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## **An Unexpected Friend: Liberalism’s Response to Corporate Political Spending**

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### ABSTRACT

Much of the scholarly literature critical of the Supreme Court’s decision in *Citizens United* rings true to people predisposed to view corporate power and free markets with suspicion. In this Article, I seek to reach a different audience—people who believe in the power of free markets to promote social welfare. To do so, I maintain that corporate political expenditures are inconsistent with the principles of classical liberalism and against the interests of the corporations that make the expenditures.

I also pose solutions consistent with classical liberalism. If corporate political spending so threatens the system that preserves liberty and the efficient operation of a free-market society, it is reasonable, under classical liberalism, to permit the state to set rules to preserve its limited role. It also follows that if corporate spending on independent political expenditures is not in the interests of corporations or shareholders, managers should voluntarily limit them by entering industry-wide agreements, or, at minimum, adopt policies requiring full disclosure of the expenditures.

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*“But what does ‘freedom’ mean? When men mutually agreed to pass laws against robbing, mankind became more free, not less so. Individuals locked into the logic of the commons are free only to bring on universal ruin; once they see the necessity of mutual coercion, they become free to pursue other goals.”*<sup>1</sup>

*“To many, the word coercion implies arbitrary decisions of distant and irresponsible bureaucrats; but this is not a necessary part of its meaning. The only kind of coercion I recommend is mutual coercion, mutually agreed upon by the majority of the people affected.”*<sup>2</sup>

—Garrett Hardin, *The Tragedy of the Commons*

## I. INTRODUCTION

Much of the scholarly literature critical of the Supreme Court’s *Citizens United v. Federal Election Commission*<sup>3</sup> decision is likely to ring true to people predisposed to view corporate power and free markets with suspicion.<sup>4</sup> Although many of those articles are well reasoned and advance the analysis of the issue, few contain arguments likely to convince people who believe in the

1. Garrett Hardin, *The Tragedy of the Commons*, 162 *SCIENCE* 1243, 1248 (1968).

2. *Id.* at 1247. Hardin argued that the pursuit of individual interests in a commons (a place with limited resources) courts “ruin.” *Id.* at 1244. As to pollution, he observed the same problem, but in reverse. There, the issue is not what is removed, but rather what is added. A person acting only in her own interests benefits from each unit of pollution she is able to discharge, and bears only a portion of the costs, which are distributed among the rest of society. Hardin, although respectful of the power of the markets for promoting social welfare, recognized that in the commons, “[r]uin is the destination toward which all men rush, each pursuing his own best interest in a society that believes in the freedom of the commons.” Hardin, *supra* note 1, at 1244. To address the problem, he argued for self-imposed limits on human behavior.

3. 558 U.S. 310 (2010).

4. See Ronald Dworkin, *The “Devastating” Decision*, N.Y. REV. BOOKS, Feb. 25, 2010, <http://www.nybooks.com/articles/archives/2010/feb/25/the-devastating-decision>; Richard L. Hasen, *Money Grubbers: The Supreme Court Kills Campaign Finance Reform*, SLATE (Jan. 12, 2010, 12:58 PM), [http://www.slate.com/articles/news\\_and\\_politics/jurisprudence/2010/01/money\\_grubbers.html](http://www.slate.com/articles/news_and_politics/jurisprudence/2010/01/money_grubbers.html).

power of free markets to promote social welfare. Preaching to the choir rarely reaches an audience beyond the congregation. Real progress on the issue of corporate political expenditures requires engagement among people who have more fundamental philosophical disagreements.<sup>5</sup> That engagement entails listening without judgment, and accepting, at least initially, that others hold their beliefs in good faith. Agreement is not necessary, but a commitment to society requires “tolerance” and “humility” grounded on the recognition that no one is right all of the time.<sup>6</sup> As Milton Friedman maintained, people holding divergent views have little hope of resolving differences unless they ask, “‘what facts [and presumably arguments] . . . if they were observed, [would each person] . . . regard as sufficient to contradict [his or her] view, and *vice versa*?’ and then [consider] whether the evidence contradicts or supports the view [each] has.”<sup>7</sup>

I use the term liberalism as Milton Friedman and Friedrich Hayek used it. Friedman referred to liberalism as “the intellectual movement that . . . emphasize[s] freedom as the ultimate goal and the individual as the ultimate entity in the society. . . . pertaining to a free man.”<sup>8</sup> Similarly, Hayek wrote, “[t]he fundamental principle [of liberalism is] that in the ordering of our affairs

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5. In this Article, I maintain that corporate political expenditures are inconsistent with liberalism and contrary to the long-term interests of the corporations that make them. I believe that individual political expenditures may also be inconsistent with principles of liberalism, but this Article is limited to addressing corporate political expenditures. If one is to advocate that corporations cease spending their own money on independent political expenditures, it is necessary to take a consistent position with respect to individual spending by high-net-worth individuals, or somehow distinguish it. See Amy J. Sepinwall, *Citizens United and the Ineluctable Question of Corporate Citizenship*, 44 CONN. L. REV. 575, 579-91 (2012). See generally Carl R. Rogers, *Interpersonal Relationships: U.S.A. 2000*, 4 J. APPLIED BEHAV. SCI. 265 (1968) (discussing importance of listening); Milton Friedman, *Milton Friedman on Libertarianism and Humility*, YOUTUBE (Aug. 14, 1990), <http://www.youtube.com/watch?v=bibfslEFk2s> (“[The process to get] closer to those fundamental principles [is to recognize] the opinions of people who fundamentally disagree with us.”).

6. See KEITH C. BARTON & LINDA S. LEVSTIK, *TEACHING HISTORY FOR THE COMMON GOOD* 33 (2004) (arguing citizens in democratic societies must consider question of how we can “live together justly” by seeking out common ground that recognizes shared value of our human community); AMY GUTMANN & DENNIS THOMPSON, *DEMOCRACY AND DISAGREEMENT* 12 (1996) (arguing American democracy requires collective deliberation); Friedman, *supra* note 5 (“I regard the basic human value that underlines my own beliefs as tolerance based on humility. I have no right to coerce someone else because I cannot be sure I am right and he is wrong.”).

The conception of deliberative democracy that we defend here . . . . consists of three principles—reciprocity, publicity, and accountability—that regulate the process of politics, and three others—basic liberty, basic opportunity, and fair opportunity—that govern the content of policies. It would promote extensive moral argument about the merits of public policies in public forums, with the aim of reaching provisional moral agreement and maintaining mutual respect among citizens.

GUTMANN & THOMPSON, *supra*, at 12 (footnote omitted).

7. Friedman, *supra* note 5.

8. MILTON FRIEDMAN, *CAPITALISM AND FREEDOM* 5-6 (40th Anniversary ed. 2002). There is, of course, the argument that corporate political spending is contrary to liberalism to the extent that it elevates corporate entities and unions over the individual, and creates a state of entities not individuals.

we should make as much use as possible of the spontaneous forces of society, and resort as little as possible to coercion.”<sup>9</sup> As discussed in more detail below, unlike some current proponents of libertarianism, liberalism provides that government has an important role in setting the rules of the game, mediating disputes, and acting in the few, but important, areas where markets cannot act efficiently.<sup>10</sup>

I maintain that corporate political spending is inconsistent with liberalism because it: undermines government’s ability to fulfill its proper role; weakens the checks and balances that the separation of political and economic power places on political authority; and reduces the ability of individuals to counter special interests, be well informed, and create a society consistent with individual liberty. Furthermore, it is an inefficient use of corporate profits, and is inconsistent with the rights of shareholders. I elaborate on each of these rationales in turn in Part II.<sup>11</sup> In Part III, I address a potential demurrer from corporate managers. That is, they might respond to the foregoing arguments with a question—why should we care if corporate political spending is inconsistent with liberalism if it seems profitable? I respond that corporate political spending is not in the long-term interests of corporations because, as set forth in Part II: it undermines the ability of government to fulfill an organizational role that is essential to the success of corporations, it is not the most efficient use of corporate funds, it risks a backlash from shareholders and intervention by regulators, and it offsets any short-term gains.<sup>12</sup> In Part IV, I seek a solution. If corporate political spending so threatens the system that preserves liberty and the efficient operation of a free-market society, it is reasonable to permit the state to impose rules to preserve its limited role, or for a solution to come from the market and voluntary action.<sup>13</sup> If spending their money on independent political expenditures is not in the interests of

9. F. A. HAYEK, *THE ROAD TO SERFDOM* 71 (Bruce Caldwell ed., Routledge 2008) (1944).

10. *See generally* AYN RAND, *ATLAS SHRUGGED* (1957). Rand’s argument does not respond to those who believe that there should be no role for government. Though there are anarchist arguments for the creation and maintenance of rules, the question of whether corporate political expenditures are consistent with anarchist philosophy is beyond the scope of this Article. *See generally* ROBERT NOZICK, *ANARCHY, STATE, AND UTOPIA* (Blackwell Publishing 2004).

