

Brendan W. Donckers, Chair
Hardeep Singh Rekhi, Vice Chair
Seattle Ethics & Elections Commission
PO Box 94729
Seattle, Washington 98124-4729

RE: Political spending by foreign-influenced corporations
Limits on contributions to super PACs

August 5, 2019

Dear Chairman Donckers and Vice Chairman Rekhi,

I am the Legal Director of Free Speech For People, a national non-partisan non-profit organization with approximately 15,000 supporters in Seattle, that works to renew our democracy and to limit the influence of money in our elections. We were proud to help defend the Honest Elections Seattle Initiative by submitting an amicus brief in its support at the Washington Supreme Court in the recent case *Elster v. City of Seattle*.¹ I now write in support of a proposed ordinance that addresses political spending by foreign-influenced corporations, and contributions to independent expenditure PACs.

I. Political spending by foreign-influenced corporations

The 2016 election showed that foreign interference in our elections is a serious problem. The recent news that at least one Russian company bought political ads on Facebook shows one way that foreign interests can use corporations to influence elections. But Facebook is not the only way that foreign interests can use American companies to influence U.S. elections. This proposal would close a major loophole.

Under well-established federal law, upheld by the U.S. Supreme Court, it is illegal for a foreign government, business, or individual to spend

¹ See <https://freespeechforpeople.org/elster-v-city-of-seattle/>.

money to influence federal, state, or local elections.² However, *no* law prevents a foreign interest from using a U.S.-based corporation to accomplish the same goal, particularly since the U.S. Supreme Court’s 2010 *Citizens United* decision invalidated laws that banned corporate political spending.³

Citizens United created a loophole for foreign interests to acquire stakes in U.S. corporations, such as a company incorporated in Delaware, and then use that leverage to influence or control the corporation’s political activity, including both direct spending and contributions to super PACs. The Supreme Court indicated in *Citizens United* that it was aware of this problem and its decision would not prevent a law that was designed to address this problem,⁴ yet it has been now nine years and neither Congress nor the beleaguered Federal Election Commission have done anything. However, as explained in more detail in written testimony submitted by Professor Laurence Tribe of Harvard Law School, Seattle does not need to wait for federal action to protect its state and local elections from foreign influence. The 2016 election showed us that the threat of foreign influence in elections is real. These bills would plug the loophole that *Citizens United* created for corporations partly or wholly owned by foreign interests.

A. Constitutionality of Regulating Political Spending by Foreign-Influenced Entities

Commissioner (now Chair) Ellen Weintraub of the Federal Election Commission explained the issue in an op-ed in the New York Times: “Throughout *Citizens United*, the court described corporations as ‘associations of citizens,’ she wrote, “States can require entities accepting political contributions from corporations in state and local races to make sure that those corporations are indeed associations of American citizens—and enforce the ban on foreign political spending against those that are not.”⁵

² 52 U.S.C. § 30121; *Bluman v. Federal Election Comm’n*, 800 F. Supp. 2d 281, 288 (D.D.C. 2011), *aff’d*, 132 S. Ct. 1087 (2012); *United States v. Singh*, 924 F.3d 1030, 1042 (9th Cir. 2019).

³ *Citizens United v. Federal Election Comm’n*, 558 U.S. 310 (2010).

⁴ *See id.* at 362.

⁵ Ellen Weintraub, “Taking on Citizens United,” N.Y. Times, Mar. 30, 2016, <http://nyti.ms/1SwK4gK>.

The problem at issue in this loophole was identified by Justice Stevens in his dissent in *Citizens United* when he wrote, “Because [corporations] may be managed and controlled by nonresidents, their interests may conflict in fundamental respects with the interests of eligible voters.”⁶ This threat is not merely hypothetical. Uber has shown an increasing appetite for political spending in a variety of contexts.⁷ Although Uber started in Silicon Valley, the Saudi government now owns more than 10 percent of the company.⁸ In October 2016, Airbnb responded to the New York Legislature’s growing interest in regulating the homestay industry by arming a super PAC with \$10 million to influence New York’s legislative races.⁹ Airbnb is a privately held company, so ownership data is not complete, but it is partly owned by Moscow-based (and Kremlin-linked) DST Global.¹⁰ Investment by foreign sovereign wealth funds, like Saudi Arabia’s, is expected to increase exponentially as oil-rich Middle Eastern states seek to diversify their investment portfolios.¹¹

⁶ *Citizens United*, 558 U.S. 310, 394 (2010) (Stevens, J., dissenting).

⁷ Glenn Blain, “Uber spent more than \$1.2M on efforts to influence lawmakers in first half of 2017,” *New York Daily News*, Aug. 13, 2017, <http://www.nydailynews.com/news/national/uber-spent-1-2m-lobbying-efforts-2017-article-1.3408470>; Karen Weise, “This is How Uber Takes Over a City,” *Bloomberg*, June 23, 2015, <http://bloom.bg/1Ln2MaN>.

