



Statement to the House Committee on Financial Services
Subcommittee on Capital Markets and Government Sponsored Enterprises

**Hearing on Corporate Governance:
Fostering a System that Promotes Capital Formation and Maximizes Shareholder Value**

September 21, 2016
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Rayburn House Office Building, Room 2128

SEC Rule 14a-8: Ripe for Reform

James R. Copland
Senior Fellow and Director, Legal Policy
Manhattan Institute for Policy Research
52 Vanderbilt Avenue
New York, NY 10017

The Manhattan Institute for Policy Research does not take institutional positions on legislation, rules, or regulations. Although my comments draw upon my long-running research on shareholder proposals and corporate governance as an Institute scholar, my statement before the subcommittee is solely my own, not my employer's.

About Mr. Copland

James R. Copland is a senior fellow at the Manhattan Institute, where he has served as director of legal policy since 2003.¹ He has authored many policy reports; book chapters; articles in academic journals including the *Harvard Business Law Review* and *Yale Journal on Regulation*; and opinion pieces in publications including the *Wall Street Journal*, *National Law Journal*, and *USA Today*. Mr. Copland has testified before Congress as well as state and municipal legislatures; speaks regularly on civil- and criminal-justice issues; has made hundreds of media appearances in such outlets as PBS, Fox News, MSNBC, CNBC, Fox Business, Bloomberg, C-Span, and NPR; and is frequently cited in news articles in periodicals including the *New York Times*, *Washington Post*, *The Economist*, and *Forbes*.

In 2011, Mr. Copland helped launch the Manhattan Institute's Proxy Monitor database,² a publicly available catalogue of shareholder proposals at the 250 largest publicly traded American companies, by revenues, as determined by *Fortune* magazine.³ Mr. Copland has periodically authored or co-authored findings and reports on the shareholder-proposal process,⁴ as well as writing on the subject in popular⁵ and academic⁶ journals. In 2011 and 2012, Mr. Copland was named to the National Association of Corporate Directors "Directorship 100" list, which designates the individuals most influential over U.S. corporate governance.⁷

Prior to joining the Manhattan Institute, Mr. Copland served as a management consultant with McKinsey and Company in New York and as a law clerk for Ralph K. Winter on the U.S. Court of Appeals for the Second Circuit. Mr. Copland has been a director of two privately held manufacturing companies since 1997 and has served on multiple government and nonprofit boards. He holds a J.D. and an M.B.A. from Yale University, where he was an Olin Fellow in Law and Economics and a Teaching Fellow in Macroeconomics and Game Theory; an M.Sc. in Politics of the World Economy from the London School of Economics and Political Science; and a B.A. in Economics, with highest distinction and highest honors, from the University of North Carolina at Chapel Hill, where he was a Morehead Scholar and was awarded the Honors Prize in Economics.

¹ See James R. Copland, <https://www.manhattan-institute.org/expert/james-r-copland>. The Manhattan Institute is a non-profit, non-partisan think tank developing ideas that foster economic choice and individual responsibility. See About MI, <https://www.manhattan-institute.org/about>.

² See Proxy Monitor, <http://www.proxymonitor.org/> ("ProxyMonitor.org is a unique, publicly available database that tracks shareholder proposals in real time.").

³ See Fortune 500, <http://beta.fortune.com/fortune500/> ("In total, Fortune 500 companies represent two-thirds of the U.S. GDP with \$12 trillion in revenues, \$840 billion in profits, \$17 trillion in market value, and employ 27.9 million people worldwide."). Because several of the Fortune 250 companies are not publicly traded, some of the companies among the 250 largest that are subject to SEC proxy rules are from the broader Fortune 300 group.

⁴ See Proxy Monitor, Reports and Findings, http://proxymonitor.org/Forms/reports_findings.aspx.

⁵ See, e.g., James R. Copland, *Getting The Politics out of Proxy Season*, WALL ST. J., Apr. 23, 2015, available at <https://www.manhattan-institute.org/html/getting-politics-out-proxy-season-5461.html>; Copland, *Politicized Proxy Advisers vs. Individual Investors*, WALL ST. J., Oct. 7, 2012, available at <https://www.manhattan-institute.org/html/politicized-proxy-advisers-vs-individual-investors-3863.html>.

⁶ See James R. Copland, *Against an SEC-Mandated Rule on Political Spending Disclosure: A Reply to Bebchuk and Jackson*, 3 HARV. BUS. L. REV. 381 (2013).

⁷ See NACD 2012 Honorees, <https://www.nacdonline.org/directorship100/2012honorees.cfm> ("Each year, NACD Directorship identifies the most influential people in the boardroom community, including directors, corporate governance experts, journalists, regulators, academics and counselors.").

Written Statement

Chairman Garrett, Ranking Member Maloney, and members of the Subcommittee, my name is James R. Copland. Since 2003, I have been a senior fellow with and director of legal policy for the Manhattan Institute for Policy Research, a public-policy think tank in New York City. Although my comments draw upon my research conducted for the Manhattan Institute,⁸ my statement before the subcommittee is solely my own, not my employer's.

I would like to thank you for the invitation to testify today. One of the topics of focus for today's hearing has constituted a significant focus in my recent research: the shareholder-proposal process governed by the Securities and Exchange Commission's Rule 14a-8. I will leave discussion of new disclosure rules under the FAST Act and Dodd-Frank Act to other witnesses, although I will share some of my specific research related to proposed additional disclosures of corporate political spending and lobbying, which are a matter of current controversy.

Summary of Argument

The SEC's Rule 14a-8 permits stockholders of publicly traded companies who have held shares valued at \$2,000 or more for at least one year to introduce proposals for shareholders' consideration at corporate annual meetings.⁹ The SEC's process is ripe for reform:

- The shareholder-proposal process has strayed far from the principal legal purpose authorizing the rule under the Securities Exchange Act—namely ensuring that shareholders obtain adequate, non-deceptive disclosures to inform their investment decisions.
- The shareholder-proposal process has been used almost exclusively by a small number of investors, with a focus potentially or actually centered on concerns other than maximizing share value—the principal state corporate law focus that defines directors' and managements' fiduciary duties.
- The shareholder-proposal process has actually operated to permit such minority shareholders to extract corporate rents or influence corporate behavior to the detriment of the average diversified shareholder.

Potential solutions to this problem include:

⁸ Some language in this testimony may be identical to that in the author's previous publications. In addition, I have included the following Manhattan Institute reports as appendices, to be incorporated by reference: James R. Copland & Margaret M. O'Keefe, *Proxy Monitor: A Report on Corporate Governance and Shareholder Activism* (Manhattan Institute 2015), available at http://www.proxymonitor.org/Forms/pmr_11.aspx; Tracie Woidtke, *Public Pension Fund Activism and Firm Value* (Manhattan Institute 2015), available at <https://www.manhattan-institute.org/html/public-pension-fund-activism-and-firm-value-7871.html>. Some data and analysis in this testimony draw upon that developed for the Manhattan Institute's 2016 Proxy Monitor report, to be released later this fall, authored by myself with Ms. O'Keefe.

⁹ See 17 C.F.R. § 240.14a-8 (2007) [hereinafter *14a-8*].

- Revisiting the SEC’s 1976 rule forcing companies to include on their proxy ballots most shareholder proposals that involve “substantial policy . . . considerations”—an approach I have publicly favored.¹⁰
- Forcing shareholder-proposal sponsors to reimburse the corporation at least some portion of the direct costs of assessing, printing, distributing, and tabulating their proposals if any proposal fails to receive majority or threshold shareholder support—an idea suggested by Yale Law professor Roberta Romano.¹¹
- Revising the SEC’s rule permitting companies to exclude resubmitted shareholder proposals if they fail to garner minimum threshold shareholder support within the preceding five calendar years¹²—an idea suggested by the U.S. Chamber of Commerce and other business groups in a 2014 rulemaking petition submitted to the SEC.¹³

I focus my testimony on the following subjects:

- (1) the legal background surrounding Rule 14a-8;
- (2) the principal sponsors of shareholder proposals;
- (3) the principal subject matters of shareholder proposals;
- (4) shareholder-proposal voting results;
- (5) the role of proxy-advisory firms;
- (6) shareholder-proposal resubmissions;
- (7) the controversy surrounding corporate disclosure of political spending and lobbying; and
- (8) the potential value-destroying impact of social-issue investing on public-employee pension funds.

1. Legal Background

Pursuant to its authority under the Securities Exchange Act of 1934,¹⁴ the SEC first promulgated a “shareholder proposal rule”—the antecedent to the current Rule 14a-8—in 1942.¹⁵ Then-SEC chairman Ganson Purcell explained the purpose of the rule to the House Interstate and Foreign Commerce Committee as follows:

Once a shareholder could address a meeting[;] today he can only address the assembled proxies which are lying at the head of the table. The only opportunity that the stockholder has of expressing his judgment comes at the time when he considers the execution of the proxy form, and we believe, whether we are right and whether we are wrong—and I think

¹⁰ See James R. Copland (2015), *supra* note 5.

¹¹ See Roberta Romano, *Less Is More: Making Institutional Investor Activism a Valuable Mechanism of Corporate Governance*, 18 YALE J. REG. 174, 229–49 (2001).

¹² See 14a-8, *supra* note 9, at 14a-8(i)(12).

¹³ See Thomas Quaadman, *Request for Rulemaking to Amend Rule 14a-8 under the Securities Exchange Act of 1934 Regarding Resubmission of Shareholder Proposals* (Apr. 9, 2014).

¹⁴ Pub. L. No. 73-291, Ch. 404, 48 Stat. 881 (1934) (codified at 15 U.S.C. §§ 78a–78oo (2006 & Supp. II 2009)), at §§ 78m, 78n & 78u; 15 U.S.C. §§ 80a-1 to 80a-64 (2000) (pursuant to Investment Company Act of 1940, Pub. L. No. 76-768, 54 Stat. 841(1940)).

¹⁵ See Securities Exchange Act of 1934 Release No. 3347 (Dec. 18, 1942), 7 Fed. Reg. 10,653 (1942).

we are right—that that is the time he should have the full information before him and the ability to take action as he sees fit.

The proxy solicitation is now in fact the only means by which a stockholder can act and can perform the functions which are his as owner of the corporation. It, therefore, seems clear to us that only by making the proxy a real instrument for the exercise of those functions can we obtain what the Congress and this committee called for in the form of “fair corporate suffrage.”¹⁶

In a 1945 opinion release, the director of the SEC’s division of corporate finance explained:

Speaking generally, it is the purpose of [the shareholder proposal rule] to place stockholders in the position to bring before their fellow stockholders matters of concern to them as stockholders in such corporation; that is, such matters relating to the affairs of the company concerned as are proper subjects of stockholders’ action under the laws of the state under which it was organized. It was not the intent of [the rule] to permit stockholders to obtain the consensus of other stockholders with respect to matters which are of a general political, social or economic nature. In short, [the rule] should operate so as to leave intact the primary substantive regulation which state law seeks to achieve.¹⁷

The opinion release was predicated on the well-founded understanding that the Securities Exchange Act’s delegation of powers overseeing the proxy process to the SEC did not alter the substantive rights governing such measures, which would remain largely a question of state corporate law.¹⁸ In 1952, the SEC again emphasized that companies could exclude shareholder proposals that were introduced “primarily for the purpose of promoting general economic, political, racial, religious, social, or similar causes.”¹⁹

¹⁶ Hearings on H.R. 1498, H.R. 1821, and H.R. 2019, Before the House Committee on Interstate and Foreign Commerce, 78th Cong., 1st Sess., pt. 2, at 174-75 (1943).

¹⁷ Securities Exchange Act Release No. 3638 (Jan. 3, 1945), 11 Fed. Reg. 10,995 (1946).

¹⁸ As the Supreme Court emphasized in its 1987 decision in *CTS Corp. v. Dynamics Corp.*, “No principle of corporation law and practice is more firmly established than a State’s authority to regulate domestic corporations, including the authority to define the voting rights of shareholders.” 481 U.S. 69, 89. The section of the Securities Exchange Act upon which Rule 14a-8 is promulgated, § 14(a), is principally designed to ensure corporate disclosures to shareholders to afford investment information and prevent deception. See *J.I. Case Co. v. Borak*, 377 U.S. 426, 431 (1964) (“The purpose of § 14(a) is to prevent management or others from obtaining authorization for corporate action by means of deceptive or inadequate disclosure in proxy solicitation.”). In its 1990 *Business Roundtable* decision, the D.C. Circuit Court of Appeals explained further:

That proxy regulation bears almost exclusively on disclosure stems as a matter of necessity from the nature of proxies. Proxy solicitations are, after all, only communications with potential absentee voters. The goal of federal proxy regulation was to improve those communications and thereby to enable proxy voters to control the corporation as effectively as they might have by attending a shareholder meeting.