11. *See infra* Part II.A (discussing effect of corporate spending on government’s ability to fulfill its role); Part II.B (examining how corporate political spending weakens checks and balances on political authority); Part II.C (considering conflict between corporate political spending and shareholders’ property rights and contractual firm theory); Part II.D (analyzing corporate political spending’s effect on individual rights and liberty).

12. *See infra* Part II.A (discussing how corporate political spending undermines government’s ability to fulfill role); Part II.B (examining how corporate political spending furthers business and government convergence producing increased government intervention); Part II.C (explaining how corporate political spending can clash with shareholders’ rights and interests); Part III (explaining short-term gains outweighed by damage to governmental ability and corporate reputation).

13. *See* Andreas Georg Scherer & Guido Palazzo, *Toward a Political Conception of Corporate Responsibility: Business and Society Seen from a Habermasian Perspective*, 32 *ACAD. MGMT. REV.* 1096, 1107 (2007) (discussing paper industry compact requiring sustainable harvesting of forest resources).

corporations, then there will be no need for coercion. Corporate leaders will recognize that the long-term costs of corporate political expenditures exceed the likely benefits and voluntarily limit them, or adopt policies requiring the disclosure of what they do with the funds, both of which some corporations have already done.<sup>14</sup> The purpose of this Article then is to argue that corporate political expenditures are inconsistent with liberalism and contrary to the long-term interests of the corporations that make them.

## II. CORPORATE POLITICAL SPENDING IS INCONSISTENT WITH LIBERALISM

There are two distinct concerns with respect to corporate political spending—corruption (i.e., politicians will favor the entities who spent money to help them get elected) and distortion (i.e., those with more money will overwhelm the airwaves, thereby preventing the public from hearing a wide range of messages).<sup>15</sup> One could imagine a world in which people could only disseminate anonymous advertisements supporting or opposing candidates for office. In this world, corruption concerns would virtually disappear, because politicians would not know who spent money to get them elected. But distortion concerns would remain. Part II is divided into four sections to address liberalism’s response to the problems of both corruption and distortion.

### *A. Corporate Political Spending Undermines Government’s Ability To Fulfill Its Proper Role*

This section addresses corruption, and the problem of too much business involvement in government. To maximize economic and personal freedom, liberalism recognizes that it is the proper role of the state to set, mediate and enforce “the rules of the game.”<sup>16</sup> Friedman explained that the “existence of a free market does not . . . eliminate the need for government. On the contrary, government is essential both as a forum for determining the ‘rules of the game’ and as an umpire to interpret and enforce the rules decided on.”<sup>17</sup> He summarized the role of the state as follows:

The need for government . . . arises because absolute freedom is impossible. However attractive anarchy may be as a philosophy, it is not

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14. See *Political Contributions Policy*, COLGATE, <http://www.colgate.com/app/Colgate/US/Corp/Governance/GlobalEthicsandCompliance/PoliticalContributionsPolicy.cvsp> (last visited Feb. 15, 2014) [hereinafter *Colgate Policy*].

15. See *Citizens United v. Fed. Election Comm’n*, 558 U.S. 310, 394 (2010) (Stevens, J., dissenting). In his dissenting opinion, Justice Stevens identified both corruption and distortion as problems associated with corporate political spending. See *id.* at 447-61 (Stevens, J., dissenting) (discussing anticorruption interests); *id.* at 465-76 (Stevens, J., dissenting) (discussing antidistortion argument).

16. FRIEDMAN, *supra* note 8, at 15 (internal quotation marks omitted).

17. *Id.* Applying the umpire analogy—who would play a game (or would think it fair) if the rulemaker or the umpire selected owed her position to the financial expenditures of the opposing team?

feasible in a world of imperfect men. Men's freedoms can conflict, and when they do, one man's freedom must be limited to preserve another's—as a Supreme Court Justice once put it, “My freedom to move my fist must be limited by the proximity of your chin.”<sup>18</sup>

Thus, contrary to common perceptions of liberalism, “[t]he consistent liberal is not an anarchist”<sup>19</sup> and government plays an important role in the organization and maintenance of the market and “law and order [so as] to prevent coercion of one individual by another.”<sup>20</sup> Implicitly recognizing the necessary limits on free enterprise, Friedman defined the concept with the following:

In the United States, “free” [in the context of the term free enterprise] has been understood to mean that anyone is free to set up an enterprise, which means that existing enterprises are not free to keep out competitors except by selling a better product at the same price or the same product at a lower price.<sup>21</sup>

In describing the liberal view, Scherer and Palazzo write, “the market cannot establish the conditions of its own existence. Rather, these conditions have to be erected by the state apparatus that defines the rules of the game.”<sup>22</sup> As Berle and Means wrote, the operation of the market and corporate law can lead to an improper separation of ownership from control within the corporation such that the interests of corporate managers diverge from those of their principals, the shareholders.<sup>23</sup> One of the ways government defines the rules of the game is to work to make sure that the separation of ownership from control does not work an injustice on the owners, the shareholders. With those principles in mind, the following examples demonstrate a manifestation of a different facet of the agency problem, or the same problem but with differing practical effects. They also highlight the proper role of government in a free society and demonstrate how corporate political spending interferes with the ability of government to fulfill that role.<sup>24</sup>

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18. *Id.* at 25-26.

19. *Id.* at 34; *see id.* at 35-36 (listing things governments do now but should not).

20. FRIEDMAN, *supra* note 8, at 27.

21. *Id.* at 26.

22. Scherer & Palazzo, *supra* note 13, at 1106.

23. *See generally* ADOLF A. BERLE & GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* (Transaction Publishers 1991) (1932).

24. With respect to the manner in which government is to fulfill its role, liberalism maintains that the rules that government enacts should be “imposed so far as possible in accordance with the preferences and desires of the public,” and in order to enact laws, it is necessary to “persuade a majority of . . . citizens to be of like mind,” which must be “attain[ed] by undemocratic procedures.” Milton Friedman, *The Social Responsibility of Business Is To Increase Its Profits*, N.Y. TIMES MAG., Sept. 13, 1970, at 32, 122-23.

*Example 1.* Pennsylvania Judges are accused of accepting kickbacks from a for-profit youth detention center in connection with declaring over 2,000 minors delinquent, and forcibly sending them to the center.<sup>25</sup>

In connection with the responsibility of government to set the rules of the game, government may properly enact laws prohibiting bribery even where bribery would otherwise make the corporation more profitable. The need to protect individual liberty against wrongful detention and maintain fair competition among other for-profit youth detention facilities permits the state to impose limits on the liberty of businesses to use their money as they see fit.<sup>26</sup>

*Example 2.* Companies that manufacture weapons systems donate money to an industry group that uses the funds to purchase advertising supporting and opposing the election of candidates. Representative Johnson is nearing the end of her first term in office and faces a strong competitor in an upcoming election. Her campaign funds are running out. Lobbyist Peterson lets her know that he believes that the industry will support her, and asks whether she will be a “friend”<sup>27</sup> to the industry as Congress considers whether to approve a new defense system that would generate income for the corporations.