⁸ Eric Newcomer, “The Inside Story of How Uber Got Into Business with the Saudi Arabian Government,” Nov. 3, 2018, <https://www.bloomberg.com/news/articles/2018-11-03/the-inside-story-of-how-uber-got-into-business-with-the-saudi-arabian-government>.

⁹ Kenneth Lovett, *Airbnb to spend \$10M on Super PAC to fund pre-Election day ads*, *N.Y. Daily News*, Oct. 11, 2016, <http://nydn.us/2EF5Lgi>.

¹⁰ See Jon Swaine & Luke Harding, *Russia funded Facebook and Twitter investments through Kushner investor*, *The Guardian*, Nov. 5, 2017, <https://www.theguardian.com/news/2017/nov/05/russia-funded-facebook-twitter-investments-kushner-investor>; Dan Primack, *Yuri Milner adds \$1.7 billion to his VC war chest*, *FORTUNE*, Aug. 3, 2015, <http://fortune.com/2015/08/03/yuri-milner-adds-1-7-billion-to-his-vc-warchest/> (DST Global is Moscow based); Scott Austin, *Airbnb: From Y Combinator to \$112M Funding in Three Years*, *The Wall Street Journal*, July 25, 2011, <http://blogs.wsj.com/venturecapital/2011/07/25/airbnb-from-y-combinator-to-112m-funding-in-three-years/>. Reportedly, \$40 million of the \$112 million that Airbnb raised in its 2011 funding round came from DST Global. See Alexia Tsotsis, *Airbnb Bags \$112 Million In Series B From Andreessen, DST And General Catalyst*, *TechCrunch*, July 24, 2011, <http://tcrn.ch/2EF6IF2>. However, the calculation of DST Global’s ownership stake may be based on a valuation of \$1 billion or more; if so, DST Global’s \$40 million could represent 4%, not the 5% needed to qualify as a “foreign-influenced corporation.”

¹¹ According to one report, Saudi Arabia’s Public Investment Fund is expected to deploy \$170 billion in investments over the next three to four years. Sarah Algethami, “What’s Next for Saudi Arabia’s Sovereign Wealth Fund,” *Bloomberg BusinessWeek*, Oct. 21, 2018, <https://www.bloomberg.com/news/articles/2018-10-22/what-s-next-for-saudi-arabia-s-sovereign-wealth-fund-quicktake>.

As Professor Laurence Tribe of Harvard Law School and I explained in a joint op-ed in the Boston Globe, “while the Supreme Court was careful to note that its decision would not foreclose limits that apply specifically to corporations with significant foreign influence, Congress hasn’t updated the law since the *Citizens United* decision. Meanwhile, the Federal Election Commission, the agency in charge of interpreting and applying the law, has been stuck in stalemate.”¹² And as Commissioner Weintraub noted in the New York Times, even partial foreign ownership of corporations calls into question whether *Citizens United*, which three times described corporations as “associations of citizens” and which expressly reserved questions related to foreign shareholders,¹³ would apply. Indeed, after deciding *Citizens United*, the Supreme Court case of *Bluman v. Federal Election Commission* specifically upheld a ban on foreign nationals spending their *own* money in U.S. elections.¹⁴ In light of the Court’s post-*Citizens United* decision in *Bluman*, a restriction on political spending by corporations with foreign ownership at levels potentially capable of influencing corporate governance can be upheld on the authority of *Bluman* and as an exception to *Citizens United*.

B. Mechanics of Proposed Ordinance

The proposal would prohibit a foreign-influenced corporation from making an independent expenditure or contributing to an independent expenditure committee (often called a “super PAC”). It would also , and require any corporation making an independent expenditure or contributing to a super PAC to promptly file a statement of certification, signed by its chief executive officer under penalty of perjury, avowing that, after due inquiry, the corporation was not a foreign-influenced corporation when the expenditure or contribution was made.

¹² Laurence Tribe & Ron Fein, “How Massachusetts can fight foreign influence in our elections,” Boston Globe, Sept. 26, 2017, <https://www.bostonglobe.com/opinion/2017/09/26/how-massachusetts-can-fight-foreign-influence-our-elections/CM8rjPu8NtmRJIYRVeUVJM/story.html>.

¹³ *Citizens United*, 558 U.S. at 349, 354, 356, 362.

¹⁴ *Bluman v. Federal Election Comm’n*, 800 F. Supp. 2d 281, 288 (D.D.C. 2011), *aff’d*, 132 S. Ct. 1087 (2012).

