See *English v. General Elec. Co.*, 496 U.S. 72, 79 (1990) (“[S]tate law is pre-empted to the extent that it actually conflicts with federal law. Thus, the Court has found pre-emption where it is impossible for a private party to comply with both state and federal requirements”).

⁷⁶ See, e.g., Securities Act of 1933, 15 U.S.C. §§ 77a-77aa; Securities Exchange Act of 1934, 15 U.S.C. § 78a-78pp.

⁷⁷ *Nat’l Resources Def. Council v. SEC*, 606 F.2d 1031, 1051 (D.C. Cir. 1979). See also, e.g., Section 14(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78n(a). Generally, the SEC has the power to “make such rules and regulations as may be necessary or appropriate to implement the provisions” of the Act. 15 U.S.C. § 78w(a)(1).

⁷⁸ *Basic Inc. v. Levinson*, 485 U.S. 224, 234 (1988).

⁷⁹ See *Oregon v. Mitchell*, 400 U.S. 112 (1970) (holding that Congress does not have the power extend the franchise to 18 year olds in state elections). Congress can regulate state elections under specific constitutional grants of power, such as the Fifteenth Amendment's prohibition on race-based voting requirements. See U.S. CONST. amend. XV.

⁸⁰ U.S. CONST. art. I, § 8 (“The Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States, and with the Indian tribes.”).

⁸¹ See, e.g., *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 478-80 (1977); *Bus. Roundtable v. SEC*, 905 F.2d 406, 410-411 (D.C. Cir. 1990).

⁸² *Santa Fe*, 430 U.S. at 479.

⁸³ Aguilar, supra note 3.

⁸⁴ See 17 C.F.R. 240.13a-13 (requiring quarterly filing of Form 10-Q by issuers).

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⁸⁷ Aguilar, supra note 3.