Business Roundtable v. SEC, 905 F.2d 406 (D.C. Cir. 1990) (“While the House Report indeed speaks of fair corporate suffrage, it also plainly identifies Congress’s target—the solicitation of proxies by well informed insiders ‘without fairly informing the stockholders of the purposes for which the proxies are to be used.’” (citing H.R.Rep. No. 1383, 73d Cong., 2d Sess. 14 (1934))). See also S.Rep. No. 792, 73d Cong., 2d Sess. 12 (1934) (characterizing purpose of proxy protections as ensuring stockholders’ “adequate knowledge” about the “financial condition of the corporation”).

¹⁹ Exchange Act Release No. 4775, 17 Fed. Reg. 11,431, 11,433 (1952).

That rule would exist until the early 1970s, when a decision by the D.C. Circuit Court of Appeals challenged the application of the rule by the SEC staff, which in April 1969 had issued a no-action letter to Dow Chemical permitting the company to exclude a shareholder proposal from the Medical Committee on Human Rights asking that the company cease manufacturing napalm.²⁰ The circuit court invoked the “philosophy of corporate democracy” in sharply questioning the rule as applied:

No reason has been advanced in the present proceedings which leads to the conclusion that management may properly place obstacles in the path of shareholders who wish to present to their co-owners, in accord with applicable state law, the question of whether they wish to have their assets used in a manner which they believe to be more socially responsible but possibly less profitable than that which is dictated by present company policy. . . . We think that there is a clear and compelling distinction between management’s legitimate need for freedom to apply its expertise in matters of day-to-day business judgment, and management’s patently illegitimate claim of power to treat modern corporations with their vast resources as personal satrapies implementing personal political or moral predilections. It could scarcely be argued that management is more qualified or more entitled to make these kinds of decisions than the shareholders who are the true beneficial owners of the corporation; and it seems equally implausible that an application of the proxy rules which permitted such a result could be harmonized with the philosophy of corporate democracy which Congress embodied in section 14(a) of the Securities Exchange Act of 1934.²¹

Technically, the court did not overturn the SEC’s rule but rather remanded the case to the agency for reconsideration so that “the basis for (its) decision (may) appear clearly on the record, not in conclusory terms but in sufficient detail to permit prompt and effective review.”²² Dow decided to include the proposal on its proxy ballot, and the Supreme Court, on *certiorari*, vacated the lower court decision as moot.²³

Although there certainly would have been a state-law basis for excluding proposals such as that faced by Dow,²⁴ the SEC decided instead in 1972 to narrow its rule.²⁵ Rather than the earlier

²⁰ See *Med. Comm. for Human Rights v. Sec. & Exch. Comm’n*, 432 F.2d 659, 663 (D.C. Cir. 1970), *vacated as moot*, 404 U.S. 403 (1972); see also 17 C.F.R. § 240.14a-8(c) (1970).

²¹ *Med. Comm. for Human Rights*, 432 F.2d at 681.

²² *Id.* at 682.

²³ 404 U.S. 403.

²⁴ See *Guth v. Loft*, 5 A2d 503, 510 (Del. 1939) (“Corporate officers and directors . . . stand in a fiduciary relation to the corporation and its stockholders. A public policy, existing through the years, and derived from a profound knowledge of human characteristics and motives, has established a rule that demands of a corporate officer or director, peremptorily and inexorably, the most scrupulous observance of his duty, not only affirmatively to protect the interests of the corporation committed to his charge, but also to refrain from doing anything that would work injury to the corporation, or to deprive it of profit or advantage which his skill and ability might properly bring to it, or to enable it to make in the reasonable and lawful exercise of its powers.”); see also 8 Del. C. § 141(a) (“The 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.”); cf. *Dodge v. Ford Motor Co.*, 170 N.W. 668, 684 (Mich. 1919) (“A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end.”).

²⁵ See Exchange Act Release No. 9784, 37 Fed. Reg. 23,178, 23,180 (1972).

language intended to permit companies to exclude proposals motivated primarily by social, economic, or policy concerns, the new release merely permitted companies to exclude shareholder proposals “not significantly related to the business of the issuer or not within its control.”²⁶ In 1976, the SEC issued an interpretive release stating that shareholder proposals related to the “ordinary business” of the corporation could only be invoked to exclude proposals that “involve business matters that are mundane in nature and do not involve any substantial policy or other considerations”²⁷—essentially inverting the prior rule.

Today’s Rule 14a-8 is written in a question-and-answer format setting forth the circumstances in which companies may exclude shareholder proposals. Companies wishing to exclude a shareholder proposal from the proxy ballot typically seek a “no action” letter from the SEC staff suggesting that the agency will take no action if the proposal is excluded.²⁸ The SEC issues no-action letters to petitioning companies if the agency’s staff determines that a shareholder proposal does not comply with SEC rules. Procedurally, the shareholder must establish his ownership in the company and meet filing deadlines.²⁹ Substantively, a company would be permitted to exclude a shareholder proposal that was too vague or indefinite to implement, that asked the company to do something that it had already done or lacks the power to implement, that conflicted with state law, that duplicated or conflicted with another ballot proposal, or that involved the company’s ordinary business operations.³⁰ Companies are also permitted to exclude repeat proposals that failed to gain minimal shareholder support in earlier years.³¹

2. *Shareholder Proposal Sponsors*

For each of the last eleven years tracked in the Manhattan Institute’s Proxy Monitor database,³² a small group of shareholders has dominated the process of introducing shareholder proposals:

²⁶ *Id.*

²⁷ See Adoption of Amendments Relating to Proposals by Security Holders, Exchange Act Release No. 12,999, 41 Fed. Reg. 52,994, 52,997–98 (1976).

²⁸ See *No-Action Letters*, SEC, <http://www.sec.gov/answers/noaction.htm>.

²⁹ See 14a-8, *supra* note 9.

³⁰ See *id.*

³¹ See *id.*

³² As discussed in notes 2 and 3 and the accompanying text, the Proxy Monitor database contains all shareholder proposals for the 250 largest publicly traded companies by revenues, as listed by *Fortune* magazine. These companies constitute a substantial majority of the total stock market capitalization held by diversified investors. Notwithstanding this fact, some shareholder activists and their supporters have objected to Proxy Monitor data on the grounds that many companies that receive shareholder proposals are not included in the database. See, e.g., Heidi Welsh, *Accuracy in Proxy Monitoring*, HLS Forum on Corporate Governance and Financial Regulation, Sept. 16, 2013, <https://blogs.law.harvard.edu/corpgov/2013/09/16/accuracy-in-proxy-monitoring-2/>. A broader dataset, however, risks obscuring the impact of shareholder-proposal rules on the average diversified investor, given the broad variance in market capitalization among companies. Even among the large companies comprising the Proxy Monitor dataset, there are significant variations in market capitalization; the five largest companies in the Fortune 250 have a combined market capitalization almost 18 times as large as companies 246 through 250 on Fortune’s list. (The five largest companies by revenues in the 2015 Fortune 500 list—Walmart, Exxon Mobil, Chevron, Berkshire Hathaway, and Apple—had a combined market capitalization of more than \$1.7 trillion on September 1, 2016, which constitutes 7.6% of the U.S. total stock market capitalization, based on the Wilshire 5000 Price Full Cap Index. The companies listed as 246 through 250 on the list—DTE Energy, Ameriprise Financial, VF, Praxair, and J.C. Penney—had a combined market capitalization of \$96 billion, or 0.4% of the U.S. total stock market capitalization. Overall, the S&P 100 alone contains more than 54% of the U.S. total market capitalization.) Thus,

- A.** A very small group of individuals and their family members—often referred to as “**corporate gadflies**”³³—repeatedly file substantially similar proposals across a broad set of companies. Typically, these individuals own very small percentages of a company’s stock. For instance, John Chevedden, the most-active sponsor of shareholder proposals dating back to 2006, has made substantially the same proposal at Ford Motor Company each of those years, individually or through a family trust. In its 2016 proxy statement, Ford disclosed that Mr. Chevedden owned 500 shares of the company’s stock³⁴—an investment valued at \$6,750 at the close of trading on the company’s March 16 record date—approximately 0.00001% of the company’s market capitalization. All told, Mr. Chevedden and four individual gadfly investors and their family members sponsored 29% of all shareholder proposals from 2006–15 (**Figure 1**); six gadfly investors and their family members have sponsored one-third of all shareholder proposals to date in 2016 (**Figure 2**).³⁵
- B.** Institutional investors focusing on “**socially responsible**” investing,³⁶ which expressly concern themselves with social or political issues apart from solely share-price maximization, are very active in sponsoring shareholder proposals. Such investors include special-purpose social-investing funds, as well as policy-oriented foundations and various retirement and investment vehicles associated with religious or public-policy organizations.³⁷ Such investors sponsored 27% of all shareholder proposals across the ten-year period from 2006 through 2015 and 38% of all shareholder proposals to date in 2016. Many of these investors, like corporate gadflies, sponsor shareholder proposals in companies in which they have very small investments. For instance, in 2016, a social

from the average shareholder’s perspective, the Proxy Monitor data set paints a significantly more accurate picture than do the vote tallies of most shareholder activists, who simply straight-line-average votes across a much larger data set of companies, without regard to market capitalization.

³³ See Charles M. Yablon, *Overcompensating: The Corporate Lawyer and Executive Pay*, 92 COLUM. L. REV. 1867, 1895 (1992); Jessica Holzer, *Firms Try New Tack against Gadflies*, WALL ST. J., June 6, 2011, <http://online.wsj.com/article/SB10001424052702304906004576367133865305262.html>.

³⁴ See Ford Motor Co., *Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934*, proposal no. 5 (Apr. 1, 2016).

³⁵ Jonathan Kalodimos, a professor and former SEC staffer, is a new corporate gadfly in 2016. See Jonathan Kalodimos, *A Gadfly’s Perspective on “Gadflies at the Gate,”* Sept. 2, 2016. Kalodimos introduced multiple proposals seeking to encourage companies to pursue share buybacks in lieu of paying cash dividends. Kalodimos’s prior experience with the SEC did not help him to draft a shareholder proposal that garnered widespread shareholder support. Indeed, more than 97% of shareholders voted against each of his proposals, meaning that none will be eligible for resubmission for five years.

³⁶ See Michael Chamberlain, *Socially Responsible Investing: What You Need to Know*, FORBES, Apr. 24, 2013, <http://www.forbes.com/sites/feeonlyplanner/2013/04/24/socially-responsible-investing-what-you-need-to-know> (“In general, socially responsible investors are looking to promote concepts and ideals that they feel strongly about”). The modern push for “corporate social responsibility” generally traces to a pair of 1970s books, *Where the Law Ends*, by Christopher Stone (1975), and *Taming the Giant Corporation*, by Ralph Nader, Mark Green, and Joel Seligman (1976). For a critique of the early concept of corporate social responsibility advocated by these authors, see David L. Engel, *An Approach to Corporate Social Responsibility*, 32 STAN. L. REV. 1, 1 (1979) (“Any mandatory governance reforms intended to spur more corporate altruism are almost sure to have general institutional costs within the corporate system itself. . . . But the proponents of “more” corporate social responsibility have never bothered to analyze or examine, from any clearly defined starting point, even just the benefits they anticipate from reform . . .”).

³⁷ Religious organizations’ pension plans are generally exempt from the fiduciary requirements of the Employee Retirement Income Security Act (ERISA). 29 U.S.C. § 1003(b).

investor known as Holy Land Principles, Inc. sponsored shareholder proposals, relating to employment practices in areas governed by Israel and the Palestinian Authority, on the ballots of seven of the 231 Fortune 250 companies to hold annual meetings by the end of August. In each case, its investment was a miniscule percentage of the company's outstanding market capitalization; in Pepsico, it owned a reported 55 shares,³⁸ worth \$5,932.85 on the company's February 26 record date—approximately 0.000003% of the company's market capitalization.

