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Tough Dilemmas for Companies on Campaign Spending

January 6, 2012

By: Ben W. Heineman, Jr.

Should companies use funds from the corporate treasury to advocate directly for or against political candidates in contested elections?

This basic question — now made immediate with the opening of the election season in the Iowa caucuses — raises dilemmas for boards and business leaders:

- Should we adopt detailed governance rules or keep decisions informal and in a small group?
- Should we be passive and avoid such spending, or be active and get involved in partisan politics?
- Should we voluntarily disclose all expenditures or keep expenditures hidden unless disclosure is required by law?
- Should we support generally moderate candidates who can compromise on major structural issues facing the U.S., or narrow, even ideological candidates who will advocate for issues of immediate concern to the corporation?

These are some of the most salient issues of campaign finance facing CEOs and boards of directors as the nation heads into what will certainly be a bitter election year, with both houses of Congress and the Presidency up for grabs. As well, it is a time of political gridlock on major social, economic and budgetary issues, and the choices leaders make pose real risks and opportunities — financial, legal, reputational and political — for companies.

The issues arise in the wake of the Supreme Court's 2010 decision in *Citizens United v. Federal Communications Commission* which declared unconstitutional the provisions of the *Bipartisan Campaign Reform Act* of 2002 (McCain-Feingold) that had prohibited corporations and unions from paying directly for ads even if those ads were made independently of a candidate's campaign.

Prior to *Citizens United*, most major corporations participated in campaign finance through employee funded Political Action Committees (PACs) which are legally authorized to make direct contributions to candidates under strict limits (e.g. \$5,000 per election). Now, in addition to such limited employee PAC contributions, corporations can use unlimited company funds for either (a) "independent expenditures" which support or oppose a particular candidate, or (b) "electioneering communications" which may mention a candidate favorably or unfavorably in a discussion of campaign issues but which do not expressly advocate election or defeat.

This power in corporations (and unions) to make unlimited expenditures independent of campaigns has spawned a robust ideological debate: does it constitute freedom of speech and advocacy, or does it distort the American political culture and invite corruption. *But underneath the contentious issues of corporate free speech lie equally fundamental questions for each company about its positions on first order public policy issues which affect the strength of American society and the American economy.*

Let me offer some perspective, if not definitive positions, on each of these tough new dilemmas raised by direct expenditures from corporate treasuries after *Citizens United* (putting employee PAC issues to the side as largely unchanged from past practice):

Adopt and Publish Governance Measures

Given the importance of independent expenditures or electioneering communications, corporations would clearly be wise to have governance procedures that, among other things: ensure compliance with applicable law; make clear that funds are to be used for the good of the corporation not for goals of individual officers; demarcate a high level group of business leaders who will make such decisions; delineate principles, policies and priorities which will guide such decisions in the particular election cycle (such positions may be set forth in the public policy section of a company's citizenship report); have a systematic process for submission and approval of funding requests; audit both adherence to law and to company policy; and ensure that a board committee, or the board itself, oversees these core aspects of corporate campaign finance. Such procedures seem unexceptionable to me as a standard means of ensuring due care is taken on important corporate decisions. More than half of the S&P 100 have instituted such governance measures, but this trend does not appear to be taking hold with smaller public companies. (See the website of the [Center for Political Accountability](#))

Avoid Direct Expenditures Altogether

Some major corporations — such as Pfizer and UPS — have taken the position that they will not use corporate funds directly either for independent expenditures or for electioneering communications. The reasons for this abnegation include the following: a desire to avoid being constantly battered on all sides for campaign funds by activists associated with candidates or causes; a desire to avoid being caught up in the intensely partisan nature of our current electoral battles, and to present a non-partisan face to national constituencies across the political spectrum; a lack of skill in political advertising; and an understanding that corporate funds may be more effectively spent developing and advocating public policy positions after elections in the Congress, the Executive, the regulatory agencies and the courts. When I was at GE, before *Citizens United*, we chose not to use corporate funds for "soft money/issue ads" for precisely these reasons (and the company today expressly states it will not engage directly in independent expenditures).

Disclose Company's Own Political Spending

If a company chooses to use its own funds for direct campaign spending, the issue raised in many shareholder proposals is whether such corporations should — in addition to the governance procedures noted above — issue a comprehensive report which lists in one place all the recipients both of such direct spending and of contributions made from the company's employee PAC. Such a report would aggregate legally required individual reports — and any other campaign funding — to afford stakeholders a consistent and comprehensive overview. Again, more than half the S&P 100 have committed to the issuance of such a report, although precise details (such as frequency) may differ. I believe that such spending is an important dimension of a corporation's activity and should be disclosed. Put another way, in an open society where long-term corporate performance is built on trust among its various constituencies, it is difficult to defend hiding such direct corporate action (or forcing stakeholders to piece information together from myriad reports), even though a comprehensive report may cause stakeholder or media scrutiny and criticism. Upholding disclosure requirements in *Citizens United*, Justice Kennedy stated that "prompt disclosure of expenditures can provide shareholders and citizens with information needed to hold corporations....accountable."