Liberalism recognizes government’s role in providing for and determining the amount of public funds that will be allocated to national defense.<sup>28</sup> One person may believe that society needs X amount of defense, while another person may believe we need 2X.<sup>29</sup> The defense industry, like any other, wishes to maximize its profits. Its main customer is the state. The more “defense” the state purchases, the better the industry fares, but the industry’s request in the above example would exert undue influence on the representative, and the

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25. See *Pennsylvania: Mixed Verdict for Disgraced Judge*, N.Y. TIMES, Feb. 18, 2011, [http://www.nytimes.com/2011/02/19/us/19brfs-Judge.html?\\_r=0](http://www.nytimes.com/2011/02/19/us/19brfs-Judge.html?_r=0); *Luzerne Kids-for-Cash Scandal*, JUV. L. CENTER, <http://www.jlc.org/current-initiatives/promoting-fairness-courts/luzerne-kids-cash-scandal> (last updated Feb. 2012).

26. The example is somewhat complicated by the fact that a public official is involved, but similar reasoning would apply to laws against bribing a manager of a supplier to offer goods at a discounted price.

27. See *PARK AVENUE: MONEY, POWER & THE AMERICAN DREAM* (PBS Nov. 12, 2012), available at <http://video.pbs.org/video/2296684923>. The PBS film *Park Avenue* used the term “friend” to describe the way lobbyists and politicians discuss whether the politician will be voting consistently with the wishes of the lobby. The producers also interviewed Jack Abramoff, who, in 2006 pled guilty to two counts of fraud in connection with lobbying activities. Upon his release three-and-a-half years later, Abramoff began lobbying against problems he saw with the system. In the film, he explained, “when you have campaigns that are costing tens of millions of dollars, the people who have the money want something back. Money is being used to buy results. That is the problem. That is how I used money. I knew what I was doing.” *PARK AVENUE: MONEY, POWER & THE AMERICAN*, *supra*; see Kate Zernike & Anne E. Kornblut, *From Big-Time Lobbyist To Object of Derision*, N.Y. TIMES, Jan. 10, 2006, <http://www.nytimes.com/2006/01/10/politics/10lobbyist.html?pagewanted=print> (describing Abramoff guilty plea and aftermath).

28. See *FRIEDMAN*, *supra* note 8, at 23.

29. See *id.*

result of the vote may be in the interests of the industry and Representative Johnson, but not necessarily her constituents.

The defense industry's action in Example 2 is the political equivalent of the agency problems arising from the separation of ownership from control. Here, Johnson's role is akin to a corporate manager, except that her principals are the citizens of her state, not shareholders. The industry is providing Johnson with an incentive that may cause her to elevate her interests over those of her principals, the public. That action prevents government from fulfilling its proper role.

*Example 3.* A mining industry group, led by Jane Lobbyist spends \$200,000, which it collected from member mining companies in Pennsylvania, on advertising in support of the election of Jim, a candidate for the state legislature with few other financial resources. Although Jim was initially down in public opinion surveys, exit polls credited the mining industry's advertisements as the main reason for the shift. Three years into his four-year term a new bill, which would prohibit mining in pristine areas of the state, is coming up for a vote. If enacted, the bill would protect the water supplies of a town, preserve the important trout fishing and tourism industry, and ensure the purity of the sources of two national water-bottling companies. On the day of the vote, which comes on the eve of a new election cycle in which the legislator is again short on cash and up against a strong opponent, Jane approaches Jim and asks whether he is going to be a "friend" of the mining industry with respect to the bill.<sup>30</sup>

In Example 3, the industry's exercise of its free speech rights exerts undue influence on Jim and creates several conflicts inconsistent with liberalism, including one among industry groups. If Jim is a "friend" of the mining industry, he is against the interests of at least three other industries, tourism, fishing, and spring-water bottling. If one side is largely responsible for his election, its exercise of corporate free speech rights may undermine Jim's ability to enact efficient market rules for other corporations.

One response may be that the other businesses should also exercise their free speech rights. That is not an efficient solution. Such a system would create a wasteful arms race, requiring several industries to spend money on advertising where they could otherwise invest the money in the production of better and less expensive products or return it to shareholders.<sup>31</sup>

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30. See David J. Jackson & Steven T. Engel, *Don't Bite the PAC that Feeds You: Business PAC Punishment over the China Vote*, 31 AM. POL. RES. 138, 149 (2003) (reporting corporations withhold money from politicians who do not support industry-favored laws).

31. One might reasonably wonder whether there is an advertising lobby behind corporate political spending because that industry seems to be the one that benefits most from such spending.



*Example 4.* As Friedman observed,

[the federal government maintained] import quotas on oil. Keeping oil wells idle most of the time to keep up prices seems to me featherbedding of precisely the same kind as paying coal firemen on diesel locomotives for being idle. Yet some representatives of business who are loudest in their condemnation of labor featherbedding as a violation of free enterprise—notably the oil industry itself—are deafeningly silent about featherbedding in oil.<sup>32</sup>

When federal import quotas on oil need to be renewed or are about to expire, it does not strain credulity to imagine that instead of staying “silent” (as Friedman wrote above), industry lobbyists might argue for the retention of quotas and purchase advertising supporting candidates who vote in favor of import quotas and opposing those who would seek to end them.

Friedman maintains that tariffs lead to inefficient industry and coercion.<sup>33</sup> Protectionism allows inefficient companies to prosper when market forces would otherwise see them fail, which under liberalism, they should do. Tariffs are coercive because they prevent willing exchanges between people who would otherwise trade.<sup>34</sup> As Friedman explained:

Tariffs have of course been imposed largely to “protect” domestic industries, which means to impose handicaps on potential competitors. They always interfere with the freedom of individuals to engage in voluntary exchange. After all, the liberal takes the individual, not the nation or citizen of a particular nation, as his unit. Hence he regards it just as much a violation of freedom if citizens of the United States and Switzerland are prevented from consummating an exchange that would be mutually advantageous as if two citizens of the United States are prevented from doing so.<sup>35</sup>

To the extent that corporate political expenditures help the industries protected by tariffs and harm others, they create an inefficient market and are contrary to liberalism’s support of free trade.

*Example 5.* A recent news article reported “three major private prison corporations spent roughly \$45 million over the past decade to influence state and federal government.”<sup>36</sup> In that story, *The Nation* identified the following

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32. FRIEDMAN, *supra* note 8, at 126.

33. *See id.* at 129.

34. *See id.*

35. *Id.*; see Gus Lubin, *25 American Products that Rely on Huge Protective Tariffs To Survive*, BUS. INSIDER (Sept. 27, 2010, 3:20 PM), <http://www.businessinsider.com/americas-biggest-tariffs-2010-9?op=1>.

36. Lee Fang & Francis Reynolds, *What Does Millions in Lobbying Money Buy? Five Congresspeople*

members of Congress and the amount of money they received or spent on their behalf by the private prison industry over the years: Marco Rubio \$33,500; John McCain \$127,725; John Cornyn \$31,950; Lamar Smith \$17,750; Jim Sensenbrenner \$7,750.<sup>37</sup>

The main tenant of liberalism—and implicitly the greatest wish of citizens—is the maximization of individual freedom. The prison industry, like any other, wishes to maximize its profits, but it makes more money when more people are placed in prison. Its main customer is the state. The more “incarceration” the state purchases, the better the industry fares, but the industry’s payments in the above example would exert undue influence on the representative, and the result may be in the interests of the industry and politicians, but not necessarily the public.

*Example 6.* A March 13, 2013 ProPublica article provides that the EPA changed its stance on an aquifer exemption needed for a uranium mining project in Goliad County, Texas, after prominent Democratic lobbyist Heather Podesta lobbied the EPA’s top administrators.<sup>38</sup> Reportedly, Uranium Energy Corp. paid Podesta and her employer \$400,000 to intervene on their behalf.<sup>39</sup>

The problem of corporate political spending becomes especially acute in cases where “strictly voluntary exchange is either exceedingly costly or practically impossible.”<sup>40</sup> One example of such a situation is where the market cannot limit the effects of a use of private property to those willing to accept its burdens.<sup>41</sup> Friedman termed this situation the problem of “neighborhood effects,” which he claimed arose “when actions of individuals have effects on other individuals for which it is not feasible to charge or recompense them.”<sup>42</sup>

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*in the Pocket of the Private Prison Industry*, THE NATION, Feb. 27, 2013, <http://www.thenation.com/article/173122/what-does-millions-lobbying-money-buy-five-congresspeople-pocket-private-prison-indus#>.