- C. Apart from investors with a social or policy orientation, the principal institutional investors involved with sponsoring shareholder proposals are **labor-affiliated pension funds**—including “multiemployer” plans affiliated with labor unions such as the American Federation of Labor–Congress of Industrial Organizations (AFL-CIO) or American Federation of State, County, and Municipal Employees (AFSCME), as well as state and municipal pension plans, particularly those representing New York City and State. Overall, labor-affiliated investors sponsored 32% of all shareholder proposals from 2006–15 and 21% to date in 2016.³⁹ Typically, these plans have substantial investment stakes in the companies at which they file shareholder proposals, though the private labor unions have been known to file such proposals from investment vehicles with small holdings. For example, in 2016, the AFL-CIO sponsored a human-rights-related proposal at Mondelez International, but reportedly held only 925 shares,⁴⁰ valued at \$38,803.75 on the March 9 record date, approximately 0.00006% of the company's outstanding market capitalization.⁴¹

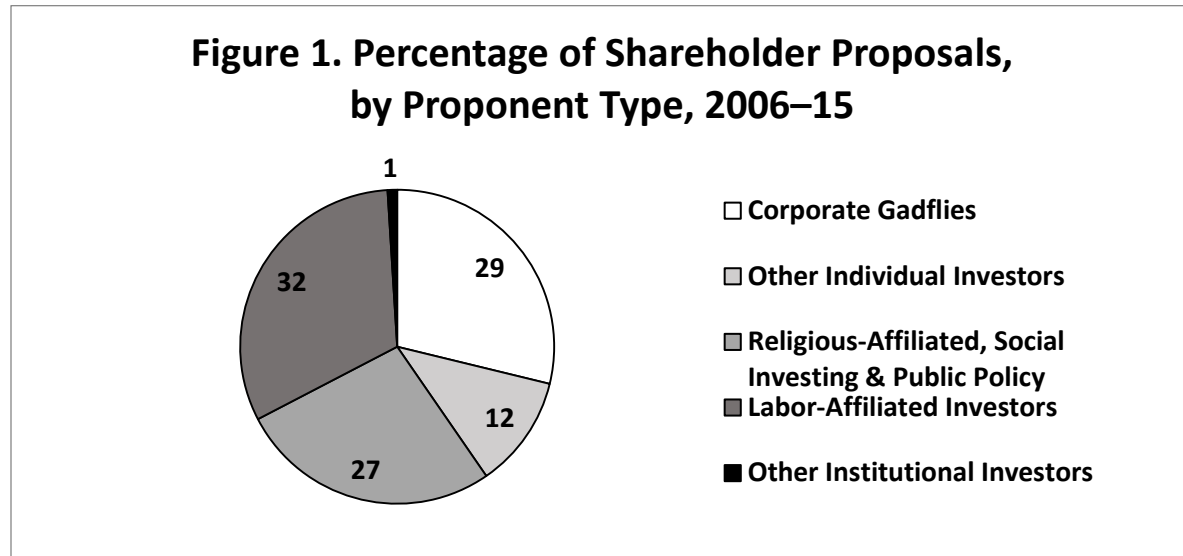
³⁸ See Pepsico, *Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934*, proposal no. 7 (Mar. 18, 2016).

³⁹ The low sponsorship numbers in 2016 are somewhat deceptive, in that the most-active labor-affiliated shareholder proponent over the last eleven years, the New York City pension funds, withdrew a large fraction of its shareholder proposals. Most of the shareholder proposals sponsored by the New York City pension funds in 2015 and 2016 involved “proxy access,” the idea that shareholders should have the right to place their own nominees for director on corporate proxy ballots to compete with boards' own director nominees. These proposals mirrored the SEC's previously released Rule 14a-11, which would have mandated that publicly traded companies list shareholders' nominees for director on their corporate proxy ballots, as long as the nominating shareholder had held at least 3% of a company's stock for a minimum of three years. The SEC promulgated the rule in August 2010, but the D.C. Circuit rejected it as “arbitrary and capricious” in July 2011. See *Business Roundtable v. SEC*, 647 F.3d 1144, 1152 (D.C. Cir. 2011). The SEC did not appeal the decision but instead approved amendments to Rule 14a-8—the rule for shareholder proposals—to allow shareholders to introduce proxy-access rules on their own. See Abigail Caplovitz Field, *Proxy Access Debate Far from Over*, CORPORATESECRETARY.COM., (Sept. 9, 2011), <http://www.corporatesecretary.com/articles/proxy-voting/12000/proxy-access-debate-far-over/>. In 2015, most of the New York City funds' proxy-access proposals received majority shareholder backing, and in 2016, most of the companies in the Fortune 250 that faced a New York City-sponsored shareholder proposal involving proxy access reached an agreement to adopt a form of proxy access rule, prompting the sponsor to withdraw the proposal.

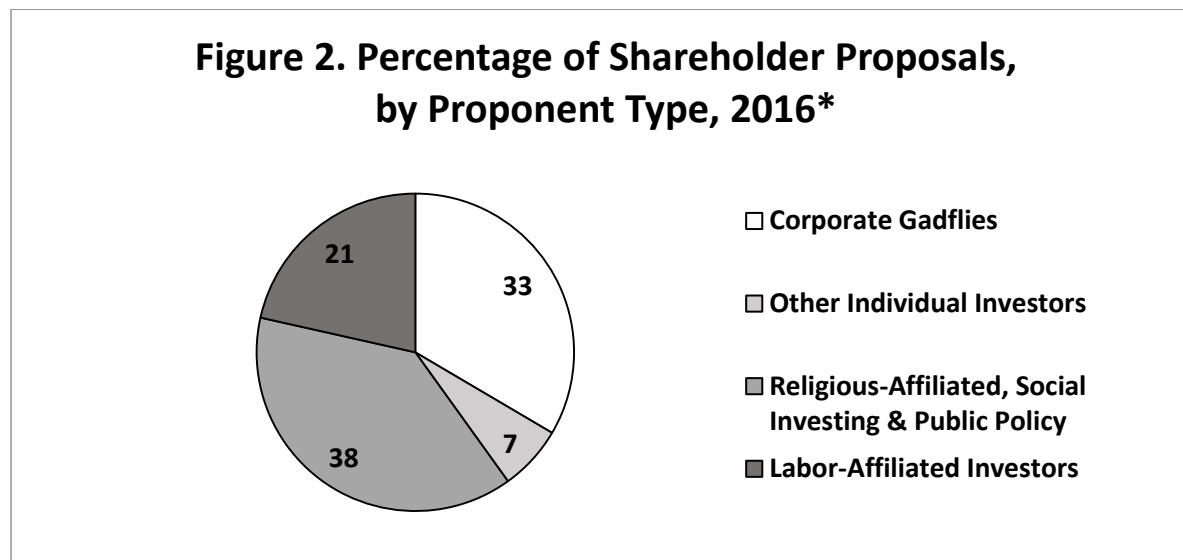
⁴⁰ See Mondelez International, Inc., *Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934*, proposal no. 6 (Mar. 28, 2016).

⁴¹ Labor unions may choose to engage in socially oriented shareholder activism through small-investment vehicles rather than multiemployer private pension plans to avoid fiduciary strictures of ERISA, which govern their investment approaches, unlike state and municipal plans or religious plans. See 29 U.S.C. § 1003(b). This approach may or may not shift going forward, given the Department of Labor's Interpretive Bulletin 2015-01, an October 2015 rule broadening the fiduciary scope for private pension plans' investments in “economically targeted investments.” See *Interpretive Bulletin Relating to the Fiduciary Standard Under ERISA in Considering Economically Targeted Investments*, <https://www.federalregister.gov/articles/2015/10/26/2015-27146/interpretiv.e-bulletin-relating-to-the-fiduciary-standard-under-erisa-in-considering-economically>.

Only 1% of shareholder proposals introduced in the decade between 2006 and 2015 involved institutional investors without a labor affiliation or social, religious, or policy focus. No institutional investor without such an affiliation or focus has sponsored a shareholder proposal in 2016.



Source: ProxyMonitor.org



*Based on 231 companies holding annual meetings by August 31

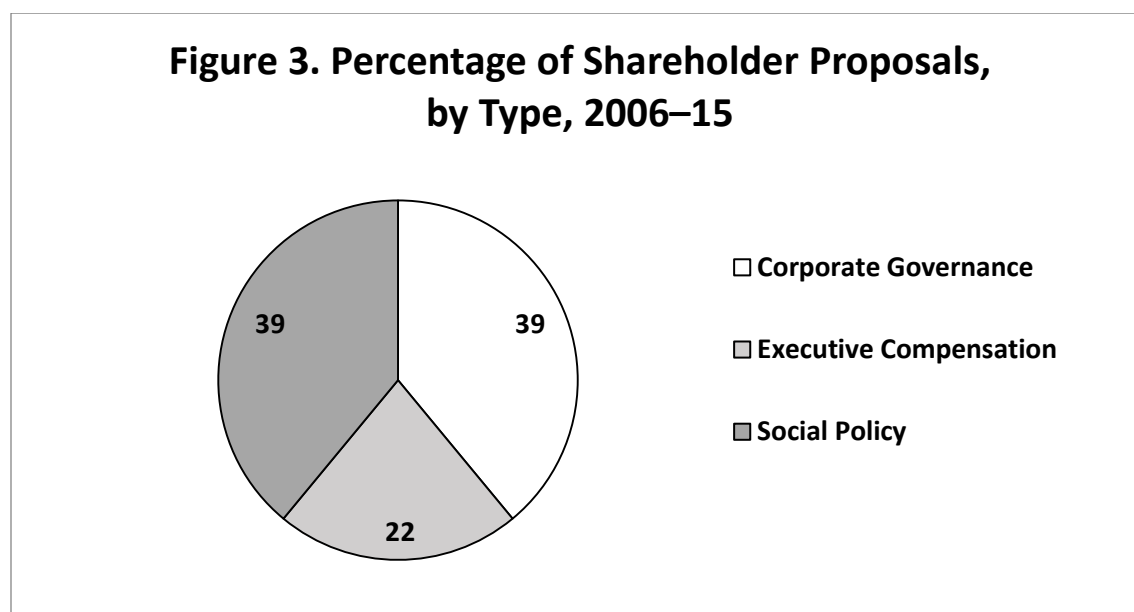
Source: ProxyMonitor.org

3. Shareholder Proposal Subjects

Shareholder proposals tend to be broadly divided among:

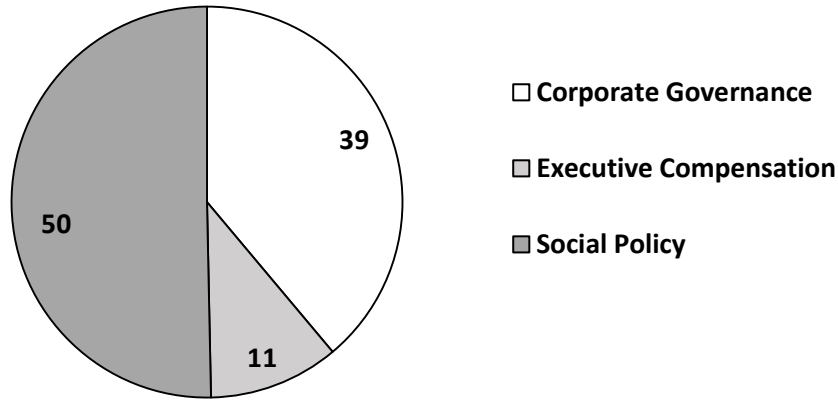
- A. Proposals that seek to modify the process by which the companies allocate powers between the board and shareholders (“**corporate governance**” proposals);
- B. Proposals that seek to influence corporate management by altering **executive compensation**, purportedly to better align management’s incentives with shareholders’ interests; and
- C. Proposals that seek to reorient a company’s approach to align with a **social or policy** goal that may not be related—or at least has an attenuated relationship—to share value.

Over the ten-year period from 2006 through 2015, most shareholder proposals related to corporate governance or to social/policy concerns—39% apiece, with 22% of shareholder proposals relating to executive compensation (**Figure 3**). In 2016, to date, **half** of shareholder proposals have related to a social or policy issue (**Figure 4**). The most commonly introduced proposals, in each year from 2014 through 2016, have been those involving environmental issues or the company’s political spending or lobbying (**Figure 5**).



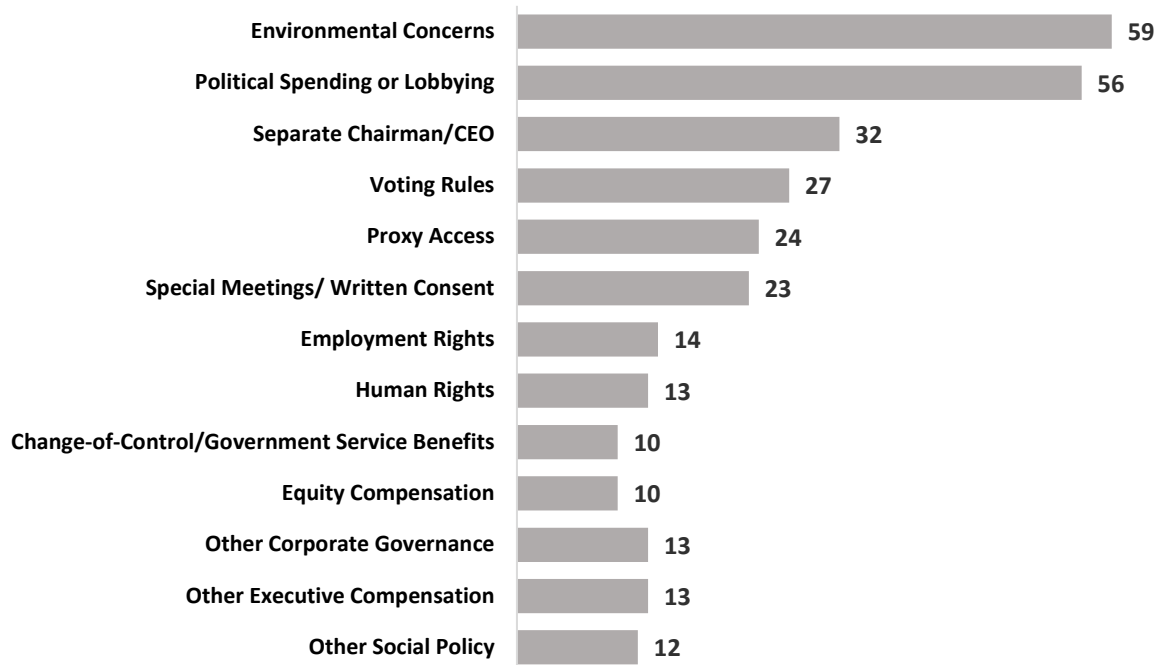
Source: ProxyMonitor.org

Figure 4. Percentage of Shareholder Proposals, by Type, 2016*



*Based on 231 companies holding annual meetings by August 31
 Source: ProxyMonitor.org

Figure 5. Shareholder Proposals, 2016*



*Based on 231 companies holding annual meetings by August 31
 Source: ProxyMonitor.org

4. *Shareholder Proposal Voting*

Shareholder proposals are commonly introduced at large publicly traded companies, but they very rarely garner majority shareholder support (**Figure 6**).⁴² Proposals that have been relatively likely to pass have involved altering rules on director elections—by requiring that shareholders be permitted to vote on all directors annually, rather than in “staggered” board terms (like the U.S. Senate); by requiring that companies refuse to seat directors who receive less than majority shareholder support in an uncontested election; or, most recently, by granting shareholders above a certain ownership threshold and holding period “proxy access” to place some of their own director nominees on the company ballot.