Disclosing Policy and Spending for Trade Associations

This is the area of greatest controversy. Much of the direct spending for or against a candidate independent of a politician's campaign is carried out by so-called social welfare organizations or **trade associations** established as non-profits under the tax laws (sections 501(c)(4) and 501(c)(6)). Other direct spending on "issues" to influence an election is undertaken by so-called "**527 organizations**," which are also set up under the tax laws. Under long-standing policy, the IRS does not disclose the donors to these

organizations. Thus, corporations can, through dues or other donations, keep their identities hidden when such tax-exempt organizations engage in direct campaign spending. The involvement of individual corporations is also hidden when those entities organized under the tax laws give money to so-called "Super PACs" which are of looming importance in this election. The Super PACs are organized under the Federal Election Law; can raise and spend unlimited political funds so long as they do not "coordinate" with formal campaigns; and have to reveal only the umbrella organizations, not individual corporations, that give them money. The obvious benefit of such organizational spending for corporations is that it aggregates resources, but the risk is that a trade association may support candidates whose basic positions are at odds with the public positions of the company.

The limiting cases on trade association policy and disclosure are companies that seek to prohibit trade associations from using dues for campaign spending altogether, (see, e.g. Wells Fargo) or, on the other hand, companies that let such associations do as they wish. A handful of corporations seek a middle ground. They may seek more information about association political activities, including how much of a company's dues are spent on politics, and disclose that. Alternatively, they may simply report if their dues to a trade association active in campaign spending exceed a certain threshold — say, \$25,000. (See, e.g. Merck) Generally, such trade association disclosure is sporadic — even among companies who issue reports on their own actions — and often opaque.

Ultimately, public policy must change if there is to be consistent disclosure of specific corporate donors by trade associations and Super PACs. It makes little sense that organizations regulated by the Federal Election Commission have to disclose campaign donors, but associations regulated by the IRS do not, when those associations are active in campaign spending — and contributing to Super PACs. The SEC has a petition before it on requiring uniform disclosure on campaign finance for all publicly held companies, but, given Dodd-Frank overload and partisan rancor about its role in general, the SEC is unlikely to act on this anytime soon (certainly not in this election cycle). The chances of Congressional action on this issue in 2012 are zero.

Shareholder Proposals on Information Requests Only

Shareholder proposals have rightly played an important role in prodding companies both to adopt governance measures and to disclose campaign spending, often following a model developed by the Center for Political Accountability. The percentage of votes cast in favor of such "procedural" proposals has been increasing with each succeeding proxy season (an average of 20% from 2004-2010 and an average of 30% in 2011, with eight over 40%). But, in my view, it would be a serious mistake to give shareholders a vote (advisory or otherwise) on companies' campaign spending. (Such proposals are being submitted at a few companies this year and a bill to this effect, following UK

precedent, has been introduced in Congress, albeit with no prospect of success.) This could turn annual meetings into heated political contests over what is, essentially, a complex business judgment. If shareholders do not like the corporation's position on public policy or candidate support/opposition, they can withhold votes from directors and deny them the majority of votes cast which are necessary at most corporations today for automatic re-election.

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At the end of the day, important as governance procedures and disclosure policies are, they should not obscure the fundamental question boards and business leaders must address: *What are the corporation's substantive and detailed policy positions on critical issues facing the nation?* Obviously, those policy positions will guide both campaign spending and advocacy before governmental institutions, and each company will have to make its own decisions about those substantive positions.

But, I would end with this thought. Unless we have a political system capable of addressing our nation's most basic issues, we are doomed to decline. No set of issues is more fundamental than resolving our acute fiscal imbalance and putting in place policies to create economic growth. Our current fractured, polarized and demagogic political system makes compromise on such policies close to impossible. For example, many business people in the Fortune 500 would broadly support the "**Simpson-Bowles**" solution to the budget deficits set forth in December 2010 as a fair "sharing of the pain." Yet, Simpson-Bowles has many controversial, painful provisions which can only pass with bipartisan support — from elimination of tax benefits (home owners deduction, non-tax of employee health plans) to defense cuts to changes in Medicare and Social Security to individual tax reform. It is DOA in the current Congress.

Were I still in business and still deeply involved in decisions about public policy, my fundamental criterion in this election would be for companies to use fully disclosed and accounted for employee PAC funds to support moderates (from either party) who could work to find, not block, solutions to our related deficit and growth issues. The ultimate campaign spending dilemma facing corporations, in my view, is how to find and support such candidates in a year which — due in no small part to inflammatory and unlimited campaign spending — is more likely to exacerbate partisanship than moderate it.

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