37. *See id.*

38. Abraham Lustgarten, *After a Powerful Lobbyist Intervenes, EPA Reverses Stance on Polluting Texas County’s Water*, PROPUBLICA (Mar. 13, 2013, 5:00 AM), <http://www.propublica.org/article/after-a-powerful-lobbyist-intervenes-epa-reverses-stance-on-polluting-texas>.

39. *See id.* It is, of course, possible that the EPA was going to reverse itself anyway and issue the permit, but the exercise of such influence would be problematic. It does not matter whether influence is exerted by those on the political right or left (as in the case of Uranium Energy Corp.). It undermines government’s credibility and the likelihood that it will be able to fulfill its role, consistent with principles of liberalism, to prevent neighborhood effect and coercion in environmental and pollution matters.

40. FRIEDMAN, *supra* note 8, at 28. Government should set the rules of the game, “prevent coercion of one individual by another, . . . enforce[] . . . contracts voluntarily entered into, [and define] property rights, [as well as] interpret[] and enforce[] . . . such rights.” *Id.* at 27.

41. *See HAYEK, supra* note 9, at 87.

42. FRIEDMAN, *supra* note 8, at 30. Like Hayek, Friedman also identified “monopoly and similar market imperfections” as the other instances where government intervention in the economy is necessary. *See id.* at 28.

Environmental issues are paradigmatic here, as Friedman noted:

An obvious example is the pollution of a stream. The man who pollutes a stream is in effect forcing others to exchange good water for bad. These others might be willing to make the exchange at a price. But it is not feasible for them, acting individually, to avoid the exchange or to enforce appropriate compensation.<sup>43</sup>

Similarly, Hayek reasoned that “[t]o prohibit the use of certain poisonous substances or to require special precautions in their use . . . is fully compatible with the preservation of competition.”<sup>44</sup> Hayek further reasoned that

the price system becomes . . . ineffective when the damage caused to others by certain uses of property cannot be effectively charged to the owner of that property. . . . Nor can certain harmful effects of deforestation, of some methods of farming, or of the smoke and noise of factories be confined to the owner of the property in question or to those who are willing to submit to the damage for an agreed compensation.<sup>45</sup>

Accordingly, liberalism accepts that where competition produces “effects on other individuals for which it is not feasible to charge or recompense them”<sup>46</sup> or there is “a divergence between the items which enter into private calculation and those which affect social welfare . . . some method other than competition may have to be found to supply the services in question.”<sup>47</sup> Addressing those situations is a proper role of government with which corporate political spending may interfere.<sup>48</sup> Such interference will have improper coercive effects because some people will be forced to exchange clean air, clean water, or unpolluted land for polluted air, water, or land.<sup>49</sup>

*B. Corporate Political Spending Is Inconsistent with Liberalism Because It Weakens the Checks and Balances that the Separation of Political and Economic Power Places on Political Authority*

Whereas the problem of too much business involvement in government was discussed above in section A, I now turn to the problem of too much

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43. *Id.* at 30.

44. HAYEK, *supra* note 9, at 86. Hayek goes on and states that “[t]he only question here is whether in the particular instance the advantages gained are greater than the social costs which they impose.” *Id.* at 86-87

45. *Id.* at 87.

46. FRIEDMAN, *supra* note 8, at 30.

47. HAYEK, *supra* note 9, at 87.

48. *See* FRIEDMAN, *supra* note 8, at 27-28.

49. *See id.* at 30.

government in business.<sup>50</sup> The dominant way in which there is an improper intermingling of government and business affairs arises where businesses support the election of politicians by purchasing advertising or lobbying. The underlying goal of the support is to discourage politicians from exercising their proper role in setting the rules of the game or preventing neighborhood effects. However, there are other modes of intermingling that produce undesirable government intervention in business. For example, businesses may encourage government to pass inefficient protectionist or deregulation measures, and then expect government to bail them out when the lack of regulation leads to calamity (as with the repeal of the Glass-Steagall Act, which many believe contributed to the financial crisis).<sup>51</sup>

The exercise of corporate free speech rights in the United States furthers the convergence because it expands the ability of businesses to affect the decisions of government officials, and, consequently, expands the role of government in business.<sup>52</sup> Just as government has a role in checking the power of business where the market cannot properly operate, business has a role to play in checking the power of government, which is undermined by corporate political spending because it causes a convergence of the two.<sup>53</sup>

Hayek, in particular, warned of the risks societies take when they confer excessive economic power on political authorities.<sup>54</sup> Similarly, Galbraith observed a “convergence between the great bureaucratic organizations of capitalism and those of the socialist world.”<sup>55</sup> He argued the convergence arose from the growing similarities between government and corporate bureaucracies, and similar efforts of individuals within those bureaucracies to increase their power.<sup>56</sup> Friedman reasoned that the separation of political

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50. Compare FRIEDMAN, *supra* note 8, at 32 (“Every act of government intervention limits the area of individual freedom directly and threatens the preservation of freedom indirectly . . .”), and HAYEK, *supra* note 9, 79-80, with R. F. PETTIGREW, *IMPERIAL WASHINGTON* 9 (1922) (“[B]ankers, lawyers, manufacturers and business men . . . dominate the life and thought as well as the industries of these United States, and it is just such men that have been in control of the United States.”).

51. See Milton Friedman, *Government Interference in the Free Market: Understanding the Significance of the Auto Bailout*, YOUTUBE (Dec. 28, 2009), <http://www.youtube.com/watch?v=j9CTo8aqYRE>. Friedman maintained that government should not bail out inefficient industries. Pursuant to principles of liberalism, an industry can properly seek deregulation, but if their business model proves to be unsuccessful, it cannot claim to be entitled to a bail out. See *id.*

52. See HENRY N. BUTLER & LARRY E. RIBSTEIN, *THE CORPORATION AND THE CONSTITUTION* 59-60 (1995).

53. Although the Supreme Court denied that there is a risk of corruption where money spent on political speech is independent of the candidate’s campaign, this position is not persuasive, particularly when the politician knows the donor well, even if the spending is not directed or controlled by them.

54. See HAYEK, *supra* note 9, at 112.

55. JOHN KENNETH GALBRAITH, *THE NEW INDUSTRIAL STATE* xli (4th ed., Princeton Univ. Press 2007) (1967). The question is whether such a convergence of government and business is consistent with how people define social welfare. It does not take into account what is best for business or for government, nor what is consistent with the contract or regulatory theory of the firm.

56. The convergence of business and government is of concern to the individual. As Galbraith further

power from economic power serves as a check on both, and should be maintained. He wrote that:

The fundamental threat to freedom is power to coerce, be it in the hands of a monarch, a dictator, an oligarchy, or a momentary majority. The preservation of freedom requires the elimination of such concentration of power to the fullest possible extent and the dispersal and distribution of whatever power cannot be eliminated—a *system of checks and balances*. By removing the organization of economic activity from the control of political authority, the market eliminates this source of coercive power. It enables economic strength to be a check to political power rather than a reinforcement.

. . . [I]f economic power is joined to political power, concentration seems almost inevitable. On the other hand, if economic power is kept in separate hands from political power, it can serve as a check and a counter to political power.<sup>57</sup>

Accordingly, consistent with liberalism, businesses should not seek governmental intervention—except to the extent that they seek to exclude government from business and assume the risk of such actions—because doing so interferes with the freedom of businesses to independently order their affairs, and, as set forth above, the government’s ability to fairly set and mediate the rules of the game.

*C. Corporate Political Spending May Be Inconsistent with the Property Rights of Shareholders and the Contractual Theory of the Firm*

Managerial decisions that are contrary to the interests of shareholders are inconsistent with the contractual theory of the firm. According to this theory, the relationship between the corporation and its shareholders consists of a collection of contractual relationships, the terms of which the parties may freely alter. As Henry Butler explained,

argued,

[The focus of the] corporate bureaucrat[,] . . . in the presumed manner of all bureaucrats, [is on] . . . size, power, and influence . . . [and they] will have concern for their . . . power within the bureaucratic structure. As it must be believed that power is a goal for the individual, so, plausibly, it must be a goal for the organization. . . . In the large corporation the rules of bureaucratic aspiration and behavior clearly invade and partly replace those of profit motivation [as a driver for human action].