In contrast to some shareholder-proposal activism related to corporate governance, shareholder proposals related to social or policy concerns have consistently failed to garner broad shareholder support. Among the companies in the Fortune 250, not a single shareholder proposal involving social or policy concerns won majority shareholder support over board opposition over

⁴² In determining shareholder support for shareholder proposals, the Manhattan Institute counts votes consistent with the practice dictated in a company’s bylaws, consistent with state law. Some companies measure shareholder support by dividing the number of votes for a proposal by the total number of shares present and voting, ignoring abstentions. Other companies measure shareholder support by dividing the number of favorable votes by the number of shares present and entitled to vote—thus including abstentions in the denominator of the tally. Neither practice necessarily skews shareholder votes in management’s favor: whereas the latter method makes it relatively more difficult for shareholder resolutions to obtain majority support, it also makes it more difficult for management to win shareholder backing for its own proposals, such as equity-compensation plans.

Although shareholder-proposal activists prefer to exclude abstentions consistently in tabulating vote totals, without regard to corporate bylaws—which necessarily inflates apparent support for their proposals—such a methodology is inconsistent with federal law. The SEC’s Schedule 14A specifies that for “each matter which is to be submitted to a vote of security holders,” corporate proxy statements must “[d]isclose the method by which votes will be counted, including the treatment and effect of abstentions and broker non-votes under applicable state law as well as registrant charter and bylaw provisions”—clearly indicating that corporations can adopt varying counting methodologies in assessing shareholder votes and that state substantive law governs the parameters of vote calculation. Schedule 14A, Item 21. Voting Procedures, <http://taft.law.uc.edu/CCL/34ActRIs/rule14a-101.html> (last visited August 16, 2013).

Under the state law of Delaware, in which most large public corporations are chartered, “the certificate of incorporation or bylaws of any corporation authorized to issue stock may specify the number of shares and/or the amount of other securities having voting power the holders of which shall be present or represented by proxy at any meeting in order to constitute a quorum for, and the votes that shall be necessary for, the transaction of any business.” Del. Gen. Corp. L. § 216. As a default rule, absent a bylaw specification, Delaware law specifies that “in all matters other than the election of directors,” companies should count “the affirmative vote of the majority of shares of such class or series or classes or series present in person or represented by proxy at the meeting,” *id.* at 216(4)—the precise inverse of shareholder-proposal activists’ preferred counting rule.

The SEC staff has adopted a rule that for the very limited purpose of determining whether a proposal has met the “resubmission threshold” to qualify for inclusion on the next year’s corporate ballot—a permissive standard requiring merely a minimum 3%, 6%, or 10% vote, respectively, in successive years, *see* Amendments to Rules on Shareholder Proposals, Exchange Act Release No. 40,018; 63 Fed. Reg. 29,106, 29,108 (May 28, 1998) (codified at 17 C.F.R. pt. 240)—“[o]nly votes for and against a proposal are included in the calculation of the shareholder vote of that proposal,” ignoring abstentions. SEC Staff Legal Bulletin No. 14, F.4., July 13, 2001, <http://www.sec.gov/interps/legal/cfslb14.htm> (last visited August 16, 2013). Because this is a staff rule not voted on by the Commission; because it exists for a limited purpose (with multiple rationales, including reducing workload in processing 14a-8 no-action petitions and adopting a permissive standard for ballot inclusion); and because it contravenes clear and longstanding deference to substantive state law in the field of corporate governance, the notion that this limited SEC staff vote-counting rule should dictate counting methodology, irrespective of state law and governing corporate bylaws, is untenable.

the entire 2006–15 period. In 2016, one of 155 shareholder proposals with a social or policy purpose won majority (52%) shareholder backing: a politics-related proposal at Fluor Corporation that sought disclosure of “[p]olicies and procedures for making, with corporate funds or assets, contributions and expenditures (direct or indirect) to (a) participate or intervene in any political campaign on behalf of (or in opposition to) any candidate for public office, or (b) influence the general public, or any segment thereof, with respect to an election or referendum,” as well as disclosure of amounts given to each identified recipient and the corporate officer responsible for decision-making.⁴³ The Fluor proposal is certainly anomalous:⁴⁴ among 446 shareholder proposals related to corporate political spending or lobbying in the Proxy Monitor database, it is the only shareholder proposal, opposed by management, to receive majority shareholder support;⁴⁵ and it is the only shareholder proposal of 1,444 related to social policy concerns to receive majority shareholder support at any Fortune 250 company from 2006–16.⁴⁶

⁴³ Fluor Corp., Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934, proposal no. 4 (Mar. 10, 2016).

⁴⁴ As a major construction company, Fluor is heavily involved in government-contracting work, which may make shareholders particularly sensitive to its political engagement. Moreover, the company’s market capitalization fell more than 43% from the record date for its 2014 annual meeting and its 2016 annual meeting, when it missed its earning target. A proposal by the New York State Common Retirement Fund on greenhouse gas emissions also received more than 40% support at Fluor, suggesting broader shareholder dissatisfaction with the company in 2016 or an idiosyncratic shareholder base.

⁴⁵ In 2006, a shareholder proposal at Amgen related to political-spending disclosure received 67 percent shareholder support, with the board of the company supporting the proposal.

⁴⁶ Note that this statement holds true for the current Fortune 250, but a shareholder proposal at KBR, Inc. did receive 55% shareholder support over board opposition in 2011, when the company was in the Fortune 250 list. (KBR is currently ranked number 501.) That proposal, sponsored by the New York City pension funds, encouraged the board to amend the company’s equal-employment opportunity policy to prohibit discrimination based on sexual orientation. Also, in addition to the political-spending-related proposal at Amgen, four other shareholder proposals received majority shareholder support with the board of directors backing the proposal, including one in 2016—an animal-rights-related proposal introduced at Kellogg that applauded the company for switching to eggs produced by cage-free chickens.

Figure 6. Shareholder Support by Proposal Class, 2016*

Proposal Class	Proposals Introduced	Proposals Defeated	Proposals Winning Majority Support
Corporate Governance	119	100	19
Separate Chairman and CEO	32	32	0
Proxy Access	24	11	13
Shareholder Action by Written Consent	12	12	0
Shareholder Power to Call Special Meetings	11	10	1
Eliminate Supermajority Provisions in Bylaws**	8	5	3
Change Vote-Counting Standard	8	8	0
Change Stock Classes or Voting Rights	6	6	0
Majority Voting for Directors	4	2	2
Other	14	14	0
Executive Compensation	33	33	0
Change-of-Control/Government Service Benefits	10	10	0
Equity Compensation Rules	10	10	0
Other	13	13	0
Social Policy	155	153	2
Environmental Issues	59	59	0
Political Spending or Lobbying	56	55	1
Employment Rights	14	14	0
Human Rights	13	13	0
Other***	13	12	1

*Based on 231 companies holding annual meetings by August 31

**A fourth shareholder received majority support but failed because it was presented as an amendment to the company's certificate of incorporation, requiring unanimous support.

***The shareholder proposal winning majority support was supported by board of directors.

Source: ProxyMonitor.org

5. *The Role of Proxy Advisory Firms*

Prior to the 1980s, institutional investors had generally paid little attention to shareholder voting matters, but the wave of hostile takeover actions in that decade forced institutional investors to take at least occasional notice. Some institutional investors' broader need to assess shareholder voting issues, including proxy proposals, took on added significance in the late 1980s when the U.S. Department of Labor required retirement benefit funds governed by the Employee Retirement Income Security Act (ERISA) to vote their shares according to a "prudent man" standard.⁴⁷ In 2003, the SEC clarified that similar fiduciary duties attach to mutual funds and other registered investment companies.⁴⁸ These requirements place significant burdens on institutional investors: according to a 2010 report by the Investment Company Institute, Russell 3000 companies faced more than 20,000 proxy ballot items annually⁴⁹—even before Dodd-Frank-required executive compensation voting.⁵⁰

Concurrent with these trends, institutional investors have managed an increasing percentage of U.S. equity market holdings: from 1997 through 2009, the equity percentage of the 1,000 largest U.S. publicly traded companies by assets held by institutional investors increased from 60% to 73%.⁵¹ In 2009, the SEC approved amendments to the New York Stock Exchange rules that eliminated stockbrokers' ability to vote discretionarily the shares of their individual investors for director elections;⁵² and in 2012, the NYSE applied the limitation to a broader array of issues.⁵³ In essence, this combination of trends has substantially increased the relative power of institutional investors in proxy voting matters, even as such matters have multiplied in complexity.

To manage their proxy voting, institutional investors rely heavily on a pair of proxy advisory firms, Institutional Shareholder Services, or ISS, which is today owned by private-equity firm Vestal Capital Partners;⁵⁴ and Glass, Lewis & Co., a subsidiary of the Ontario Teachers' Pension

⁴⁷ See Letter from U.S. Dep't of Labor to Helmut Fandl, Chairman of Retirement Board, Avon Products, Inc. (Feb. 23, 1988); see also 73 Fed. Reg. 61731 (Oct. 17, 2008).

⁴⁸ See 68 Fed. Reg. 6585 (Feb. 7, 2003) ("The duty of care requires an adviser with proxy voting authority to monitor corporate events and to vote the proxies. To satisfy its duty of loyalty, the adviser must cast the proxy votes in a manner consistent with the best interest of its client and must not subrogate client interests to its own." (internal citations omitted)).

⁴⁹ See Investment Company Institute, Trends in Proxy Voting by Registered Investment Companies, 2007–09, 16 Research Perspective 4 (Nov. 2010), <http://www.ici.org/pdf/per16-01.pdf>.

⁵⁰ Under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, publicly traded companies must hold shareholder advisory votes on executive compensation annually, biennially, or triennially, at shareholders' discretion. See Pub. L. No. 111-203, 124 Stat. 1376, § 951 (2010).

⁵¹ See Matteo Tonello & Stephan R. Rabimov, The 2010 Institutional Investment Report: Trends in Asset Allocation and Portfolio Composition, The Conference Board Research Report, No. R-1468-10-RR, 27, 2010, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1707512.

⁵² See SEC Rel. No. 34-60215, <http://www.sec.gov/rules/sro/nyse/2009/34-60215.pdf>.

⁵³ See NYSE, Information Memo No. 12-4, Application of Rule 452 to Certain Types of Corporate Governance Proposals (Jan. 25, 2012), available at http://www.nyse.com/nyse/nyse/nyse/rulechanges/pdf?memo_id=12-4.

⁵⁴ See Press Release, Vestal Capital Partners Completes Acquisition of Institutional Shareholder Services, <http://www.issgovernance.com/vestar-capital-partners-completes-acquisition-of-institutional-shareholder-services> (last visited Sept. 3, 2014).

Plan Board.⁵⁵ Together, these two proxy advisors control approximately 97% of the market for proxy advisory services, with ISS alone having about a 61% share.⁵⁶ By its own estimation, ISS helps more than 1,600 clients execute nearly 8.5 million ballots representing more than 2 trillion shares.⁵⁷

These proxy advisory firms' power over shareholder voting is vast. A 2012 analysis I lead authored for the Manhattan Institute found that an ISS recommendation "for" a given shareholder proposal—controlling for other factors including company size, industry, proponent type, proposal type, and year—was associated with a 15-percentage-point increase in the shareholder vote for any given proposal.⁵⁸ Thus, in the shareholder-proposal context, ISS acts like a 15% owner of the largest publicly traded companies in terms of its influence over the voting market. As Leo Strine, a former chancellor on the Delaware Court of Chancery, observed: "Powerful CEOs come on bended knee to Rockville, Maryland, where ISS resides, to persuade the managers of ISS of the merits of their views about issues."⁵⁹

Notwithstanding its influence, ISS is a relatively small operation. Prior to its 2014 acquisition by Vestal, ISS was owned by MSCI, a publicly traded company; at that time, the world's largest proxy advisor had fewer than 700 employees and just over \$15 million in profits on \$122 million in revenues.⁶⁰ A significant fraction of those revenues came not from sales to the institutional-investment community itself but rather from the company's "Corporate Sales" division, which offers governance and proxy advice to corporations—in essence, the very companies on whose proxies ISS advises institutional investors on how to vote. In 2013, ISS's Corporate Sales group generated 29% of its revenues, up from 21% two years earlier.⁶¹

The probable reason for the disconnect between ISS's cash flows and influence is that institutional investors simply do not place a very large economic value on the services it offers. In almost all situations, there is little competitive advantage to be gained from being a "better voter" on proxy items, at least those proposed by shareholders through the 14a-8 process.⁶²

⁵⁵ See Robyn Bew & Richard Fields, *Voting Decisions at US Mutual Funds: How Investors Really Use Proxy Advisers 6* (Tapestry Networks, Inc. & Investment Research Center Institute, June 2012), <http://www.tapestrynetworks.com/issues/corporate-governance/upload/Voting-Decisions-at-US-Mutual-Funds-June-2012.pdf>.