The proposal does *not* regulate other forms of corporate political activity, such as lobbying or spending in ballot measure elections, nor does it in any way regulate the personal political activities or spending of the individual employees or stockholders of the company. Nor does it have any effect whatsoever on opportunities for political expression by individual foreign nationals. It simply prohibits use of *corporate treasury money* by foreign-influenced corporations to make independent expenditures or contributions to super PACs.

The term “foreign-influenced corporation” is defined via a three-layer definition. First, the term “foreign investor” is defined to mean a a foreign government, foreign company, or individual foreign national that owns stock in a company. Second, the term “foreign owner” is defined to mean either a foreign investor, *or* a company for which a foreign investor owns half or more of the shares. This latter part of the definition of “foreign owner” is intended to include a U.S.-registered company that is majority-owned or controlled by a foreign corporation or individual foreign investor, because many foreign entities invest in American companies through such subsidiaries. Finally, the term “foreign-influenced corporation” is defined to include a corporation, LLC, or similar business entity where either a single foreign owner owns 1% of shares, or multiple foreign owners own 5% of shares in the aggregate, or a foreign owner participates directly or indirectly in the corporation’s decision-making process with respect to the corporation’s political activities in the United States.

C. Foreign ownership thresholds

Foreign investment often outweighs local considerations, no matter how iconic the company is to its “hometown.” Even if a company was founded in the United States and keeps its main offices here, companies are responsive to their shareholders, and significant foreign ownership affects corporate decision-making.

The proposal’s thresholds of 1% for a single foreign owner, or 5% for multiple foreign owners, may appear low at first. However, as explained in some detail in written testimony submitted by Professor John Coates of Harvard Law School for a similar bill in Massachusetts, these

thresholds reflect levels of ownership that are widely agreed (including by entities such as the Business Roundtable) to be high enough to influence corporate governance.

For a large multinational corporation, an investor that owns 1% of shares might well be the largest single stockholder. The proposed 1% threshold is also grounded in current Securities and Exchange Commission requirements and thresholds for shareholder proposals.¹⁵ Of course, this does not mean that *every* investor who owns 1% of shares will *always* influence corporate governance, but rather that the business community generally recognizes that this level of ownership presents that opportunity, and—for a foreign investor in the context of corporate political spending—that risk.

In other cases, no single foreign investor holds 1% or more of corporate equity, but multiple foreign investors own a substantial aggregate stake. To pick one example, at the moment of this writing (it may change later, of course, due to market trades), Amazon does not have any 1% foreign investors, but at least 7.5% of its equity (and possibly much more) is owned by foreign investors.¹⁶ While presumably foreign investors as a class are not all perfectly aligned on all issues, they can be assumed to share certain common interests and positions that may, in some cases, differ from those of U.S. shareholders—certainly when it comes to matters of local Seattle public policy.

Neither corporate and securities law nor empirical research provide a bright-line threshold at which this type of aggregate foreign interest begins to affect corporate decision-making, but anecdotally it appears that CEOs do take note of this aggregate foreign ownership and that at a certain point it affects their decision-making. The proposed ordinance selects a 5% aggregate foreign ownership threshold. Under federal

¹⁵ Owning one percent of a company's shares allows an owner to submit shareholder proposals, which creates substantial leverage. See 17 C.F.R. 240.14a-8(b).

¹⁶ See *Amazon.com*, CNBC, <https://cnb.cx/2JShvAt> (visited Aug. 5, 2019) (ownership tab). As of the date of writing, two foreign investors (Baillie Gifford and Norges Bank) each hold 0.9% but no foreign investor holds 1.0% or more. Aggregate ownership data, however, shows 6.7% in Europe (including Russia) and 0.8% in Asia. In fact, the total aggregate foreign ownership may be as high as 40%, as the summary data show only 59.7% of shares owned in North America. CNBC obtains its geographic ownership concentration data from Thomson Reuters, which in turn obtains it from Refinitiv, a provider of financial markets data that has access to some non-public sources.

securities law, 5% is the threshold that Congress has already chosen as the level at which a single investor *or group of investors working together* can have an influence so significant that the law requires disclosure not only of the stake, but also the residence and citizenship of the investors, the source of the funds, and even in some cases information about the investors' associates.¹⁷ In this case, while it may not be appropriate to treat unrelated foreign investors as a single bloc for *all* purposes, it is appropriate to do so in the context of analyzing how they may influence decision-making regarding political spending in U.S. elections.

In Seattle, a number of companies would qualify as a “foreign-influenced corporations.” As noted above, this includes companies with local origins that keep their main offices here; it is important to be clear-eyed about the fact that corporate decision-making is responsive to the company’s actual current shareholders, wherever they are.