GALBRAITH, *supra* note 55, at xl-xli. As Bruce Caldwell wrote of F.A. Hayek’s warning about the use of war as a means to gain power: “No matter what rhetoric they employ, politicians and the bureaucracies over which they preside love power, and power is never easily surrendered once the danger, if there ever was one, has passed.” Bruce Caldwell, *Introduction to THE ROAD TO SERFDOM*, *supra* note 9, at 1, 32.

57. FRIEDMAN, *supra* note 8, at 15-16 (emphasis added).

The contractual theory views the corporation as founded in private contract, where the role of the state is limited to enforcing contracts. In this regard, a state charter merely recognizes the existence of a “nexus of contracts” called a corporation. Each contract in the “nexus of contracts” warrants the same legal and constitutional protections as other legally enforceable contracts. Moreover, freedom of contract requires that parties to the “nexus of contracts” must be allowed to structure their relations as they desire.<sup>58</sup>

Butler and Ribstein argue that the propriety of restrictions on corporate speech depends upon the nature of the restriction and the entity doing the restricting.<sup>59</sup> They maintain that restrictions that arise out of the contractual theory of the firm are permissible, but those that arise out of the regulatory theory of the firm are not.<sup>60</sup> They explain, “[m]anagers’ use of corporate assets to support political causes that they favor but that are inconsistent with shareholder interests, for example, does not differ significantly from any other type of managerial misbehavior.”<sup>61</sup> In such instances, consistent with the contractual theory of the firm, state law provides shareholders with the power to constrain managerial spending by requiring that managers disclose expenditures, or by prohibiting certain expenditures altogether.<sup>62</sup>

For Friedman, “[t]he corporation is an instrument of the stockholders who own it.”<sup>63</sup> That is so because “[i]f the corporation makes a [charitable] contribution, it prevents the individual stockholder from himself deciding how he should dispose of his funds.”<sup>64</sup> The same reasoning applies when a corporation makes political contributions, with which its shareholder may agree or disagree. In spending the money for those purposes, the corporation takes the shareholders money and makes ideological choices for the shareholder without his or her consent. Compounding the problem, a corporation may make a donation to a trade association or a charitable organization, and these entities are not required to disclose what they do with the funds. As such, management itself will lack knowledge about how the third party will eventually spend the money, and it thereby abandons further control over what shareholders may view as their money.<sup>65</sup>

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58. Henry N. Butler, *The Contractual Theory of the Corporation*, 11 GEO. MASON L. REV., Summer 1989, at 99, 100 (footnote omitted).

59. See BUTLER & RIBSTEIN, *supra* note 52, at 59-60.

60. See *id.* The regulatory theory of the firm is based on the idea that corporations are entities the state creates and may regulate. See *id.*

61. *Id.*

62. See *id.*

63. FRIEDMAN, *supra* note 8, at 135.

64. *Id.*

65. See Bruce F. Freed & Karl J. Sandstrom, *Dangerous Terrain*, CONF. BOARD REV., Winter 2012, at 21, 22, available at <http://politicalaccountability.net/index.php?ht=a/GetDocumentAction/i/6057>.

A contributor's own goals and intentions can be easily ignored. Lacking basic internal controls and external accountability, the groups spend as they please. And if that spending generates scandal—all too possible—a company giving money can find itself mired in controversy and, as a passive contributor, unable to control the narrative.<sup>66</sup>

As a result, Butler and Ribstein maintain that it would be permissible for the corporation to “adopt default rules provided by state corporate codes that are intended to minimize agency costs by directly controlling managerial misuse of corporate assets, or by increasing the shareholders’ voice in corporate affairs.”<sup>67</sup> Although the adoption of such codes would restrict free speech rights of the corporation, the fact that the corporation chooses its state of incorporation and the applicable law allows for the rules to be tested by the market.<sup>68</sup> Consistent with the contract theory of the firm, there is no risk of coercion because businesses will only select the rules in which the benefits exceed the costs.<sup>69</sup>

*D. Corporate Political Spending Is Inconsistent with Liberalism Because It Reduces the Ability of Individuals To Counter Special Interests, To Be Well Informed, and To Create a Society Consistent with Individual Liberty*

Although we have a system of majority rule, except with respect to certain essential rights, government is more responsive to special interest groups.<sup>70</sup> This is largely because special interest groups make their wishes clear to government, and unless the proposal is onerous or prohibitively expensive, other individuals or groups do not care enough to act against them.<sup>71</sup> Special interest groups have an incentive to “mount a propaganda barrage to assure that the majority are not well informed, and their task is easier than that of their opponents. They have visible, immediate effects to portray; their opponents, indirect delayed effects.”<sup>72</sup> Friedman expressed confidence that once the American people understood the problem (and he was referring to the

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66. *Id.*

67. BUTLER & RIBSTEIN, *supra* note 52, at 60.

68. *See id.*

69. *See id.* at 60. Butler and Ribstein oppose legislative restrictions on corporate free speech rights, which they maintain are based on the “regulatory theory of the corporation.” *Id.* at 59. The contractual theory of the corporation starkly contrasts the legal concept of the corporation as a state-created entity. The entity theory of the corporation supports state intervention—in the form of either direct regulation or the facilitation of shareholder litigation—on the grounds that the state created the corporation by giving it a charter. Butler and Ribstein view such regulations as improper because the market does not test their efficiency, and because they view such rules as being improperly justified by the government’s desire to control businesses. *See id.*

70. *See* MILTON FRIEDMAN & ROSE FRIEDMAN, TYRANNY OF THE STATUS QUO 6-7 (1984).

71. *See id.* (describing apathetic citizenry).

72. *Id.* at 7.

involvement of government in business affairs), “they [would] be able to control their government.”<sup>73</sup>

With respect to political spending, as high-net-worth individuals, corporations, and unions use their free speech rights to present facts in the light that favors their interests it becomes more difficult for citizens to ascertain the truth. Hundreds of thousands of dollars spent on negative advertising can go a long way in painting a picture of candidates for local, state, and federal office.<sup>74</sup> Like liberalism’s concern with the size of government, the ability of government to set the rules of the game requires an ability to consider society’s collective interests. When corporations, unions, and high-net-worth individuals seek special favors through government, their actions are akin to special interests that do not necessarily consider what is best for society or the individual. Given the limited ability of government to address society’s collective interests, corporate political spending may lead to the creation of rules that are more consistent with special interests rather than individual interests, which is contrary to the principles of liberalism.<sup>75</sup>

### III. A POTENTIAL CORPORATE DEMURRER, AND A RESPONSE

I now address a potential demurrer from corporate managers. As noted above, some corporate managers may respond to the foregoing arguments with a question: “Why should we care if corporate political spending is inconsistent with liberalism if it seems to be in our interests?” The answer lies in challenging the objection’s factual predicate—corporate political spending is in the company’s best interests. In fact, a long-range view of the corporation’s interests strongly suggests just the opposite.

One way to demonstrate that corporate political spending may not be in the best interests of corporations is to examine the actual decisions of for-profit corporations in our capitalist society. That is, if corporations declined to make independent political expenditures, it would be an indication that the managers believed there were better uses for corporate funds. For example, four companies, IBM, Colgate-Palmolive Company, Goldman Sachs Group, Inc., and Praxair Technologies, Inc., “do not spend from their corporate treasuries to influence elections, and they ask trade associations not to use their payments for political purposes.”<sup>76</sup>

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73. *Id.* at 10.

74. For example, the swift boat advertisements had a hugely negative effect on John Kerry’s candidacy. See Swift Boat Veterans for Truth, *Swiftboat Veterans Ad on John Kerry—Sellout (2004)*, YOUTUBE (Nov. 8, 2006), <http://www.youtube.com/watch?v=phqOuEhg9yE>.

75. See FRIEDMAN & FRIEDMAN, *supra* note 70, at 165-66. Friedman maintained that only the office of the President and the ratification of a constitutional amendment have the ability to focus on the majority’s interests over special or regional interests. See *id.* at 166.

76. CTR. FOR POLITICAL ACCOUNTABILITY, THE 2012 CPA-ZICKLIN INDEX OF CORPORATE POLITICAL ACCOUNTABILITY AND DISCLOSURE: HOW LEADING COMPANIES NAVIGATE POLITICAL SPENDING IN THE WAKE



Additionally, although the following corporations use employee-funded political action committees to make political expenditures, they do not use corporate funds to do so: Accenture Public Limited Company, Air Products and Chemicals, BB&T Corporation, Dell Inc., and Illinois Tool Works.<sup>77</sup> If corporate political spending for the purposes of influencing elections were a powerful force driving corporate profits, these corporations would likely be using corporate funds for that purpose.

