THE YALE LAW JOURNAL ONLINE

ELIZABETH POLLMAN

Citizens Not United: The Lack of Stockholder Voluntariness in Corporate Political Speech

With the Supreme Court hearing a new round of oral arguments in *Citizens United v. Federal Election Commission*,[1] the Court appears poised to alter dramatically the landscape of corporate political speech law. The case concerns whether the government may limit a nonprofit political advocacy group from showing a film during election season when the film casts an electoral candidate in a negative light and is financed in part by corporate donations. In the first round of argument, Citizens United narrowly argued that the Bipartisan Campaign Reform Act of 2002[2] could not constitutionally be applied to its feature-length, video-on-demand film, which it argued did not contain express advocacy and was funded primarily by individual donations rather than general corporate expenditures. Unexpectedly, at the end of last Term, the Court asked the parties to address in re-argument whether it should overrule two key precedents upholding restrictions on corporate political spending from general funds: *Austin v. Michigan Chamber of Commerce*[3] and part of *McConnell v. FEC*.[4]

In reconsidering these precedents the Court should modernize its analysis of an important concern expressed for over a century in this context: that when corporations are allowed to spend general funds on electoral advocacy, stockholders may have money they invested in a corporation used for political advocacy they oppose. Dramatic changes in the amount and types of U.S.

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1. 129 S. Ct. 2893 (2009).
2. Pub. L. No. 107-155, 116 Stat. 81 (2002).
3. 494 U.S. 652 (1990) (holding that corporations may be prohibited from spending general funds on electoral advocacy).
4. 540 U.S. 93 (2003) (upholding the facial validity of a provision of the Bipartisan Campaign Reform Act prohibiting corporations from using their general funds to pay for certain "electioneering communications").

stockholding have occurred in the past several decades that should heighten this concern, making it more compelling than ever, particularly in combination with the related concern about the corruptive influence of corporate money in politics. Overruling *Austin* and *McConnell* could clear the way for the nation's largest for-profit corporations to electioneer with general treasuries amassed from investors who did not intend the money be used for political purposes and who will not likely obtain relief.

I. ORIGINS OF THE CONCERN ABOUT STOCKHOLDER VOLUNTARINESS IN CORPORATE POLITICAL SPEECH

The concern about stockholder voluntariness in corporate political speech[5] dates back to the early 1900s and a scandal involving life insurance company executives who used corporate funds for self-serving political contributions.[6] The public was outraged that company executives would use other people's money for their own personal gain or to suit their own personal political tastes, exploiting stockholders who did not wish to make a political statement with their financial investments. Although stockholders are generally not involved in corporate decisionmaking, they entrust directors as fiduciaries to manage the corporation, which in the for-profit business context is often characterized as for the purpose of maximizing firm value.[7] In response to the public call for corporate spending reform, President Theodore Roosevelt told Congress: "All contributions by corporations to any political committee or for any political purpose should be forbidden by law; directors should not be permitted to use stockholders' money for such purposes . . . ."[8] Subsequently, Congress passed the Tillman Act of 1907,[9] which banned corporations from spending money "in connection with" any federal election.[10] The concern about corporate political

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5. Because the Court does not appear to be reconsidering underlying premises such as whether corporations should be treated as "persons" with constitutional rights, or whether the spending of money on elections is "political speech," this Essay uses such terminology without commenting on its merit.

6. *See* Adam Winkler, *"Other People's Money": Corporations, Agency Costs, and Campaign Finance Law*, 92 GEO. L.J. 871, 887-96 (2004).

7. ROBERT CHARLES CLARK, CORPORATE LAW 21-24, 93-140, 675-703 (1986).

8. United States v. UAW-CIO, 352 U.S. 567, 572 (1957)(quoting 40 CONG. REC. 96 (1905)); *see also* McConnell, 540 U.S. at 115 (same).

9. Pub. L. No. 59-36, 34 Stat. 864 (1907).

10. *See McConnell*, 540 U.S. at 115.

spending without stockholder consent has continued to find a voice through a century of case law.[11]

At times, however, the Court has given little weight to this concern. In *First National Bank v. Bellotti*,[12] the Court reasoned that the concern was not critical because a stockholder "is free to withdraw his investment at any time and for any reason."[13] Further, the Court noted that stockholders "may decide, through the procedures of corporate democracy, whether their corporation should engage in debate on public issues," and "generally have access to the judicial remedy of a derivative suit to challenge corporate disbursements . . . ."[14] Whatever the strength of these assertions in 1978 when the Court decided *Bellotti*, significant changes in investment patterns in the intervening decades undercut their validity today.