Of the 63 Washington-headquartered, NASDAQ-listed companies, 14 have foreign investors of more than 1 percent, and 10 of those companies are headquartered in the Seattle metropolitan area.¹⁸ These include well-known companies like T-Mobile,¹⁹ Zillow,²⁰ and Redfin.²¹ And of course others, such as Amazon (discussed above), exceed the 5% aggregate ownership thresholds. The point is not to criticize these particular corporations (there is nothing unlawful or improper *per se* with foreign investment), nor to state definitively that they would be subject to the proposed ordinance, but simply to note that their corporate decision-making, including around Seattle politics and elections, may be influenced by their increasingly international investors.

By the same token, some super PACs active in area elections have been substantially funded by foreign-influenced corporations. As an example,

¹⁷ 15 U.S.C. §§ 78m(d)(1)-(3).

¹⁸ This information comes from Marketscreener.com.

¹⁹ *T-Mobile US Inc*, CNN Business,

<https://money.cnn.com/quote/shareholders/shareholders.html?symb=TMUS&subView=institutional>.

Noway-based Norges Banks has a 1.15 percent ownership.

²⁰ *Zillow Group Inc*, Market Screener, <https://www.marketscreener.com/ZILLOW-GROUP-INC-20814107/company/>. Australian-based Caledonia Private Investments has a 26.8 percent ownership.

²¹ *Redfin Corp*, Market Screener, <https://www.marketscreener.com/REDFIN-CORP-37247408/company/>. U.K.-based Baillie Gifford & Co. has a 4.2 percent ownership.

consider the Olympia-based Leadership Council.²² This committee’s third-largest donor in 2017 (contributing \$165,000) was Virginia-based “Altria Client Services LLC.” Altria—a tobacco conglomerate formerly known as Philip Morris—is owned at least 7.9% by foreign investors.²³ As Altria seeks to grow and protect its increasingly multinational business, it is reasonable to note how far \$165,000 or more could go in Seattle elections.

By the same token, some companies will *not* have a foreign owner with 1% or more of shares, and even of those that do, many will not spend corporate money on Seattle elections either directly or via contributions to outside-spending entities which then spend the money on Seattle elections.²⁴ Such companies either would not be covered at all (if they did not meet the threshold) or would not experience any practical impact (if they do not spend corporate money for political purposes).

The point here is *not* that these corporations do not have connections to Seattle, nor that foreign investment in Seattle companies should be discouraged, nor that the foreign owners of these companies are necessarily known to be exerting influence over the companies’ decisions about corporate political spending, nor that they would do so nefariously to undermine democratic elections. Rather, the point is simply that *Citizens United* accorded corporations the right to spend money in our elections on the theory that corporations are “associations of citizens.” But for companies of this type, that theory does not apply. Enough shares are owned or controlled by a foreign owner that it could exert influence over how the corporation spends money from the corporate treasury to influence candidate elections. And to reiterate, the bill does not limit in any way how employees, executives, or shareholders of these companies may spend their *own* money—just how the foreign-influenced corporations’ potentially vast corporate treasuries may be deployed to influence Seattle electoral democracy.

²² *The Leadership Council*, PDC, 2017, https://www.pdc.wa.gov/browse/campaign-explorer/committee?filer_id=LEADC%20%20148&election_year=2017.

²³ *Altria Group Inc.*, CNBC, <https://cnb.cx/2KqU00p> (visited Aug. 5, 2019).

²⁴ We can only say they *appear* not to have spent money on state or local elections because many times, corporations route their political spending through layers of 501(c)(4) “dark money” groups for which no disclosure is presently required.

II. Limits on contributions to independent expenditure committees

Independent expenditure committees, also known as super PACs, are political committees that promise to make only independent expenditures. Under current law, there are *no* limits on contributions to these committees. This creates some unfortunate, illogical, and harmful effects. For example, it is illegal for a wealthy donor to contribute a penny more than \$500 to a candidate for mayor, city council, or city attorney, because the city council has determined that contributions above that amount pose an unacceptable risk of corruption or the appearance of corruption.²⁵ Yet that same wealthy donor may contribute \$5,000, or \$50,000, or even \$500,000, to the candidate's super PAC.

A. Constitutionality of Regulating Contributions to Super PACs

Some believe that the Supreme Court's decisions, including *Citizens United*, ban limits on contributions to independent expenditure PACs. But, as explained in more detail in written testimony submitted to the committee by Professor Laurence Tribe of Harvard Law School and Professor Albert Alschuler of the University of Chicago Law School, that is incorrect. It is true that some federal courts of appeals, including three-judge panels of the Ninth Circuit, have interpreted *Citizens United* to require this result, on the theory that contributions to independent expenditure committees cannot *possibly* cause corruption.²⁶ However, as Professors Tribe and Alschuler explain, the reasoning of those decisions is incorrect and should not be presumed to prevail at the U.S. Supreme Court—or even necessarily before the larger “en banc” Ninth Circuit.