Some research suggests, at least during the period from 1991 to 2004,

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OF *CITIZENS UNITED* 15 (2012), available at <http://politicalaccountability.net/index.php?ht=a/GetDocumentAction/i/6903>. Colgate has a policy prohibiting the use of corporate funds for campaign contributions, as do Goldman Sachs, IBM, and Praxair Technologies, Inc. See, e.g., *Colgate Policy*, *supra* note 14; *Goldman Sachs Statement on Policy Engagement and Political Participation*, GOLDMAN SACHS (Aug. 2013), <http://www.goldmansachs.com/investor-relations/corporate-governance/corporate-governance-documents/political-statement-8-9-13.pdf> [hereinafter *Goldman Sachs Policy*]; *Political Contributions and Employee Participation in Politics*, IBM, <http://www.ibm.com/ibm/responsibility/policy5.shtml> (last visited Feb. 15, 2014) [hereinafter *IBM Policy*]; *Government Affairs: Corporate Contributions*, PRAXAIR, <http://www.praxair.com/our-company/corporate-responsibility/government-affairs> (last visited Feb. 15, 2014) [hereinafter *Praxair Policy*].

Colgate has a long standing policy against making contributions to political parties or candidates. . . . These policies prohibit contributions to any political party or candidate. . . . This prohibition covers not only direct contributions but also indirect assistance or support through buying tickets to political fundraising events or furnishing goods, services or equipment for political fundraising or other campaign purposes.

*Colgate Policy*, *supra* note 14.

Goldman Sachs does not make any political contributions in the United States from corporate funds, including contributions to so-called Section 527 entities or independent expenditure political action committees (Super PACs). We have also voluntarily elected not to spend corporate funds directly on independent expenditures, including electioneering communications, despite the Supreme Court's decision in *Citizens United* entitling corporations to make such expenditures.

*Goldman Policy*, *supra*, at 1.

It is IBM's long-standing policy that we participate in politics as private citizens, not as IBMers. Therefore, it is the policy of the IBM Company not to make contributions of resources such as money, goods or services to political candidates or parties. This policy applies equally in all countries where IBM does business, regardless of whether or not such contributions are considered legal in any host country.

*IBM Policy*, *supra*.

Praxair, Inc. and its affiliates do not make corporate contributions to state or local political parties or candidates for public office, political parties, committees, PACs, ballot initiative campaigns, or to organizations organized under Section 527 of the Internal Revenue Code, even where permitted by applicable law. In addition, Praxair does not use corporate funds to make any direct independent expenditures on behalf of candidates running for local, state, or federal office.

*Praxair Policy*, *supra*.

77. See CTR. FOR POLITICAL ACCOUNTABILITY, *supra* note 76, at 16.

corporate political spending was not widespread. Using data from the Center for Responsive Politics from 1991 to 2004, Aggarwal, Meschke, and Wang found that although other corporations may not have had a policy against making independent political expenditures, most followed that policy in practice.<sup>78</sup> Their analysis “focus[ed] . . . on donations made directly from corporate funds—soft money donations and donations to 527 Committees. [They found that during the 1991 to 2004 time period] [o]f all the publicly-traded firms, only 11.27% or 1,381 firms donated directly from corporate funds.”<sup>79</sup> Stated affirmatively, “89% of the publicly traded firms in the US [made] no political donations out of corporate funds at all during [1991 to 2004].”<sup>80</sup> In the wake of the Supreme Court’s 2010 *Citizens United* decision, it appears that the amount of corporate spending increased dramatically, but the fact that a relatively small percentage of corporations decided to use their funds for political purposes from 1991 to 2004 supports the argument that those corporations believed—at least at that time—that there were better uses for those funds.<sup>81</sup>

Following the Aggarwal, Meschke and Wang study, John Coates analyzed data before and after the 2010 *Citizens United* decision, and found it was far from clear that corporate political expenditures added shareholder value. In fact, he concluded for most industries corporate political expenditures correlate negatively with shareholder value. He wrote:

[I]n industries that are not heavily regulated or government dependent, political activity is associated with weaker shareholder power, greater signs of managerial agency costs, and lower corporate value. The value-politics relationship is strongest for firms making large capital expenditures, suggesting one channel through which politics may lead to value-destroying investments. The precise extent and means by which politics may induce poor performance remains a topic for future research, but at a minimum the findings here reinforce the case that shareholders have a legitimate interest in obtaining better information about corporate politics.<sup>82</sup>

Accordingly, the argument that corporations should engage in independent political expenditures because it works is not as clear as one might otherwise

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78. See Rajesh K. Aggarwal et al., *Corporate Political Contributions: Investment or Agency?* 3-5 (Apr. 5, 2012) (unpublished manuscript), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=972670](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=972670).

79. *Id.* at 3.

80. *Id.* at 27.

81. See CTR. FOR POLITICAL ACCOUNTABILITY, *supra* note 76, at 16.

82. John C. Coates IV, *Corporate Politics, Governance, and Value Before and After Citizens United*, 9 J. EMPIRICAL LEGAL STUD. 657, 690-91 (2012). For those industries that were heavily regulated, Coates found that “political activity . . . does not strongly correlate with measures of shareholder power, managerial agency costs, or value.” *Id.* at 658.

suspect.

Consistent with this view, shareholders appear to be deeply concerned about corporate political spending, particularly undisclosed spending. The New York State Common Retirement Fund, for example, recently submitted shareholder proposals to several corporations that successfully led to agreements by those corporations to disclose their political expenditures.<sup>83</sup> Specifically, in response to the efforts of the Retirement Fund, Southwest Airlines, Dr Pepper Snapple Group, Plum Creek Timber Co., Harley-Davidson Inc. and Nobel Energy Inc. agreed “to make public all direct and indirect monetary and non-monetary political contributions, including contributions to trade associations that are used for political purposes.”<sup>84</sup> Pressed by shareholder proposals, the number of corporations making their independent political expenditures public is expanding dramatically.<sup>85</sup>

Similarly, as a result of a petition filed, the SEC is accepting comments on a proposal for rulemaking that would require public corporations to disclose their independent political expenditures.<sup>86</sup> The petition has received thousands of

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83. See Barry B. Burr, *5 Companies Agree To Disclose Political Spending After Prodding from DiNapoli*, PENSIONS & INVESTMENTS (Apr. 9, 2013, 3:52 PM), [http://www.pionline.com/article/20130409/ONLINE/130409878?utm\\_campaign=saxo\\_rss&utm\\_source=rss02\\_rss&utm\\_medium=rss](http://www.pionline.com/article/20130409/ONLINE/130409878?utm_campaign=saxo_rss&utm_source=rss02_rss&utm_medium=rss).

84. *Id.*

85. See CTR. FOR POLITICAL ACCOUNTABILITY, *supra* note 76, at 10. The Center for Political Accountability reported that many corporations are becoming more open about their political spending. They found that “[i]n 2012, 61 companies (69 percent) disclosed some information about their direct contributions to candidates and political parties, while 12 companies (14 percent) said they don’t give any money to them. In 2011, 52 companies (59 percent) disclosed some information and the same 12 companies refrained from giving.” *Id.* Similarly, with respect to trade association, the study found that

[i]n 2012, 45 companies (51 percent) disclosed some information on their payments to trade associations, while nine companies (10 percent) said that they ask trade associations not to use their payments for political purposes. In 2011, 36 companies (41 percent) disclosed some information and four (5 percent) placed similar restrictions.