⁵⁶ See James K. Glassman and J. W. Verret, *How to Fix Our Broken Proxy Advisory System 8* (Mercatus Center, George Mason Univ., 2013), *available at* http://mercatus.org/sites/default/files/Glassman_ProxyAdvisorySystem_04152013.pdf.

⁵⁷ Institutional Shareholder Services, *About ISS*, <http://www.issgovernance.com/about/about-iss>.

⁵⁸ James R. Copland et al., *Proxy Monitor 2012: A Report on Corporate Governance and Shareholder Activism 22–23* (Manhattan Inst. for Pol'y Res., Fall 2012), *available at* http://www.proxymonitor.org/Forms/pmr_04.aspx.

⁵⁹ Leo E. Strine, Jr., *The Delaware Way: How We Do Corporate Law and Some of the New Challenges We (and Europe) Face*, 30 DEL. J. CORP. L. 688 (2005).

⁶⁰ See MSCI 2013 Annual Report 70, "Summary of Operations," "Governance," *available at* http://files.shareholder.com/downloads/MSCI/3458217323x0x739303/DAB046E7-737E-43C7-9114-040465AD560E/2013_Annual_Report.pdf

⁶¹ *Compare id.* at 10 with MSCI 2011 Annual Report 9, *available at* http://files.shareholder.com/downloads/MSCI/2008427917x0x554571/96AD1F8D-CC19-4BFD-9E47-6EFD2079886C/264713_007_MSCI_BMK_AR.pdf.

⁶² Cf. BRYAN CAPLAN, *THE MYTH OF THE RATIONAL VOTER* (2007). Institutional investors compete aggressively for investor dollars, and they gain competitive advantages largely through higher returns and lower fees. Investing in proxy-voting information raises institutional investors' costs while giving no competitive advantage in increasing

Large institutional investors, like Fidelity or Vanguard, with sufficient resources to make their own proxy voting decisions and not lose appreciable cost advantage to competitors surely find ISS's analytical tools useful but rely little on their proxy voting guidelines; smaller funds wanting to minimize their investment in voting find hiring ISS a useful way to discharge fiduciary voting obligations at low cost. But the very fact that the cost is low—less than \$80 million in annual revenues⁶³ in the context of \$26 trillion in assets—shows that ISS's services are not that highly valued by institutional investors, which also helps explain the lack of significant competitors and dearth of new entrants into the proxy advisory space.

Such forces enable ISS (and Glass Lewis) to support ballot items that are generally rejected by most investors, without fear of reprisal. My research shows that ISS has, historically, been almost eight times as likely as the median shareholder to support a shareholder proposal.⁶⁴ ISS's current policy guidelines continue to reflect this disconnect. Among the class of most-introduced shareholder proposals involving corporate governance issues that ISS is “generally for,”⁶⁵ shareholder reaction varies significantly:

- Proposals to declassify boards of directors, to grant shareholders proxy access to nominate directors under the terms of the prior SEC rule, or to eliminate supermajority voting provisions are more likely than not to pass;
- Proposals calling for majority votes to elect directors, or for shareholder power to call special meetings, or act through written consent, gain occasional support; and
- Proposals calling for separating the company's chairman and CEO roles, or enabling cumulative voting for director nominees, almost always fail.

Beyond corporate-governance proposals, the disconnect between ISS and the median shareholder is even starker. My research reveals that ISS supported shareholder proposals related to a company's equity compensation plan 75% of the time;⁶⁶ but only two of 275 such proposals introduced at Fortune 250 companies from 2006 through 2016 have received the support of a majority of shareholders. Among shareholder proposals involving social or policy concerns, as previously discussed, only one proposal of 1,444 coming to a vote at a Fortune 250 company over the last 11 years has received support from a majority of shareholders, over board opposition. In contrast, ISS is “generally for” certain classes of animal rights, employment rights, human rights, environmental, and political-spending-related shareholder proposals; against others; and decides others on a “case by case” basis.⁶⁷ Historically, ISS has backed some 70% of shareholder proposals related to political spending, 45% of those related to employment rights,

investment returns, at least for smaller, diversified investors who have low ownership shares—and whose individual votes on proxy ballot items are therefore unlikely to be dispositive. For a fuller discussion of these dynamics, see James K. Glassman & Hester Peirce, *How Proxy Advisory Services Became So Powerful* (Mercatus Ctr., June 18, 2014), <http://mercatus.org/publication/how-proxy-advisory-services-became-so-powerful>.

⁶³ At least as of 2013, just over \$79 million of ISS's revenues come from its advisory services business, as opposed to corporate contracts. See MSCI 2013, *supra* note 61, at 9–10.

⁶⁴ See Copland et al., *supra* note 58, at 23.

⁶⁵ See generally ISS, *United States Summary Proxy Voting Guidelines: 2016 Benchmark Policy Recommendations 19–29* (Dec. 18, 2015), <https://www.issgovernance.com/file/policy/2016-us-summary-voting-guidelines-dec-2015.pdf>.

⁶⁶ See Copland et al., *supra* note 58, at 23.

⁶⁷ See ISS, *supra* note 65, at 57–66.

and 35% of those related to human rights or the environment⁶⁸—a sharp contrast to the dearth of average shareholder support for these proposal classes.

Although the gap between ISS recommendations and the median shareholder could be explained by simple disagreement, it is worth noting that an increase in shareholder voting support for various proposals also increases the incentive for public companies to enter into consulting contracts with ISS to mitigate such costs. In addition, the absence of market constraints on ISS means that it may be subject to capture by some of its clients who do place more emphasis on shareholder ballot items than do other institutional investors and most individual investors—namely, labor pension funds and social-investing funds, each of which are very active in sponsoring proposals. Even if ISS support is generally unlikely to tip the balance of shareholder support in favor of a given proposal—and the evidence suggests that it is not, at least for social and policy proposals—the 15-percentage-point bump that an ISS “for” recommendation tends to generate will ensure that with ISS support, shareholder-proposal activists’ preferred issues remain on the proxy ballot as long as their proponents wish them to remain there, under current SEC resubmission standards.

6. Shareholder Proposal Resubmissions

The SEC’s current rules stipulate that companies cannot exclude identical shareholder proposals filed year after year, even if vast majorities of shareholders vote against them repeatedly. Under the SEC’s permissive standard, over a five-year period, companies can only exclude a shareholder proposal if it received less than 3% shareholder support in a preceding year, 6% if introduced for a second year, or 10% if introduced at least three times previously.⁶⁹ Given the empirical evidence that a recommendation by the proxy-advisory firm ISS that shareholders vote “for” a given shareholder proposal is associated with a 15-percentage-point boost in the proposal’s shareholder vote, all else being equal, the current SEC rule means that ISS (and probably Glass Lewis, its principal competitor) effectively serves as the gatekeeper for shareholder-proposal resubmissions: if ISS supports a proposal, it can remain indefinitely on the ballot.

The ability of shareholders to continue to place items up for a vote without winning sizable shareholder support matters. Submission of shareholder proposals is not cost-free to the company and to other shareholders; a 1998 analysis by the SEC determined that it cost the average company \$37,000 to decide whether to place a shareholder proposal on the ballot and another \$50,000 in costs to print, distribute, and tabulate the proposal;⁷⁰ aside from printing and distributing, such costs have doubtless risen over time. At least one individual shareholder, former corporate gadfly Evelyn Davis, displayed a profound ability to manipulate the shareholder-proposal process to extract corporate rents:

⁶⁸ See Copland et al., *supra* note 58, at 22–23.

⁶⁹ See Amendments to Rules on Shareholder Proposals, Exchange Act Release No. 40,018; 63 Fed. Reg. 29,106, 29,108 (May 28, 1998) (codified at 17 C.F.R. pt. 240).

⁷⁰ See Amendments to Rules on Shareholder Proposals, 17 C.F.R. 240 (1998) (Release No. 34-40,018) (describing 80 firms reporting on proposal inclusion determination costs and 67 reporting on printing and other direct costs).

Davis . . . publishe[d] a yearly investor newsletter, *Highlights and Lowlights*, which earn[ed] her an estimated \$600,000 annual income. According to one media account, Davis [sold] the \$495, 20-page newsletter in part by “cajol[ing] the nation’s business titans into subscribing . . . with a minimum order of two copies.” Company executives also regularly shower[ed] largesse on Davis to stay in her good graces. According to one report in the 1990s, executives of all three major American car companies offered to deliver any car she purchased to her. Lee Iacocca reportedly said that he would do so in person.⁷¹

Among the 153 shareholder proposals that Davis submitted to the companies in the Proxy Monitor database since 2006, only one received majority shareholder support: a 2006 proposal at Bank of New York Mellon seeking cumulative voting (allowing shareholders to aggregate their ballots for directors into a single candidate), which received 51% of the shareholder vote. (The bank decided not to act on the narrow vote, and Davis continued to submit the proposal each year through 2012, when she “retired” from shareholder activism. The proposal never again received more than 38% shareholder support.)

Though Davis is an extreme case of a single shareholder being able to profit from other shareholders through the shareholder-proposal process, other shareholder activists obviously find merit in continuing to place items on company ballots that do not garner shareholder majorities, year after year. Indeed, the social-investing funds and religious orders that regularly place losing proposals on proxy ballots are predicated upon just this idea. At a minimum, such efforts use the proxy process to gain attention to their cause. In other cases, these social-issue activists may be able to prompt changes in corporate behavior along their desired lines, even when shareholders vote down their proposals—much as Davis’s efforts encouraged companies to spend money out of corporate coffers to placate her.

One approach that the SEC could take to discourage the continued submission of shareholder proposals unrelated to share value is to revise its 1976 rule limiting companies’ ability to exclude from proxy ballots only those “ordinary business” issues “that are mundane in nature and do not involve any substantial policy or other considerations.”⁷² I have argued that the SEC should consider just this approach.⁷³

Another idea, suggested by Yale Law professor Roberta Romano, would be to force shareholders who place on corporate proxy ballots proposals that fail to receive majority shareholder support to reimburse the company at least some portion of the direct costs of assessing, printing, distributing, and tabulating their unsuccessful proposals.⁷⁴ Such a rule would make it cost-prohibitive for corporate gadflies such as Davis to utilize the shareholder-proposal process to extract corporate rents and would force social-issue activists to internalize the costs of their efforts rather than have them subsidized by other shareholders.

⁷¹ Copland et al., *supra* note 58, at 9 (citations omitted).

⁷² Adoption of Amendments Relating to Proposals by Security Holders, *supra* note 27.

⁷³ See Copland (2015), *supra* note 5.

⁷⁴ See Romano, *supra* note 11, at 229–49.

A third idea, suggested by the U.S. Chamber of Commerce and other business groups in a 2014 rulemaking with the SEC,⁷⁵ would be for the SEC to revise its rule permitting companies to exclude resubmitted shareholder proposals if they fail to garner minimum threshold shareholder support within the preceding five calendar years.⁷⁶ The remainder of this section examines empirical evidence shedding light on the impact of the SEC's resubmission rule and the Chamber's pending rulemaking petition.

Empirical Overview

Overall, of the 3,392 shareholder proposals introduced on the proxy ballots of companies in the Proxy Monitor database between 2007 and 2016 (through August 31, 2016), 1,063—31% of all shareholder proposals—were resubmissions of a preceding year's proposal. Of shareholder proposals introduced between 2006 and 2013, 100 were resubmitted three or more times. A plurality of shareholder proposals resubmitted (39%) involved social or policy concerns, and 36% of shareholder proposals resubmitted three or more times were social- or policy-related (slightly below the 41% that involved corporate-governance issues).

ExxonMobil was, by a significant margin, on the receiving end of the greatest number of resubmissions, with 26 different proposals being resubmitted and two proposals submitted nine times over the 11-year span from 2006 through 2015 (**Figure 7**). Both of Exxon's nine-time proposals involved social or policy concerns. One of these, sponsored by the Catholic order the Sisters of St. Dominic, has called on the company to set and disclose greenhouse gas emission goals. That ballot item appeared on ExxonMobil's ballot every year from 2007 through 2015, and at least 69% of shareholders voted against the proposal each time; presumably, the proposal was not on the ballot in 2016 only because in 2015 it fell below the SEC's meager 10% threshold for a third-time submission.