Furthermore, since those early decisions, empirical evidence has mounted against the assumptions underlying that decision. For

²⁵ Seattle Muni. Code § 2.04.370(B).

²⁶ See *SpeechNow.org v. Fed. Election Comm'n*, 599 F.3d 686 (2010); *Thalheimer v. City of San Diego*, 645 F.3d 1109 (9th Cir. 2011); *Long Beach Area Chamber of Commerce v. City of Long Beach*, 603 F.3d 684 (9th Cir. 2010).

example, as explained in more detail in written testimony submitted to the committee by political scientist Stephen Weissman, the actual relationships between “independent” super PACs and their large donors provides ample opportunities for quid pro quo corruption.²⁷ Recent empirical research shows that, as one might expect, this also leads to the *appearance* of corruption.²⁸

B. Mechanics of Proposed Limit

This proposed ordinance imposes a contribution limit of \$5,000 from any individual to a super PAC. This is ten times Seattle’s limit on contributions to candidates, and over five times the statewide limit on contributions to candidates in city elections.²⁹ It is more than enough to enable contributors to support their favored candidates without posing an unacceptable risk of corruption.

Some super PACs that are active in Seattle city elections also spend elsewhere in Washington or the country, where laws differ. Such super PACs have two main options to comply with the ordinance. First, they could voluntarily limit *all* incoming contributions to \$5,000. While this would be laudable, it is not necessary for compliance and we do not expect many super PACs to pursue this option. Second, the super PAC could create a segregated account (perhaps via separate political committee) exclusively for use in Seattle city elections, and that account could accept limited contributions of no more than \$5,000. While some super PACs might complain that this is burdensome, a similar type of argument was rejected by the court in the recent case of *State v. Grocery*

²⁷ Indeed, a federal grand jury indicted a sitting U.S. Senator for bribery for a contribution to a super PAC, and a federal judge upheld the indictment as consistent with *Citizens United*, although the jury later deadlocked and the judge dismissed some of the charges for insufficient evidence. *See United States v. Menendez*, No. CR 15-155, 2018 WL 526746, at *9 (D.N.J. Jan. 24, 2018). Relatedly, in 2011 the U.S. Court of Appeals for the Eleventh Circuit upheld a bribery conviction against Alabama Governor Don Siegelman where the bribe in question was given to a charitable organization that engaged only in issue advocacy. *See United States v. Siegelman*, 640 F.3d 1159, 1175 (11th Cir. 2011). The fact that a federal court found quid pro quo corruption from a contribution to a group that spent only on issue advocacy is striking because courts consider issue advocacy to pose no greater (and probably less) risk of corruption than “independent” expenditures in candidate races.

²⁸ *See* Christopher Robertson et al., *The Appearance and the Reality of Quid Pro Quo Corruption: An Empirical Investigation*, 8 *Journal of Legal Analysis* 375 (Winter 2016), available at <https://academic.oup.com/jla/article/8/2/375/2502553>.

²⁹ *See* RCW § 42.17A.405(2).

Manufacturers Association,³⁰ in which the court had little sympathy for the argument that a major national corporate lobby was unduly burdened by needing to create a separate political committee for receiving and spending money intended for Washington state elections.

C. Super PACs in Seattle and in Washington

1. Super PAC spending in Washington federal elections

As background, it is worth noting that super PACs' independent expenditures have skyrocketed since 2010 and are only increasing. Nationwide, federal super PAC expenditures nearly doubled from 2012³¹ to 2016,³² with over \$1 billion spent in 2016 alone. In 2018, even without a presidential election, expenditures nearly reached 2016 levels, with over \$800 million spent,³³ more than double the amount spent in 2014.³⁴

This spending is generally highly concentrated. From 2012-18, the five highest-spending super PACs per election cycle on average made 50 percent of all expenditures, despite there being roughly 1800 super PACs per election.³⁵ Such concentration allows a handful of super PACs to have enormous and disproportionate influence on elections across the country.

³⁰ 5 Wash. App. 2d 169, 425 P.3d 927 (Wash. App. 2018), *review granted*, 193 Wash. 2d 1001 (Apr. 3, 2019).

³¹ *2012 Outside Spending, by Super PAC*, Open Secrets, <https://www.opensecrets.org/outsidespending/summ.php?cycle=2012&chrt=V&disp=O&type=S>. Super PACs spent \$609,936,792.

³² *2016 Outside Spending, by Super PAC*, Open Secrets, <https://www.opensecrets.org/outsidespending/summ.php?cycle=2016&chrt=V&disp=O&type=S>. Super PACs spent \$1,066,914,448.