*Id.* Finally, when looking at independent expenditures the study found that “[i]n 2012, 24 companies (27 percent) disclosed some information about their independent expenditures, while 40 (45 percent) said they wouldn’t engage in such spending. In 2011, 11 companies (13 percent) disclosed this information while 20 (23 percent) said they wouldn’t engage in the spending.” *Id.*

86. See Petition from Comm. on Disclosure of Corporate Political Spending to Elizabeth M. Murphy, Sec’y, Sec. & Exch. Comm’n (Aug. 3, 2011), available at <http://sec.gov/rules/petitions/2011/petn4-637.pdf>; *Comments on Rulemaking Petition: Petition To Require Public Companies To Disclose to Shareholders the Use of Corporate Resources for Political Activities*, U.S. SEC. & EXCHANGE COMMISSION, <http://www.sec.gov/comments/4-637/4-637.shtml> (last visited Feb. 15, 2014) [hereinafter *Comments on Rulemaking Petition*]. Although it appears that the vast majority of comments are in favor of disclosure, the SEC is facing significant political pressure to back off of the issue. See Dina ElBoghdady, *SEC Pressed To Abandon Corporate Political Spending Disclosures Petition*, WASH. POST, May 16, 2013, [http://articles.washingtonpost.com/2013-05-16/business/39310145\\_1\\_sec-rulemaking-white-house-petition](http://articles.washingtonpost.com/2013-05-16/business/39310145_1_sec-rulemaking-white-house-petition). ElBoghdady’s article observed the following:

The [law] professors who submitted the petition have noted that they did not agree on whether corporate political spending helped or hurt shareholders, but they all shared the view that public companies should not have free reign to spend their shareholders’ money on political communication

comments, the vast majority of them favorable.<sup>87</sup> Based on the comments, shareholders were motivated at least in part by a concern that corporate political expenditures may not be in the best interests of shareholders.<sup>88</sup> Indeed, there is evidence that corporate political expenditures may favor the interests of the corporate managers who may wish to curry favor with government officials so as to procure future positions in government.<sup>89</sup>

There is also the problem of corporate political expenditures supporting candidates who hold positions that are inconsistent with company policies. For example, some candidates oppose gay marriage, while the corporation maintains a nondiscrimination policy.<sup>90</sup> Certainly, the use of corporate political expenditures to influence the election of candidates who may favor some laws that are consistent with shareholder interests, and other rules that are not, come with reputational risks that most corporations endeavor to avoid.

In the few instances where corporate political spending may result in short-term gains, the longer-term damage far outweighs those gains. Damage to the government's ability to set the rules of the game, potential risks to corporate reputation, backlash from shareholders, and the likelihood that the money could be spent to increase profits by making better quality products or offering superior, less expensive services all outweigh any short-term gain from political expenditures.

In sum, it is not at all clear that corporate political expenditures make the best (that is, most profitable) use of corporate funds. As such, the prudent corporation has self-interested reasons to forbear from corporate political spending.

#### IV. SEEKING A SOLUTION

Corporations have free speech rights. The question is how will corporate managers choose to exercise those rights? It may be that the best course is for corporations to unilaterally decline to make independent political expenditures, as several major corporations have done. Applying John Nash's equilibrium concept, if no one made independent political expenditures, it would not be

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without revealing what they're doing.

*Id.*

87. See *Comments on Rulemaking Petition*, *supra* note 86.

88. See *supra* note 86 and accompanying text (discussing concern of shareholders relating to corporate political spending).

89. See Coates, *supra* note 82, at 658.

90. For example, Target's contribution to a trade association supporting Minnesota Forward, an advocacy group that supported a candidate who opposed gay marriage, contravened Target's other policies. See Jay Weiner, *In the Bull's-Eye: How Target—and Minnesota—Landed at Ground Zero of an Expensive U.S. Debate*, MINN. POST, Aug. 5, 2010, <http://www.minnpost.com/politics-policy/2010/08/bulls-eye-how-target-and-minnesota-landed-ground-zero-expensive-us-debate>.

necessary for anyone to do so, and all would avoid the expense.<sup>91</sup> The United States has a market for the services and favors of government. Demand for government services and favors may be legally manipulated. Businesses have yet to recognize—or have at least been unable to act consistently with the recognition—that they are generating demand and are thereby drastically increasing the cost of government services that would otherwise be provided without cost. It is true that corporations may have to give up certain perceived benefits such as protectionist legislation, barriers to entry, or other preferential treatment that government currently provides, but liberalism rejects government intervention in such matters on grounds of efficiency and avoidance of coercion.<sup>92</sup> Consistent with liberal thought, a corporation should cease making corporate political expenditures particularly if others would agree to take similar action.

One problem is that corporations are not the only ones who make political expenditures. Other groups, such as labor unions, demand action that could harm corporate interests. A potential solution would be to include unions and other groups in the agreements. Enforcement and compliance regimens, and the scope of agreements, would have to be devised and considered. If, for example, all automobile manufacturers and labor unions for their employees agreed not to make contributions to political campaigns, all might avoid significant expenses and, in exchange, receive a government better able to properly set the rules of the game. Where a party to such an agreement wished to make a political expenditure, the agreement might provide that it must first be vetted by an independent committee with equal numbers of labor and industry members. Expenditures would only be permissible if a majority agreed its purpose did not bear upon an issue concerning the relationship of the parties. The presumption would, therefore, be against allowing the expenditure. Where one party breached the agreement, the others could seek damages from that party in an amount necessary to counter the initial advertisement.

Scherer and Palazzo provide a model for such an arrangement that avoids the need to rely upon government to address issues that may be dealt with privately.<sup>93</sup> Where government cannot act or will not do so, there are opportunities for corporations to set rules for behavior, a practice which is

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91. See generally John F. Nash, Jr., *Equilibrium Points in N-Person Games*, 36 PROC. NAT'L ACAD. SCI. 48 (1949); John Nash, *Non-Cooperative Games*, 54 ANNALS OF MATHEMATICS 286 (1951); John F. Nash, Jr., *The Bargaining Problem*, 18 ECONOMETRICA 155 (1950); John Nash, *Two-Person Cooperative Games*, 21 ECONOMETRICA 128 (1953).

92. See Lubin, *supra* note 35 (identifying U.S. tariffs).

93. See Scherer & Palazzo, *supra* note 13, at 1107. The reason why government does not or cannot act does not bear on this analysis. That is, government may not be able to act because corporations and others have helped to create a political situation where it is impossible to do so. Whether one believes that this is right or wrong depends on one's perspectives and philosophies. The point here is that in the absence of government power, corporations may come together to fill the void.

consistent with liberalism.<sup>94</sup> There is such a gap in the market for government services because it is now unconstitutional for government to regulate this type of speech. A recent example of corporate collective action in the absence of government power to legislate involved two agreements concerning labor conditions in Bangladesh, one among mostly European retailers<sup>95</sup> and the other among U.S. retailers.<sup>96</sup> Although some have criticized the American Agreement for not committing to finance improvements beyond offering loans, the parties agreed to inspect premises, share information, and maintain hotlines for workers to report problems.<sup>97</sup> Under the American Agreement, when a retailer learns of a problem, it is to report the problem to the relevant manufacturers, plant owners, and/or the Bangladeshi government.<sup>98</sup> It is then up to those entities to decide what to do.<sup>99</sup> If they fail to address the situation to the satisfaction of the U.S. retailer, the retailer may stop placing orders with that company. Accordingly, without government intervention, the American Agreement places responsibility for working conditions on the manufacturer, and does not undertake to finance the repairs. Such a result is more consistent with liberalism than government intervention.<sup>100</sup>

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94. See Scherer & Palazzo, *supra* note 13, at 1107. Indeed, self-regulation is consistent with libertarian perspectives and the views of those who may not acknowledge a permissible role of government in business.