The other nine-time ballot item for ExxonMobil was sponsored by the New York City or State pension funds each year from 2006 through 2014; it called on the oil company to formally amend its equal-employment-opportunity (EEO) policy to include sexual orientation and gender identity. (The company repeatedly maintained in its own proxy statements that it did not discriminate on those grounds and that it included sexual-orientation harassment as an example in its training manuals.) The proposal never received more than 40% shareholder support; but the company changed its EEO policy in 2015, following an Obama administration executive order requiring companies to include sexual orientation and gender identity in formal equal-employment-opportunity policies to receive federal government contracts.⁷⁷

Exxon does not, however, hold the record for the most resubmitted proposals over the last decade: Ford Motor Company and Wells Fargo faced the same corporate governance-related shareholder proposal each year from 2006 through 2016. Each year, 62% or more shareholders voted against the proposals. As previously noted, the sponsor of the Ford proposal, corporate gadfly John Chevedden, owns approximately 0.00001% of the company's outstanding shares.

⁷⁵ See Thomas Quaadman, *supra* note 13.

⁷⁶ See 14a-8, *supra* note 9, at 14a-8(i)(12).

⁷⁷ See Chris Johnson, *Exxon Mobil Adopts LGBT-Inclusive Non-Discrimination Policy*, WASHINGTON BLADE, Jan. 30, 2015.

The value of Chevedden’s holdings, \$6,750 as of the 2016 annual-meeting record date, is substantially less than both the average and the median company cost to print, distribute, and tabulate a shareholder proposal, and substantially less than the average and median company cost to determine whether to include a proposal on the ballot.⁷⁸

Figure 7. Frequently Resubmitted Shareholder Proposals, 2006–16*

Company	Proposal	Total Number	First Year	Last Year	Min. Vote %	Max. Vote %
Ford Motor	One Share – One Vote	11	2006	2016	19	37
Wells Fargo	Separate Chairman & CEO	11	2006	2016	16	38
AT&T	Political Spending	10	2006	2016	13	39
General Electric	Cumulative Voting	10	2006	2016	11	35
Home Depot	Employment Diversity Report	10	2006	2016	22	36
Exxon Mobil	Amend EEO Policy	9	2006	2014	20	40
Exxon Mobil	Greenhouse Gas Emission Goals	9	2007	2015	10	31
Ford Motor	Special Meetings	9	2007	2016	10	26
Nucor	Majority Voting for Directors	9	2006	2014	34	46

*In 2016, based on 231 companies holding annual meetings by August 31

Source: ProxyMonitor.org

AT&T faced an identical social-policy shareholder proposal in 10 of the last 11 years: a political-spending disclosure proposal sponsored by the social-investing fund Domini Social Investments. In 2006 and 2007, the proposal received only 15% and 13% of the vote, respectively. It was nevertheless placed again on the ballot in 2008, when it received almost 32% shareholder support—a 19-percentage-point increase from 2007 and 17 percentage points more than in 2006—after the proxy-advisory firm ISS changed its position and began recommending a vote “for” the proposal.⁷⁹ The proposal has since remained on the ballot every year except 2010; shareholder support has varied between 24% and 39%.

Home Depot also faced an identical social-policy proposal in 10 of the last 11 years: a proposal asking the company to prepare a “report on employment diversity,” sponsored alternatively by the social-investing funds Trillium Asset Management and Walden Asset Management and the Benedictine orders the Sisters of Mt. Angel and the Sisters of Boerne. (For some reason, the proposal did not appear on the company’s 2015 proxy ballot.) In each year, 64%–77% of shareholders voted against the proposal. ISS supports these ballot initiatives.⁸⁰

⁷⁸ See Romano, *supra* note 11, at 241 (“In a 1998 release regarding proposed reforms of the proxy proposal rule, the SEC indicated that respondents to a 1997 agency-administered questionnaire reported an average (median) expenditure of approximately \$50,000 (\$10,000) on printing, distribution and tabulation costs for including a shareholder proposal, and \$37,000 (\$10,000) on the determination whether to include a proposal.”).

⁷⁹ See Domini Social Investments, *Key Proxy Advisor Recommends Vote Against AT&T Management on Political Contributions Disclosure*, Apr. 21, 2008.

⁸⁰ See ISS, *supra* note 65, at 61.

Nucor, a Charlotte-based steel company, faced an identical corporate-governance proposal from the pension fund for the United Brotherhood of Carpenters each year from 2006 through 2014. The proposal sought a bylaw change such that director nominees who failed to garner majority shareholder support in uncontested directors elections would not be seated on the board. The proposal received the backing of 33%–47% of shareholders each year, and 41% in the last year it was introduced (2014). Notwithstanding that a majority of shareholders had voted against the shareholder proposal for nine consecutive years, the company ultimately decided to adopt the majority voting rule; in its 2016 proxy statement, Nucor sought an amendment to its certificate of incorporation adopting a majority voting rule for seating directors—concurrent with a repeal of its previously existing cumulative voting rule;⁸¹ this board proposal passed overwhelmingly.

Analysis of Hypothetical Changes to the Rule

Were the SEC to adopt a modest reform that significantly raised resubmission thresholds, it would block low-support shareholder proposals from being submitted repeatedly on the ballot without blocking shareholders' ability to continue proposing ideas that garnered at least some shareholder support from appearing essentially every year. For example, were the SEC to make its baseline threshold for shareholder support 10% rather than 3%, 149 of the 608 shareholder proposals to be resubmitted at least once would not have been eligible for resubmission over a five-year window.

Consider the case of animal rights–related shareholder proposals, which the proxy-advisory firms generally oppose. From 2006 through 2016, 67 animal rights–related proposals appeared on company proxy ballots. Two of these were “laudatory” or “complimentary” resolutions praising a company action that the board approved, and which won broad shareholder support. Among the other 65 proposals, more than 90% of shareholders voted against 63 of them, and shareholder opposition averaged 95%. Yet 49 of the 63 overwhelmingly rejected proposals were eligible for resubmission, and 14 of them were actually resubmitted proposals. It is hard to see how allowing a shareholder proposal rejected by 95% of shareholders is in the median shareholder's interest.

Were the SEC to adopt a 33% threshold as an intermediate (or even ultimate) floor for multiple shareholder-proposal resubmissions (a level sufficiently high that it would require at least some shareholder voting support beyond votes that merely follow proxy-advisory firms' guidance), 215 of the 608 resubmitted proposals would have been ineligible for resubmission—an only modestly higher number than those rejected under a baseline 10% rule. Conversely, 393 of 608 proposals that were resubmitted at least once would have been eligible for essentially perpetual resubmission. Thus, even a 33% threshold would be rather generous, only weeding out 35% of currently resubmitted proposals. Of course, the SEC may wish to adopt an even higher ultimate threshold—at or near 50%—since the propriety of permitting a minority of shareholders to

⁸¹ See Nucor Corp., *Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934*, proposal no. 3 (Mar. 21, 2016). A cumulative voting rule, which Nucor previously had, allowed shareholders to aggregate all their votes for directors up for election on a single preferred candidate. The company had long maintained, in response to the Carpenters Fund proposal, that the board could not adopt the fund's preferred rule for not seating any director not receiving a majority of votes in an uncontested election in light of the company's cumulative voting mechanism.

perpetually introduce a ballot item that two-thirds of shareholders reject is questionable, at best.⁸²

7. Corporate Political Spending and Lobbying Disclosures

Ever since the Supreme Court's 2010 decision in *Citizens United v. Federal Election Commission*⁸³—which determined that independent political expenditures were speech protected by the First Amendment, even if funded by for-profit corporations—corporate political engagement has been much debated.⁸⁴ The decision drew a rebuke from President Obama in his

⁸² By way of comparison, it is worth noting that many states with initiative ballot processes prevent reintroduction of the same or substantially similar ballot item when a voter-sponsored initiative fails to receive 50% support. See NCSL: *Restrictions on Repeat Measures*. For example, in Massachusetts, when an initiative is proposed on a ballot, then voted on and ultimately rejected, the law provides: “A measure cannot be substantially the same as any measure that has been qualified for submission or appeared on the ballot at either of the two preceding biennial state elections.” *I.e.*, there is a six-year ban on any resubmission. Rules such as Massachusetts's both put a stay on unpopular resubmission attempts for an extended period and anticipate the submission of similar “new” submissions in an effort to get around the rule, hence the “substantially the same” language. Of course, state-law initiatives would tend to be binding, not merely precatory; so the SEC would probably prefer to permit any shareholder proposal that receives 50% support just once to be resubmitted multiple times, if not acted upon, for a number of years—regardless of subsequent shareholder votes.

⁸³ 558 U.S. 310 (2010).

⁸⁴ For the purposes of this statement, I take no position on the constitutional issues underlying the Supreme Court's controversial decision in *Citizens United*. Indeed, under *Citizens United*, Congress may be able to regulate certain further disclosures of political spending, corporate or otherwise, without running afoul of the First Amendment. See *id.* at 366–67 (citing *McConnell v. FEC*, 540 U.S. 93, 198 (2003)) (rejecting facial and as-applied challenges to disclosure requirement).

That said, many proponents of a government-mandated disclosure regime in this area have too casually assume the constitutionality such proposals, without giving careful consideration to the distinction between facial and as-applied constitutional challenges and the Supreme Court's focus, in the *Citizens United* decision itself, on the potential harassment of speakers, including corporations. See, e.g., Lucian A. Bebchuk & Robert J. Jackson, Jr., *Shining Light on Corporate Political Spending*, 101 GEO. L.J. 923, 954–55 (2013) (arguing that it is “clear” that “that the Constitution leaves ample room for disclosure rules of this kind”) (citing Lucian A. Bebchuk & Robert J. Jackson, Jr., *Corporate Political Speech: Who Decides?*, 124 HARV. L. REV. 83, 107–11 (2010) (asserting that “the constitutional permissibility of the disclosure requirements that [they] propose is straightforward”).

Political spending disclosure requirements do not necessarily or easily pass constitutional muster. Rather, the Supreme Court “has subjected these requirements to ‘exacting scrutiny,’ which requires a ‘substantial relation’ between the disclosure requirement and a ‘sufficiently important’ governmental interest.” *Citizens United*, 558 U.S. at 366–67 (citing *Buckley v. Valeo*, 424 U.S. 1, 64 66 (1976)).

Even in cases in which a disclosure statute passes constitutional muster on its face, it may fail an “as applied” challenge when there exists “a ‘reasonable probability’ that disclosure of its contributors’ names ‘will subject them to threats, harassment, or reprisals from either Government officials or private parties.’” *Id.* (citing *McConnell*, 540 U.S. at 198 (quoting *Buckley*, 424 U.S. at 74)). In *Citizens United*, the Court reaffirmed this principle, see *id.* at 916 (observing that a disclosure statute “would be unconstitutional as applied to an organization if there were a reasonable probability that the group’s members would face threats, harassment, or reprisals if their names were disclosed”), but noted that “*Citizens United* . . . ha[d] offered no evidence that its members may face similar threats or reprisals. . . . [and indeed] ha[d] been disclosing its donors for years and ha[d] identified no instance of harassment or retaliation.” *Id.*

In contrast to the dearth of evidence demonstrating that disclosure of donors to *Citizens United* raised the risk of harassment or retaliation, ample evidence exists that companies would be subject to reprisals for donating to some of the very trade associations and business groups specifically targeted by the proponents of corporate political spending disclosure. See Letter from Comm. on Disclosure of Corp. Pol. Spending, to Elizabeth M. Murphy, Sec’y, U.S. Sec. & Exch. Comm’n 10 n.29 (Aug. 3, 2011), available at <http://www.sec.gov/rules/petitions/2011/petn4->

2010 State of the Union address, with many of the Supreme Court justices in front of him.⁸⁵ In 2011, several U.S. senators, including 2016 Democratic presidential candidate Bernie Sanders of Vermont, proposed amending the First Amendment in response.⁸⁶ Also in 2011, several professors of corporate and securities law petitioned the SEC seeking to have the agency establish rules for publicly traded companies to disclose fully their political spending, direct and indirect.⁸⁷ The rulemaking petition has become increasingly politicized in 2016, as U.S. Senators have openly clashed with the chairman of the SEC, Mary Jo White, over the agency's failure to respond to the petition;⁸⁸ and some of these same senators have even seized on the issue to block President Obama's new appointees to the SEC.⁸⁹

Although agitation with the SEC over corporate political spending traces largely to *Citizens United*, efforts to inject the issue into the 14a-8 shareholder-proposal process predate the controversial court decision. In 2003, Bruce Freed, a former Democratic congressional staffer, founded an organization, the Center for Political Accountability (CPA), exclusively to “campaign for corporate political disclosure and accountability.”⁹⁰ Dating back to 2006, the first year covered in the Proxy Monitor database, at least 19 shareholder proposals on companies' political engagements have been placed on Fortune 250 corporations' proxy ballots each year (**Figure 8**). The number of such proposals started to increase after *Citizens United*, peaking at 67 in 2014, before falling somewhat in 2015 and 2016. Nevertheless, as was the case last year, proposals related to corporate political spending or lobbying were the second-most-common class of shareholder proposals introduced in 2016.