³³ *2018 Outside Spending, by Super PAC*, Open Secrets, <https://www.opensecrets.org/outsidespending/summ.php?cycle=2018&chrt=V&disp=O&type=S>. Super PACs spent \$822,068,922.

³⁴ *2014 Outside Spending, by Super PAC*, Open Secrets, <https://www.opensecrets.org/outsidespending/summ.php?cycle=2014&chrt=V&disp=O&type=S>. Super PACs spent \$345,110,359.

³⁵ The total number of super PACs has drastically increased as well. In 2012, 1275 super PACs existed. In 2018, 2395.

Nationwide, in 2012 super PACs spent \$851,164 on House and Senate elections, with an average of \$85,116 spent per House seat.³⁶ In 2018, super PACs spent \$12,451,341 in Senate and House elections, with an average of \$1,131,940 spent per House seat, more than 13 times the average in 2012.³⁷ Federal super PAC spending in Washington has followed national trends and increased over election cycles. For example, in 2018, super PACs spent \$10,125,982 on Washington's 8th Congressional District alone.³⁸ Kim Schrier won the race by roughly 15 thousand votes,³⁹ and massive super PAC spending undoubtedly had an impact on such a close race.

2. *Super PAC spending in state elections*

Similarly, super PAC spending dramatically increased in Washington state elections after the rulings of *Citizens United* and *SpeechNow*. Many super PACS focused on specific, impactful elections. For example, in 2012, super PACs spent \$20,422,419 on the gubernatorial race alone, with over \$18 million spent on negative advertising.⁴⁰

In 2016, super PACs spent over \$1 million on a single Washington Supreme Court race, with over 90 percent spent on a single candidate, Dave Larson.⁴¹ The super PAC that funded Larson, Citizens for Working Courts, received large contributions from Bill Gates, Paul Allen and Ken Fisher, all three multi-billionaires.⁴²

³⁶ *2012 Outside Spending, by Race*, Open Secrets, <https://www.opensecrets.org/outsidespending/summ.php?cycle=2012&disp=R&pty=A&type=A>.

³⁷ *2018 Outside Spending, by Race*, Open Secrets, <https://www.opensecrets.org/outsidespending/summ.php?cycle=2018&disp=R&pty=A&type=A>.

³⁸ *Washington District 08 Race*, Open Secrets, <https://www.opensecrets.org/races/outside-spending?cycle=2018&id=WA08>.

³⁹ *November 6, 2018 General Election, Congressional District 8*, Office of the Secretary of State, <https://results.vote.wa.gov/results/20181106/CongressionalDistrict8.html>.

⁴⁰ *Independent Expenditures, 2012*, PDC, https://www.pdc.wa.gov/browse/more-ways-to-follow-the-money/ie/independent-expenditures?election_year=2012&category=Independent%20Expenditures.

⁴¹ *Independent Expenditures, 2016*, PDC, https://www.pdc.wa.gov/browse/more-ways-to-follow-the-money/ie/independent-expenditures?election_year=2016&category=Independent%20Expenditures.

⁴² Jim Brunner and Steve Miletich, *Bill Gates, others donate nearly \$1M to defeat Supreme Court Justice Wiggins*, The Seattle Times, Nov. 14, 2016, <https://www.seattletimes.com/seattle-news/politics/bill-gates-others-donate-1m-to-defeat-supreme-court-justice-wiggins/>.

In 2017, super PACs spent almost \$6 million on a single Washington state special election.⁴³ The outcome of the race would decide which caucus had a majority for the 2018 session. The race came down to just five thousand votes.⁴⁴

3. *Super PAC spending in Seattle elections*

Independent expenditures in Seattle have increased dramatically since the creation of super PACs in 2010. Expenditures in the Seattle mayoral race have quintupled since 2009 and almost doubled from 2013 to 2017.⁴⁵ In the most recent election, more than 83 percent of all super PAC funding went to Jenny Durkan, who won the race.⁴⁶ Durkan’s super PAC, People for Jenny Durkan, received a majority of its funding from one organization, Civic Alliance for a Sound Economy (CASE).⁴⁷ CASE in turn received \$350,000 from Amazon and \$114,062 from Vulcan Inc.⁴⁸ This “nesting doll” technique—a series of different super PACs and organizations giving money to each other—allows for corporations and other large donors to have unprecedented influence on all types of elections while also covering their tracks and making it difficult for the public to know who is funding which candidates.

There has also been a meteoric rise in super PAC spending in Seattle city council elections. While super PACs spent nothing in 2013,⁴⁹ and only \$3,577 in 2013,⁵⁰ super PAC spending jumped to \$784,644 in

⁴³ *Independent Expenditures, 2017*, PDC, https://www.pdc.wa.gov/browse/more-ways-to-follow-the-money/ie/independent-expenditures?election_year=2017&category=Independent%20Expenditures. The candidates were Manka Dhingra and Jinyoung Englund.