II. STOCK OWNERSHIP IN THE UNITED STATES

Changes in U.S. stockholding patterns and demographics in the past several decades have been dramatic. Whereas in the early 1980s less than one-fifth of American households owned stock, today nearly *half* of American households own stock.[15] This explosion in numbers has brought increasing diversity to the composition of American stock owners.[16] They have stock ownership in common but are otherwise heterogeneous across multiple demographic categories and almost certainly across the political spectrum. Thus, a near majority of Americans now stands to have their investments used by corporations for electoral speech they may oppose.

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11. *See, e.g.*, FEC v. Beaumont, 539 U.S. 146, 154 (2003); Austin v. Mich. Chamber of Commerce, 494 U.S. 652, 675 (1990) (Brennan, J., concurring); FEC v. Mass. Citizens for Life, 479 U.S. 238, 257-58 (1986); FEC v. Nat'l Right To Work Comm., 459 U.S. 197, 207-08 (1982); Pipefitters Local Union No. 562 v. United States, 407 U.S. 385 (1972); United States v. UAW-CIO, 352 U.S. 567 (1957); United States v. CIO, 335 U.S. 106 (1948).

12. 435 U.S. 765 (1978).

13. *Id.* at 794 & n.34.

14. *Id.* at 794-95.

15. *See* INV. CO. INST. & SEC. INDUS. ASS'N, EQUITY OWNERSHIP IN AMERICA, 2005, at 1, *available at* http://www.sifma.org/research/pdf/EquityOwnership05.pdf; *see also* INV. CO. INST. & SEC. INDUS. & FIN. MKTS. ASS'N, EQUITY AND BOND OWNERSHIP IN AMERICA, 2008, at 7, *available at* http://www.ici.org/pdf/rpt_08_equity_owners.pdf.

16. *See* JOINT ECON. COMM., THE ROOTS OF BROADENED STOCK OWNERSHIP (2000) (citing data from the Federal Reserve Board's Survey of Consumer Finances).

Moreover, a large amount of U.S. household stock ownership is indirect—through mutual funds, 401(k) accounts, or other pension or retirement plans.[17] Indeed, ninety percent of equity-owning U.S. households own stock in mutual funds.[18] This translates to nearly half of U.S. households, a huge increase over the six percent figure in 1980.[19] This indirect type of stock ownership has characteristics that should heighten the concern about corporations spending general funds for electoral speech: stockholders likely will have neither access to information about the political spending of the corporations in which their money is indirectly invested nor the ability to sell the stock of a particular corporation if they disapprove.

III. INADEQUATE RELIEF FOR DISSENTING STOCKHOLDERS

Even if dissenting stockholders surmounted information and collective action problems and did not face liquidity problems, they would still be left with few options for relief: sell the stock or pursue a derivative action. Neither of these options, however, gives dissenting stockholders prospective relief or a remedy that would put them in the position they would have been in had the corporate spending not occurred. Selling the stock avoids only future instances in which the corporation spends general funds on political speech that the stockholders oppose; it does nothing to address the political spending that already occurred.[20]

A derivative action based on corporate political spending is also unlikely to provide relief. First, unless the dissenting stockholders can make a case for fraud or breach of the duty of loyalty for conduct like self-dealing, they are unlikely to pass the combination of hurdles necessary to succeed at trial. Stockholders would have to make a demand on the board or show futility, withstand a high bar at the motion to dismiss stage, and, assuming the case does not settle, overcome the highly deferential business judgment rule. This last obstacle could prove particularly difficult as the directors could potentially rationalize their conduct of making or overseeing political contributions as

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17. *See* INV. CO. INST. & SEC. INDUS. ASS'N, EQUITY OWNERSHIP IN AMERICA, *supra* note 15, at 1-2.

18. *Id.* at 1.

19. INV. CO. INST., 2009 INVESTMENT COMPANY FACT BOOK 72 (49th ed. 2009), *available at* http://www.ici.org/pdf/2009_factbook.pdf.

20. Justice Brennan correctly observed this point in *Austin*, noting: "Of course, a member could resign from the Chamber and a stockholder could divest from a business corporation that used the Chamber as a conduit, but these options would impose a financial sacrifice on those objecting to political expenditures." Austin v. Mich. Chamber of Commerce, 494 U.S. 652, 674 (Brennan, J., concurring).

being in the interest of the corporation or justified on another basis.[21] Second, even if the dissenting stockholders were to succeed in a derivative action, they would not likely obtain meaningful recovery. Directors rarely pay damages out of their own pockets,[22] and the corporation would not likely obtain reimbursement from the political candidate or organization that received the corporate donation.