95. A few U.S. retailers did sign on to the European plan.

96. Compare *Accord on Fire and Building Safety in Bangladesh* (May 13, 2013), [http://www.industrialunion.org/sites/default/files/uploads/documents/2013-05-13\\_-\\_accord\\_on\\_fire\\_and\\_building\\_safety\\_in\\_bangladesh\\_0.pdf](http://www.industrialunion.org/sites/default/files/uploads/documents/2013-05-13_-_accord_on_fire_and_building_safety_in_bangladesh_0.pdf) [hereinafter *European Agreement*] (describing terms of European-led agreement), with Press Release, Alliance for Bangl. Worker Safety, *Alliance of Leading Retailers in North America Join Forces in Comprehensive, Five-Year Commitment To Improve Factory Safety Conditions for Workers in Bangladesh* (July 10, 2013), [http://az204679.vo.msecnd.net/media/documents/bangladesh-alliance-press-release\\_130179348070616796.pdf](http://az204679.vo.msecnd.net/media/documents/bangladesh-alliance-press-release_130179348070616796.pdf) [hereinafter *American Agreement*] (outlining American-led agreement). For an article outlining the differences between the two plans, see Steven Greenhouse & Stephanie Clifford, *U.S. Retailers Offer Plan for Safety at Factories*, N.Y. TIMES, July 10, 2013, [http://www.nytimes.com/2013/07/11/business/global/us-retailers-offer-safety-plan-for-bangladeshi-factories.html?\\_r=0](http://www.nytimes.com/2013/07/11/business/global/us-retailers-offer-safety-plan-for-bangladeshi-factories.html?_r=0). Some U.S. retailers reported that they were unwilling to join the European Agreement because of U.S. laws that purportedly could have made them responsible for unlimited liability. If that were true, and there are reasons to suspect that it is not (considering some U.S. retailers signed on to the European Agreement) the garment agreement would be an example of a law created by a government that actually interfered with businesses reaching agreements to help address an important business and labor issue. Given that tort liability is based on a duty of care, which includes a knowledge component, as a result of inspections U.S. companies will have difficulty claiming that they were unaware of conditions, or that their products were being produced at a given location. Accordingly, the American Agreement could increase the liability of retailers who continue to do business with Bangladeshi manufacturers that do not maintain safe conditions.

97. See *American Agreement*, *supra* note 96.

98. The Agreement could result in the Bangladeshi government exercising additional authority over factories within its jurisdiction.

99. For those concerned with the welfare of workers in Bangladesh, the plan may not go far enough, but the market may solve the problem if U.S. retailers actually require their manufacturers to meet appropriate safety standards. The question is whether manufacturers will finance the changes by increasing the fee they charge U.S. manufacturers to comply with their safety standards, or avoid this extra cost by reducing employee pay.

100. For the free market economist, the best result may be for market forces to address the labor conditions of Bangladeshi workers, without an agreement, and as workers earn more money they will

Where credibility is important, corporate managers may decide to work with nongovernmental organizations (NGOs) to develop industry agreements, and implement independent verification procedures (that is what European clothing manufacturers decided to do with respect to Bangladeshi manufacturers).<sup>101</sup> Another such example is the Forest Stewardship Council (FSC), which corporations and NGOs formed in connection with an agreement for the sustainable harvesting of forests.<sup>102</sup>

The FSC developed a set of principles and criteria for sustainable global forest management. . . . The General Assembly, as the highest decision-making body of the FSC, is organized into three membership chambers—environmental, social, and economic—for balancing the voting power of its diverse members. On the basis of its principles and criteria, the FSC has developed a certification for timber and timber products that is approved by independent bodies. The certification process itself contains rigorous standards and independent monitoring procedures, which lead to a broad acceptance of the council among critical civil society organizations.<sup>103</sup>

Rather than seek to exclude corporations from a political process that U.S. law now permits, the garment retailer agreements and the FSC provide examples of ways corporations may create binding agreements and develop consensual rules to govern their actions without coercion from the state, and without a need to influence government. A similar approach could work with respect to the

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eventually be able to trade money for safety. See Mario Rizzo, *F.A. Hayek: His 114th Birthday*, THINKMARKETS (May 8, 2013), <http://thinkmarkets.wordpress.com/2013/05/08/f-a-hayek-his-114th-birthday>. As the argument goes, and the one recently made by Mario Rizzo is emblematic (though he does recognize that the workers may not be fully aware of the risks), workers are purportedly choosing to work in dangerous factories because the other alternatives are worse, and there are substantial risks to living conditions that would result if Western retailers were pressured to leave. An agreement, of course, is more consistent with liberalism than a government crackdown or expanded liability laws. Although it does not bear upon the argument that liberalism is more consistent with corporate agreements than government regulation, I cannot pass without observing that I find the claim that the people of Bangladesh are freely choosing to work in dangerous factories a bit difficult to believe. If we are going to look at free choices, looking only at the “choices” of the workers does not reveal the true story. At some point it is also useful to examine the choices of those who profit at the expense of the lives of others. As Robert Gordon states well,

The claim . . . that workers in health-destroying factories voluntarily “choose,” in any practical sense of the term, the risks of the workplace in return for a wage premium, is probably not believed by anyone save those few expensively trained out of the capacity to recognize what is going on around them.

Robert W. Gordon, *Unfreezing Legal Reality: Critical Approaches to Law*, 15 FLA. ST. U. L. REV. 195, 199 (1987).

101. See *European Agreement*, *supra* note 96 (describing European Agreement as example of cooperation among industry, government, and NGOs).

102. See Scherer & Palazzo, *supra* note 13, at 1110.

103. *Id.*

market for government services.

Corporations could address many of the issues associated with corporate political spending by making voluntary disclosure of their political expenditures. Disclosure can, of course, be forced upon business through regulation, as the SEC is considering in the United States.<sup>104</sup> Such a rule would take the matter out of the control of managers, as well as shareholders. Voluntary disclosure may be an appropriate alternative approach. As noted above, according to the 2012 CPA-Zicklin Index of Corporate Political Activity, “[a]lmost 60 percent of companies in the top echelons of the S&P 500 are now disclosing some political spending information.”<sup>105</sup>

Disclosure has the advantage of being efficient. If corporate managers spend money in ways that shareholders are not aware of, it makes the markets less efficient and further separates ownership from control. The efficient capital markets hypothesis provides that “securities prices are efficient in that they accurately reflect all publicly available information about the security.”<sup>106</sup> When investors have full information about corporations they are able to accurately assess the value of their investments and make decisions as to when and whether to sell or buy stock.<sup>107</sup> Where information about a firm and its contracts are available to shareholders, “corporate contracts that harm investor interests will be recognized and punished by price reductions in the market.”<sup>108</sup> In that way, “incentives to maximize share value” (based on the risk that shareholders may sell) depend upon shareholders having information about the nature of the firm’s contracts. Where corporations can secretly contribute funds to finance independent political expenditures, the prices of the corporations’ stock may not accurately reflect their value, which is inefficient. Given that efficiency is the touchstone of free market theory, those in favor of it should not object to voluntary disclosure policies.

Before making independent political expenditures, corporate managers need to carefully consider whether they want to participate in the market for the services of government. It is certainly not clear that such participation is the best use of corporate profits. The best approach may be to act unilaterally or collectively to exchange a practice with questionable financial benefits for an effective government and efficient market.

## V. CONCLUSION

We should not misconstrue liberalism’s focus on individual political and economic freedom as providing a philosophical basis for demanding the

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104. See *supra* note 86 and accompanying text (discussing SEC disclosure petition).

105. CTR. FOR POLITICAL ACCOUNTABILITY, *supra* note 76, at 5.

106. Butler, *supra* note 58, at 106.

107. See *id.*

108. *Id.*



dismantlement of government in its entirety. It is true that the nineteenth-century philosophical liberal requires a smaller government than the current left-leaning liberal. Nevertheless, liberalism requires government to act where market forces cannot efficiently do so, and to set and maintain the rules of the economic game. Liberalism recognizes that there are costs whenever government issues rules, but it is a cost that liberalism balances against the intrusion and coercion of market failures and the need for the maintenance of efficient rules of the game.<sup>109</sup> Different people may draw the line in different places, but liberalism requires that the analysis be done, and action taken, where necessary, through “mutual coercion, mutually agreed upon by the majority of the people [or, if it must be, entities] affected.”<sup>110</sup> Whether the solution to problems associated with corporate political spending is found through the operation of the market, private agreements, government, or a combination of the three, it is unlikely to be found by vilifying those with whom we may otherwise disagree. You never know where you may find a friend.

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109. See FRIEDMAN, *supra* note 8, at 32.

Every act of government intervention limits the area of individual freedom directly and threatens the preservation of freedom indirectly . . . .

Our principles offer no hard and fast line how far it is appropriate to use government to accomplish jointly what it is difficult or impossible for us to accomplish separately through strictly voluntary exchange. In any particular case of proposed intervention, we must make up a balance sheet, listing separately the advantages and disadvantages. Our principles tell us what items to put on the one side and what items on the other and they give us some basis for attaching importance to the different items.

*Id.*

110. Hardin, *supra* note 1, at 1247.