⁴⁴ *Washington State Senate District 45*, Ballotpedia, https://ballotpedia.org/Washington_State_Senate_District_45

⁴⁵ Seattle Ethics & Election Commission, 2017 Election Report, 15, Mar. 9, 2018, <http://www2.seattle.gov/ethics/elpub/2017Report.pdf>

⁴⁶ Daniel Beekman, *Jenny Durkan defeats Cary Moon to become Seattle’s first woman mayor since the 1920s*, The Seattle Times, Nov. 8, 2017, <https://www.seattletimes.com/seattle-news/politics/seattle-mayoral-race-jenny-durkan-cary-moon/>.

⁴⁷ *Contributions to People for Jenny Durkan 2017 Election Cycle*, Seattle Ethics & Election Commission, http://web6.seattle.gov/ethics/elections/poplist_v2.aspx?cid=583&listtype=contributors. CASE contributed over \$600,000 in 2017.

⁴⁸ Ashley Stewart, *Amazon, Vulcan and CenturyLink top list of donors to pro-Durkan chamber group*, Puget Sound Business Journal, Nov. 2, 2017, <https://www.bizjournals.com/seattle/news/2017/11/02/jenny-durkan-seattle-chamber-case-pac-donors.html>. Other notable CASE contributors include: CenturyLink (\$27,500); Starbucks (\$25,000); Comcast (\$25,000); and Alaska Airlines (\$18,000).

⁴⁹ Seattle Ethics & Election Commission, 2017 Election Report, 1, Mar. 9, 2018,

⁵⁰ *Id.*

2015.⁵¹ Super PACs concentrated spending on two seats, Seat 1 and Seat 8.⁵² Some \$223,132 of super PAC money was spent on Seat 1,⁵³ a seat decided by just 39 votes.⁵⁴ In 2017, total super PAC spending in city council elections went down, but only because there were fewer seats up for election. In fact, average spending per seat actually *doubled* from 2015 to 2017.⁵⁵

Recent developments suggest that super PAC spending will only increase in the upcoming 2019 city council elections. In 2018, corporations with Seattle presences spent massive amounts of money to repeal a city-council-approved tax.⁵⁶ Over forty companies together contributed \$325,000 to the campaign, with Starbucks and Amazon each contributing \$25,000.⁵⁷ The campaign was a success, and the city council repealed the ordinance.

Perhaps galvanized by the victory, corporations look primed to spend big in the 2019 elections. Amazon, Expedia, Vulcan, Alaska Airlines and other corporations have already begun funding super PACs like CASE, with Amazon making an unprecedented \$200,000 contribution.⁵⁸ CASE has already raised close to \$1 million for 2019 elections.⁵⁹ Further, acceptance of super PAC money is becoming more of a necessity to have a chance, sometimes even in city council elections. Almost half of candidates running for city council have suggested they would be

⁵¹ *Id.*

⁵² See *Independent Expenditures, 2015*, PDC, https://www.pdc.wa.gov/browse/more-ways-to-follow-the-money/ie/independent-expenditures?election_year=2015&category=Independent%20Expenditures.

⁵³ *Id.*

⁵⁴ https://ballotpedia.org/Seattle,_Washington_municipal_elections,_2015

⁵⁵ 2017 Report, 16. The per seat average in 2017 was \$179,447. In 2015 \$87,182.

⁵⁶ Daniel Beekman, *Amazon, Starbucks pledge \$25,000 each to campaign for referendum on Seattle head tax*, The Seattle Times, May 23, 2018, <https://www.seattletimes.com/seattle-news/politics/amazon-starbucks-pledge-25000-to-campaign-for-referendum-on-seattle-head-tax/>.

⁵⁷ *Id.*

⁵⁸ Benjamin Romano & Paul Roberts, *Amazon contributes \$200,000 to Seattle Chamber's political action committee*, Seattle Times, Apr. 16, 2019, <https://www.seattletimes.com/business/amazon/amazon-contributes-200000-to-seattle-chambers-political-action-committee/>.

⁵⁹ *Contributions to Civic Alliance for a Sound Economy Sponsored by the Seattle Chamber 2019 Election Cycle*, http://web6.seattle.gov/ethics/elections/poplist_v2.aspx?cid=704&listtype=contributors.

pleased if CASE offered to spend money on their behalf.⁶⁰ CASE recently announced endorsements for the upcoming 2019 primary elections,⁶¹ and spending is expected to begin soon.