Procedures of corporate democracy such as a shareholder proposal likewise offer limited promise for dissenting stockholders. Corporations often seek to exclude shareholder proposals from their proxy statements and social responsibility-oriented shareholder proposals that do make it onto proxy statements rarely break the vote threshold needed to succeed.[23] Even when shareholder proposals pass, they are generally not binding upon directors.[24]

Other procedures of corporate democracy such as director elections also do not empower stockholders to control the corporation's political spending. Stockholders' implicit power to replace directors does not ensure that

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21. See, for example, the well-known case *Shlensky v. Wrigley*, 237 N.E.2d 776 (Ill. App. Ct. 1968), often cited for the proposition that a director could justify a decision made for noneconomic reasons by saying the decision was based on the long-term financial interest of the corporation. Charitable giving and constituency statutes could also potentially provide bases for justification. *See* Einer Elhauge, *Sacrificing Corporate Profits in the Public Interest*, 80 N.Y.U. L. REV. 733, 763 (2005) (noting that every state has a statute giving managers authority to donate corporate money to charitable purposes and thirty states have corporate constituency statutes giving managers authority to consider nonshareholder interests, such as the interests of the community or society).

22. *See* Bernard Black, Brian Cheffins & Michael Klausner, *Outside Director Liability*, 58 STAN. L. REV. 1055, 1063-64 (2006).

23. For information on when proposals must appear in proxy statements, see 17 C.F.R. § 240.14a-8 (2008). *See also* Lucian Arye Bebchuk, *The Case for Shareholder Access: A Response to the Business Roundtable*, 55 CASE W. RES. L. REV. 557, 564 (2005) ("[P]ast voting patterns clearly indicate that shareholder resolutions that are brought because of their appeal to shareholders with special interests generally do not pass. Shareholder resolutions that focus on social or labor issues generally fail."); Adam J. Sulkowski & Kent Greenfield, *A Bridle, a Prod, and a Big Stick: An Evaluation of Class Actions, Shareholder Proposals, and the Ultra Vires Doctrine as Methods for Controlling Corporate Behavior*, 79 ST. JOHN'S L. REV. 929, 943-45 (2005) (noting that shareholder proposals "rarely receive more than a small percentage of the actual vote" and that "[e]ven shareholder activists acknowledge that shareholder proposals would not get anywhere if not for a coordinated public relations effort"). Notably, a few years ago three institutional investors failed to pass a shareholder proposal that called for board oversight and disclosure of soft money contributions. The proposal garnered only about ten percent of the vote at twelve of the twenty-three companies targeted. Dana Gold et al., *Protecting the Polity: Strategies for Reform*, 30 SEATTLE U. L. REV. 991, 1005 (2007).

24. *See* 17 C.F.R. § 240.14a-8 (2008); *see also* Sulkowski & Greenfield, *supra* note 23, at 943 (noting that directors have discretion to consider and disregard shareholder proposals).

management will act in a certain desired way.[25] Further, a proxy campaign to elect a slate of directors to carry out a preferred policy would involve significant expense and delay, during which time incumbent managers could continue corporate political spending without stockholder consent. Moreover, stockholders likely lack information on political spending and are diverse in their preferences. At best, in the context of large publicly-held corporations, the majority view would rule and some stockholders would have corporate funds used for political speech they oppose.

IV. NEW STOCKHOLDER VOLUNTARINESS ISSUES IN LIGHT OF GOVERNMENT BAILOUTS

Finally, as we are entering a world in which the federal government has become a large, even controlling, stockholder in some of the nation's largest corporations, the possibility of overruling *Austin* and part of *McConnell* raises new questions. In the absence of strict restrictions and oversight on the use of the bailout money, taxpayer money in the form of government bailouts might be used by corporations for the reelection of politicians who treated the corporation or executives favorably. Taxpayers might have no direct recourse. This potential result may strike the public as particularly offensive because one set of agents—corporate management—would be in a position to spend other people's money for electing another set of agents—political representatives—who may be the same people who orchestrated bailouts in the first instance.

CONCLUSION

As the Supreme Court reconsiders prior decisions upholding limits on corporate electioneering from general funds, this Essay suggests that the longstanding concern about the lack of stockholder assent to corporate political speech is more compelling than ever. Patterns of U.S. stockholding have significantly changed in the past several decades so as to heighten the concern and caution against a broad overruling of precedents. Stockholders' ability to sell their securities or pursue a derivative action, and other means of corporate democracy, do not alleviate the concern. A broad decision in favor of Citizens United could leave even stockholders who carefully screen and monitor their investments at risk of having money they invested used for political advocacy they oppose.

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25. *See* Lucian Ayre Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833, 851-61 (2005).

Elizabeth Pollman is a Stanford Law Fellow. *Many thanks to my colleagues at Stanford Law School, Joan Howarth, Elaine Shoben, Jessie Rossman, and the editors of* The Yale Law Journal Online *for their helpful comments on this piece.*

Preferred citation: Elizabeth Pollman, *Citizens Not United: The Lack of Stockholder Voluntariness in Corporate Political Speech*, 119 YALE L.J. ONLINE 53 (2009), http://www.yalelawjournal.org/2009/10/15/pollman.html.