637.pdf [hereinafter the Petition] (asserting that disclosure of “contributions to intermediaries that spend a large fraction of their funds on politics . . . seems warranted,” and singling out the U.S. Chamber of Commerce). Both social-investing funds, such as Walden Asset Management, and government agents managing public-employee pension funds, such as the New York City Comptroller, have harassed and implicitly threatened reprisals against companies known to be affiliated with the U.S. Chamber. See Press Release, Walden Asset Mgmt., Investors Call on Companies Sitting on The U.S. Chamber of Commerce Board to Evaluate Their Role (Jan. 31, 2011), available at <http://climate.bna.com/climate/document.aspx?ID=153882>; Press Release, N.Y. City Comptroller, Comptroller Liu Calls on Siemens AG To Cut Ties to U.S. Chamber of Commerce (Jan. 24, 2011), available at http://comptroller.nyc.gov/press/2011_releases/pr11-01-007.shtm. In addition, the activist group Color of Change harassed companies known to be affiliated with the American Legislative Exchange Council, causing several such companies to drop their membership. See Press Release, Color of Change, Color of Change Applauds Procter & Gamble's Decision to End its Membership in ALEC: More Than a Dozen Companies Have Left the American Legislative Exchange Council (Apr. 23, 2012), available at

<http://www.colorofchange.org/press/releases/2012/4/23/colorofchange-applauds-procter-gamblesdecision-en/>.

⁸⁵ See Adam Liptak, *Supreme Court Gets a Rare Rebuke, in Front of a Nation*, N.Y. TIMES, Jan. 28, 2010, http://www.nytimes.com/2010/01/29/us/politics/29scotus.html?_r=0.

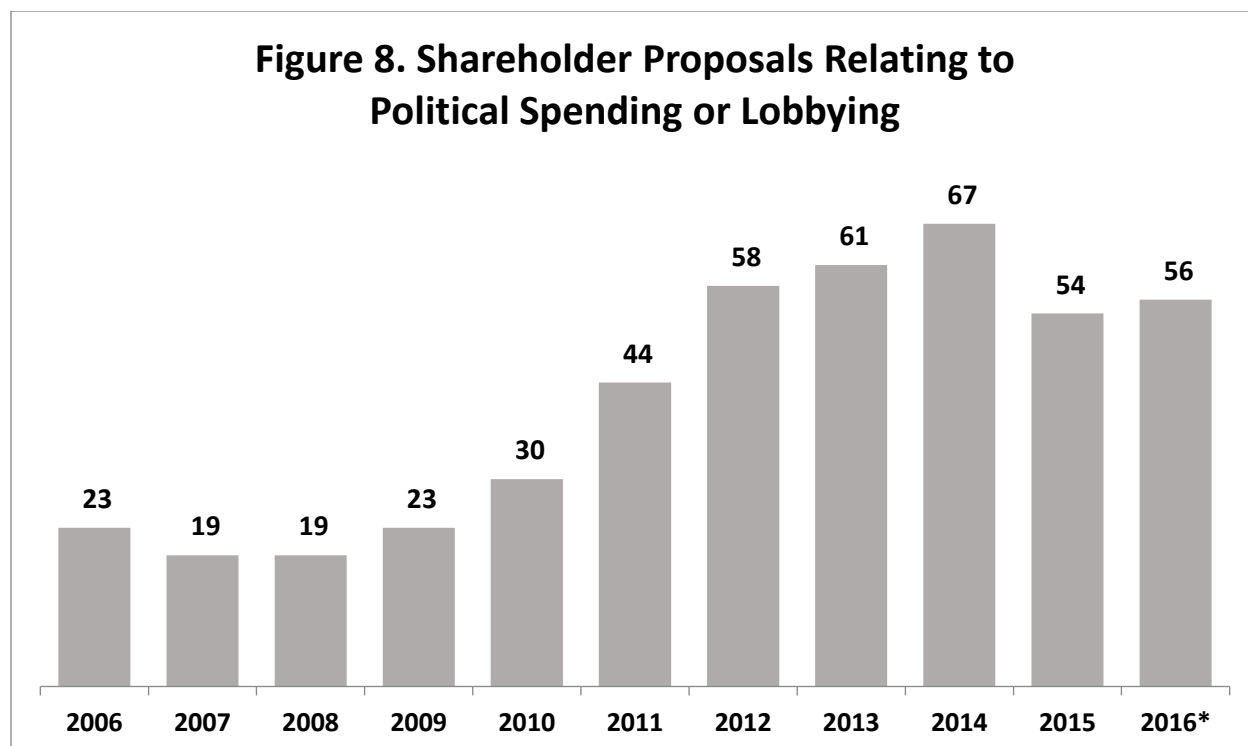
⁸⁶ See Pete Kasperowicz, *Sanders Proposes Amendment to the Constitution That Would Limit Free Speech*, THE HILL, Dec. 9, 2011, <http://thehill.com/blogs/floor-action/senate/198343-sanders-offers-constitutional-amendment-to-strip-corporations-of-first-amendment-rights>.

⁸⁷ See Petition, *supra* note 84. For a fuller response, see James R. Copland, *supra* note 6.

⁸⁸ See Francine McKenna, *Schumer Says SEC's White Is 'Poisoning' Politics*, MARKETWATCH, Jun. 15, 2016, <http://www.marketwatch.com/story/schumer-says-secs-white-is-poisoning-politics-2016-06-14>.

⁸⁹ Andrew Taylor & Marcy Gordon, *Democrats Block SEC Nominees*, U.S. NEWS & WORLD RPT., Apr. 7, 2016, <http://www.usnews.com/news/business/articles/2016-04-07/democrats-block-sec-nominees-over-political-money-fight>. I should disclose that I went to law school with one of the stalled nominees, Hester Peirce, whom I consider a friend.

⁹⁰ Center for Political Accountability, About the CPA, <http://politicalaccountability.net/about/about-us>.



*In 2016, based on 231 companies holding annual meetings by August 31
 Source: ProxyMonitor.org

As previously noted, the submission of shareholder proposals on this topic has not translated into majority shareholder support. From 2006 through 2016, companies in the Proxy Monitor database have faced votes on 446 board-opposed shareholder proposals that relate to corporate political spending or lobbying; 445 have failed to garner majority shareholder support. These actual shareholder votes held in recent years on the numerous shareholder proposals introduced on corporate political spending clearly show that a majority of shareholders believe that increased disclosure of corporate political spending as called for in shareholder proposals and in the professors’ rulemaking petition with the SEC is not in their interests as shareholders.

It is not hard to understand why. As a threshold matter, the amount of money that publicly traded corporations spend on politics—including through trade associations and other intermediaries—is not material by any reasonable standard. Among the political committees organized under Section 527 of the Internal Revenue Code, are, after *Citizens United*, political action committees that can, independently of candidate campaigns, spend money for political purposes (so-called “Super PACs”); contributions to and expenditures by such organizations must be fully disclosed. In the 2012 political cycle, such PACs raised over \$838 million and spent over \$631 million⁹¹—significant sums, to be sure, but a pittance in comparison with overall public-company budgets: the combined revenues of the 200 largest U.S. companies in 2012 exceeded \$9.4 trillion.⁹²

⁹¹ See Super PACs, CTR. FOR RESPONSIVE POL., <http://www.opensecrets.org/pacs/super/pacs.php?cycle=2012>.

⁹² See Fortune 500, CNN MONEY (May 21, 2012), http://money.cnn.com/magazines/fortune/fortune500/2012/full_list/ (listing top 500 U.S. companies by revenues). Note that certain of the Fortune 200 companies are not publicly held. That said, the 42 largest companies on the

Moreover, contributions to these Super PACs from publicly traded companies have proved virtually nonexistent.⁹³

Of course, the clamor for increased disclosures of corporate political spending would not rest on disclosed dollars given to Super PACs but rather non-disclosed groups including social-welfare organizations and trade associations organized respectively under sections 501(c)(4) and 501(c)(6) of the Internal Revenue Code, which can make political expenditures but do not have to publicly disclose their donors.⁹⁴ But the total amount spent by all outside groups in the 2012 election—including Super PACs, 527 committees, and 501(c) organizations (not only social-welfare organizations and trade associations but also labor unions)—was just over \$1 billion (drawn from all sources, corporate or not).⁹⁵ That’s equivalent to 0.011% of the Fortune 200 companies’ 2012 budgets—less than the development cost of a single biotechnology product,⁹⁶ and less than the amount that automobile manufacturers and dealers spent on television advertising spots with local broadcasting stations in the third quarter of 2012.⁹⁷ It is impossible

2012 Fortune 200 list, with a combined revenues exceeding \$5 trillion, are publicly traded (Fannie Mae and Freddie Mac, however, were delisted upon entering government receivership). The two largest American private companies, Cargill and Koch Industries do not show up on the *Fortune* list, presumably due to data limitations. See Andrea Murphy & Scott DeCarlo, *America’s Largest Private Companies*, FORBES (Nov. 28, 2012), <http://www.forbes.com/largest-private-companies/>. The largest company on the 2012 Fortune list that is not a public C corporation is State Farm, a mutual insurer, at 43rd. While the presence of such companies marginally inflates the revenues of the Fortune 200 attributable to public companies, it is also of course the case that many companies, beyond the 200 largest, make money, are publicly listed, and may be involved directly or indirectly in political spending.

⁹³ See, e.g., Anna Palmer & Annie Phillip, *Corporations Don’t Pony Up for Super PACs*, POLITICO (Mar. 8, 2012), <http://www.politico.com/news/stories/0312/73804.html> (“When super PACs emerged two years ago, critics howled that corporations would take advantage of a newfound tool to flex their muscle in politics. But so far this campaign season, publicly traded companies have shied away from the outside groups—giving less than one half of a percent of all the contributions raised by the most active super PACs.”). As I noted in my article in the *Harvard Business Law Review*:

Five [Super] PACs spent over \$20 million in the 2012 campaign: the pro-Romney Restore Our Future, the pro-Obama Priorities USA Action, Karl Rove’s American Crossroads, and Super PACs supporting Senate and House Democrats; all told, these five PACs raised and spent a majority of all Super PAC dollars in the campaign (raising and spending \$428 million and \$380 million, respectively). Only one publicly traded corporation was among the top fifty organizational donors to any of these Super PACs: the small-cap, family-controlled but Nasdaq-listed Clayton Williams Energy, which contributed \$1 million to American Crossroads. And the top-fifty donor list comprised most of each Super PAC’s funding, in total over \$314 million of the \$428 million these five political committees raised.

Copland, *supra* note 6, at 388 (citations omitted).

⁹⁴ Cf. NAACP v. Alabama, 357 U.S. 449 (1958) (holding that organization’s freedom of association rights prevented Alabama from requiring disclosure of its contributor lists).

⁹⁵ See 2012 Outside Spending, by Group, CTR. FOR RESPONSIVE POL., <http://www.opensecrets.org/outsidespending/summ.php?cycle=2012&type=p&disp=O>.

⁹⁶ See Joseph A. DiMasi & Henry G. Grabowski, *The Cost of Biopharmaceutical R&D: Is Biotech Different?*, 28 MANAGERIAL & DEC’N ECON. 469–79 (2007) (estimating the total development cost of a biotechnology product at \$1.2 billion).

⁹⁷ See Top 25 Local Broadcast TV Categories, Spot TV Q3, TVB Local Media Marketing Solutions, <http://www.tvb.org/trends/4705> (citing Kantar Media) (showing local spot TV “automotive” spend of \$925 million and “car and truck dealers” of \$273 million in the third quarter of 2012).

to conclude that political spending, on its own, is material to investors' pecuniary interests as shareholders.⁹⁸

Rather than involving a financial interest for investors, shareholder proposals filed seeking additional political spending or lobbying disclosures appear to be premised on a *political* goal: namely, to chill corporate political speech. Across the 2006–16 period, fully 53% of shareholder proposals related to corporate political spending have been sponsored by labor-affiliated pension funds (**Figure 9**)—representing interests that themselves spend heavily on the political process, often in opposition to corporations. State and municipal pension funds—including the two most active sponsors of these types of proposals, the funds for public employees in New York City and State—are often wholly or significantly controlled by partisan elected officials whose political interests may be adverse to corporations' interests. Indeed, my prior research has shown that labor-affiliated pension funds' sponsorship of such shareholder proposals has tended to target companies whose executives and political action committees gave disproportionately to Republicans.⁹⁹ Aside from labor-affiliated investors, most political-spending-related shareholder proposals have been sponsored by social-investing funds, which by definition are not oriented solely around share value and may have social or policy goals opposed to the corporations they are targeting.

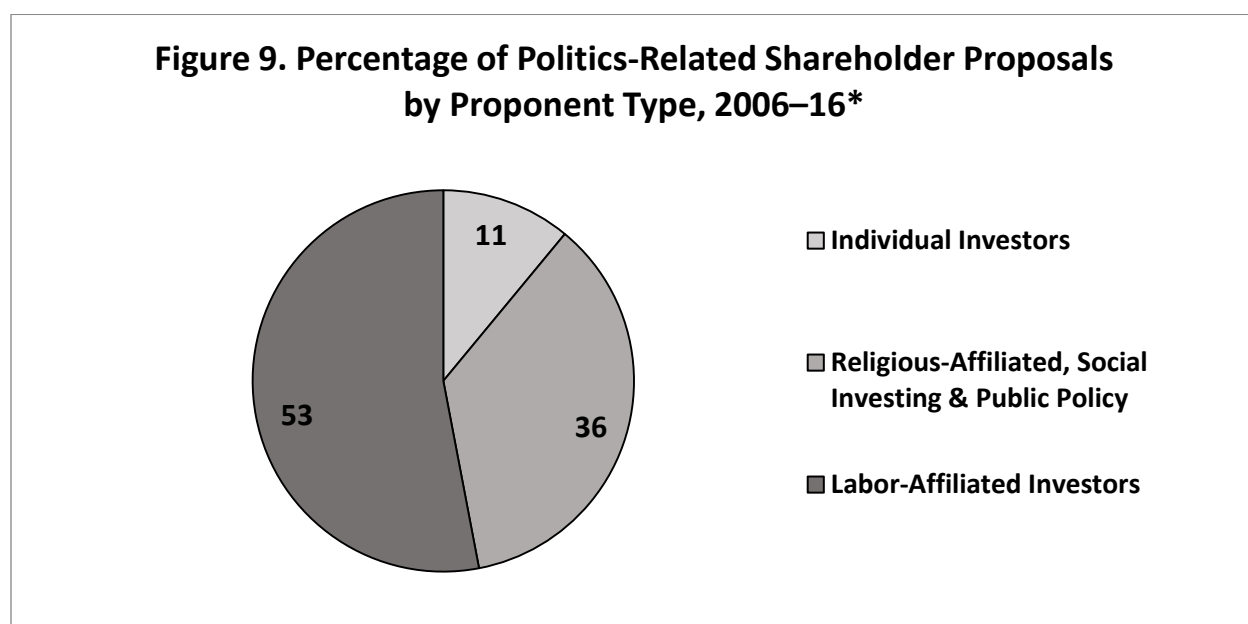
The public record amply demonstrates that many of the same sponsors of shareholder proposals seeking additional corporate disclosures of political spending also seek to influence corporations to disassociate from trade associations or to dissuade such groups from taking positions contrary to the special-interest sponsors' particular political preferences. For instance, in January 2011, leaders of the AFL-CIO Office of Investment, Domini Social Investments, Green Century Capital Management, the Nathan Cummings Foundation, and Trillium Asset Management—each

I am not the first to make this sort of comparison. In a 2010 blog post, UCLA's Stephen Bainbridge compared total 2008 political spending to Procter & Gamble's 2008 advertising on soap and toilet paper. *See* Is Citizens United the death of democracy, PROFESSORBAINBRIDGE.COM (Oct. 19, 2010), <http://www.professorbainbridge.com/professorbainbridgecom/2010/10/is-citizens-united-the-death-of-democracy.html>.

⁹⁸ Auditors typically assume that for publicly traded companies, an item is not material if it is “not greater than 5 percent of net income before income taxes.” Audit Manual Excerpt: Materiality Guidelines, Williams & Adams, CPAs, http://highered.mcgraw-hill.com/sites/dl/free/0078025435/928516/WA_Materiality_Guidelines_8e.pdf. Consistent with this general principle, under SEC rules, shareholder proposals are deemed not relevant and excludable from a publicly traded corporation's proxy statement “[i]f the proposal relates to operations which account for less than 5 percent of the company's total assets at the end of its most recent fiscal year, and for less than 5 percent of its net earnings and gross sales for its most recent fiscal year” 17 C.F.R. § 240.14a-8(i)(5) (2008). (Shareholder proposals involving corporate political spending, like other cases involving “political and moral predilections,” can appear on proxy ballots under an exception to this rule discussed in section 1, *infra*.) Similarly, under Regulation S-K, the SEC deems that legal proceedings are not material “if the amount involved, exclusive of interest and costs, does not exceed 10 percent of the current assets of the registrant and its subsidiaries on a consolidated basis.” 17 C.F.R. § 229.103(2) (2008).

⁹⁹ *See* James R. Copland & Margaret M. O'Keefe, *Proxy Monitor: A Report on Corporate Governance and Shareholder Activism 2* (Manhattan Institute 2014) (“The 43 Fortune 250 companies facing shareholder proposals sponsored by labor-affiliated investors in 2014 were twice as likely to orient their political efforts to support Republicans than was the average Fortune 250 company. A majority of shareholder proposals sponsored by labor-affiliated investors in 2014 have involved corporate political spending or lobbying, and only one company targeted by these proposals gave more money to Democrats than Republicans.”), *available at* http://www.proxymonitor.org/Forms/pmr_09.aspx.

a regular sponsor of political-spending-disclosure shareholder proposals—all co-signed a letter sent to 35 companies serving on the board of the U.S. Chamber of Commerce urging the companies “to evaluate” their role with the trade association and objecting to the Chamber’s “education and lobbying efforts to defeat legislative [sic] and regulation related to climate change, consumer protection, and financial reform.”¹⁰⁰ Former New York City Comptroller John Liu, who manages the city’s five pension funds for retired public employees, sent a similar letter to at least one company in which the funds invested.¹⁰¹ Bruce Freed’s CPA has both led and joined coalition letters pressuring companies to vocalize disagreement with trade association political positions.¹⁰² It is hard to escape the conclusion that the highly politicized push for greater corporate disclosures surrounding political spending and lobbying is about political rather than financial goals.



*In 2016, based on 231 companies holding annual meetings by August 31
 Source: ProxyMonitor.org

8. The Costs of Pension Funds’ Social-Issue Activism

For sound policy reasons—most notably federalism and comity shown to the states—federal law governing pension plans exempts state and municipal plans for public employees.¹⁰³ Nevertheless, the operation and solvency of plans is a matter of significant public-policy concern: public pension funds for state and municipal workers in the United States have accumulated, by most recent estimates, approximately \$4 trillion in obligations—roughly one-

¹⁰⁰ Press Release, Walden Asset Mgmt., *supra* note 84.

¹⁰¹ See Press Release, N.Y. City Comptroller, *supra* note 84.

¹⁰² See CPA Leads Effort to Press Companies on Climate-Change Misalignment; Company Cuts Chamber Dues, CTR. FOR POL. ACCOUNTABILITY NEWSLETTER (Nov. 2009), <http://www.politicalaccountability.net/index.php?ht=a/GetDocumentAction/i/2663>.

¹⁰³ See 29 U.S.C. § 1003(b).

fourth of U.S. GDP and almost 130 percent of state and local governments' annual budgets—to fund government workers' retirements.¹⁰⁴ Actual assets available to fund these obligations, however, total only about \$3 trillion, leaving a \$1 trillion shortfall that threatens to jeopardize public employees' retirement security and/or burden the public fisc—potentially squeezing out vital spending on health, education, and infrastructure.¹⁰⁵ I and many of my Manhattan Institute colleagues have written about at some length;¹⁰⁶ so I wanted to bring to the attention of Congress some of the research we have sponsored that relates to the impact of such pension funds' social-investing activism on share value.

The ultimate test of whether shareholder proposals are an effective tool—at least from the standpoint of the average diversified investor—is not whether they win majority shareholder support but whether they enhance share value.¹⁰⁷ Individual investors might, of course, have different priorities, and certain institutional investors are designed to have different priorities. But precisely because most investors inherently disagree about many issues of public concern, corporate governance has tended to assume that shareholder value is the orienting concern for equity investors; such concerns are implicit in the fiduciary duties that pension funds owe to retirees.¹⁰⁸

To study the relationship between public-employee pension funds' shareholder activism and share value, the Manhattan Institute commissioned an econometric study by Tracie Woidtke, a professor at the Haslam College of Business at the University of Tennessee.¹⁰⁹ Building on a

¹⁰⁴ Pew Charitable Trusts and Laura and John Arnold Foundation, *State Public Pension Investments Shift over Last 30 Years* 1 (June 2014),

<http://www.pewtrusts.org/en/research-and-analysis/reports/2014/06/03/state-public-pension-investments-shift-over-past-30-years>. GDP data are available at

<http://www.bea.gov/national/an1.htm>. State and local budget data are available at <http://www.census.gov/govs/local>.

¹⁰⁵ See Pew Charitable Trusts, *supra* note 104.

¹⁰⁶ For a fuller discussion, see James R. Copland & Steven Malanga, *Safeguarding Public-Pension Systems: A Governance-Based Approach* (Manhattan Institute 2016), available at <http://www.manhattan-institute.org/html/safeguarding-public-pension-systems-governance-based-approach-8595.html>.

¹⁰⁷ Traditionally, corporate law has oriented corporate boards and managers' fiduciary duties around a single variable, share value, see *Dodge v. Ford Motor Co.*, 170 N.W. 668. (Mich. 1919) (holding that corporate fiduciary duties flowed to shareholders, not employees or other interests), which avoids the ownership costs—chiefly conflicts of interest that arise among various owners—that are inherent in non-corporate ownership forms. See generally HENRY HANSMANN, *THE OWNERSHIP OF ENTERPRISE* 35–49 (1996) (arguing that the costs of collective decision-making best explain the predominance of the corporate equity-ownership form in large-scale for-profit enterprise); see also Stephen M. Bainbridge, *The Case for Limited Shareholder Voting Rights*, 53 UCLA L. REV. 601 (2006) (arguing that increasing shareholder power imposes significant costs in reduced managerial authority). Since shortly after *Dodge v. Ford* was decided, an academic debate has proliferated between those arguing for a social responsibility for corporations, see E. Merrick Dodd, Jr., *For Whom are Corporate Managers Trustees?*, 45 HARV. L. REV. 1145, 1148 (1932) (arguing for the view that “the business corporation as an economic institution which has a social service as well as a profit-making function”), and those supporting the traditional rule centered on share value, see Adolf A. Berle, Jr., *For Whom Corporate Managers Are Trustees: A Note*, 45 HARV. L. REV. 1365, 1367 (1932).

¹⁰⁸ 29 C.F.R. § 2509.08-2(1) (2008) (requiring pension plan managers to “consider only those factors that relate to the economic value of the plan’s investment” and not to “subordinate the interests of the participants and beneficiaries in their retirement income to unrelated objectives”). These fiduciary duties under ERISA do not apply to pension plans for state and municipal employees or for those affiliated with religious institutions. See 29 U.S.C. § 1003(b).

¹⁰⁹ See *The University of Tennessee Knoxville: Tracie Woidtke*, <http://finance.bus.utk.edu/Faculty/TWoidtke.asp>.

research methodology initially developed for her doctoral dissertation, Woitke examined the valuation effects associated with pension fund influence, measured through ownership, on Fortune 250 companies, during 2001–13.¹¹⁰ Firm value was assessed through industry-adjusted Tobin’s Q, with various controls added to the analysis, including firm leverage, research and development expenses, advertising expenses, index membership, assets, positive income, stock transaction costs, insider ownership, and year fixed effects.

Woitke finds that “public pension funds’ ownership is associated with lower firm value” and, more particularly, that “social-issue shareholder-proposal activism appears to be negatively related to firm value.”¹¹¹ As such, public employee pension funds’ use of the shareholder-proposal process in an effort to affect corporate behavior in pursuit of social or policy goals may be harming the financial interests of plan beneficiaries—and ultimately state and local taxpayers—as well as, by inference, the average diversified investor.

Conclusion

In sum, it is hard to argue that the 14a-8 shareholder-proposal process is functioning well. A small group of shareholders dominates the process—including idiosyncratic individual “corporate gadflies” and institutional investors whose interests diverge from the ordinary diversified investor, namely labor-affiliated pension funds and social-investing funds. Increasingly, the 14a-8 process has tilted toward social and political concerns with little relationship to share value, market efficiency, or capital formation. By co-opting proxy advisory firms with substantial power over voting outcomes but limited resources, these activists are able to finance their agendas at other shareholders’ expense—even when most shareholders vote down the activists’ ideas repeatedly. At least some shareholder-proposal activism appears to be depressing share value.

Rule 14a-8 is a long-standing rule that has some utility, but activists have seized upon the SEC’s outdated and overly permissive standards to push policy agendas—and chill political speech—in an effective end-run around Congress. Congress has a vested interest in addressing this situation and reorienting the SEC around its statutory obligation to “promote efficiency, competition, and capital formation.”¹¹²

¹¹⁰ See Woitke, *supra* note 8, at 3.

¹¹¹ See *id.* at 16.

¹¹² 15 U.S.C. § 78c(f).