CASE is not an anomaly, as ex-mayor Tim Burgess recently started his own super PAC, People for Seattle, to influence city council elections.⁶² The super PAC raised \$120,000 in just five days, and received donations from the likes of multi-millionaire Tom Alberg, a former director at Amazon.⁶³ With Burgess suggesting People for Seattle will be around beyond the 2019 election, Seattle will have yet another major super PAC in city elections for years to come.

4. *Super PACs and quid pro quo corruption*

From a legal standpoint, the problem with super PACs is not their spending *per se*, but rather how donors and politicians can use them as vehicles for corruption by circumventing contribution limits.

According to the Supreme Court, the basis for limits on direct contributions to candidates is the prevention of quid pro quo corruption or the appearance of quid pro quo corruption. As noted above, right now the state limit on contributions to candidates for city office is \$800, and Seattle has chosen to impose an even more protective limit of \$500. The point of those limits is not that a contribution of \$502 is *necessarily* a bribe paid quid-pro-quo for official favors. Rather, the point is that the city council has determined that limiting contributions to \$500 protects against corruption (since smaller contributions are less valuable to candidates and hence less likely to be bribes) and also reduces the *appearance* of corruption (since voters will be less likely to think that a

⁶⁰ Lester Black and Nathalie Graham, *As Amazon Opens the Cash Spigot to Flip the Council, These Candidates Say, "Yes, Daddy!"*, The Stranger, May 21, 2019, <https://www.thestranger.com/slog/2019/05/21/40264827/as-amazon-opens-the-cash-spigot-to-flip-the-council-these-candidates-say-yes-daddy>.

⁶¹ CASE Announces 2019 Endorsements, Seattle Chamber, June, 19, 2019, <https://www.seattlechamber.com/home/advocacy/advocacy-news/details/2019/06/19/case-announces-2019-endorsements>.

⁶² David Kroman, *Ex-Mayor Burgess, Business Leaders Raise \$120k to Overhaul City Council*, Crosscut, May 28, 2019, <https://crosscut.com/2019/05/ex-mayor-burgess-business-leaders-raise-120k-overhaul-city-council>.

⁶³ Lester Black, *Tim Burgess Forms a PAC for Rich People, the Possibility of No Black Representation, And More City Council Election News*, The Stranger, May 31, 2019, <https://www.thestranger.com/slog/2019/05/31/40360039/tim-burgess-forms-a-pac-for-rich-people-the-possibility-of-no-black-representation-and-more-city-council-election-news>.

smaller contribution is a bribe), while permitting citizens to support their preferred candidates and those candidates to raise funds effectively.

But if Seattle has determined that a \$502 contribution to a candidate poses an unacceptable risk of corruption, then a \$50,000, or even \$500,000 contribution to a super PAC supporting that candidate poses a far greater risk of corruption. This opportunity arises even assuming that a super PAC does not “coordinate” its campaign strategy with a supported candidate, because the *contributor* is free to discuss both the “quid” and the “quo” with the candidate. We are not yet aware of a specific case of bribery in the city of Seattle via a contribution to a super PAC, but examples are cropping up around the country,⁶⁴ and the city is not required to wait for a specific local example of criminal bribery by super PAC before it can protect its democracy.

Furthermore, the *appearance* of corruption via large super PAC contributions is well established. Opinion surveys consistently show a pervasive appearance of corruption *specifically attributable to large super PAC contributions*.

In an April 2012 Brennan Center for Justice survey focusing specifically on super PACs, 69% of respondents (including 74% of Republicans and 73% of Democrats) agreed that “new rules that let corporations, unions and people give unlimited money to Super PACs will lead to corruption.”⁶⁵ Seventy-three percent of respondents (75% of Republicans, 78% of Democrats) agreed that “there would be less corruption if there were limits on how much could be given to Super PACs.”⁶⁶ In a March 2012 ABC News/Washington Post survey, 69% of respondents stated that super PACs should be illegal.⁶⁷ A similar survey that asked the same question in North Carolina yielded nearly

⁶⁴ See *United States v. Lindberg*, No. 5:19-CR-00022 (W.D.N.C. indictment filed May 18, 2019); *United States v. Menendez*, No. CR 15-155, 2018 WL 526746, at *9 (D.N.J. Jan. 24, 2018).

⁶⁵ Brennan Ctr. for Justice, *National Survey: Super PACs, Corruption, and Democracy* (Apr. 24, 2012), <https://www.brennancenter.org/analysis/national-survey-super-pacs-corruption-and-democracy> (summary and appendix).

⁶⁶ *Id.*

⁶⁷ Damla Ergun, *Seven in 10 Would Send Super PACs Packing*, ABC News (Mar. 13, 2012), <http://abcnews.go.com/blogs/politics/2012/03/seven-in-10-would-send-super-pacs-packing/>; Wash. Post, *Washington Post-ABC News Poll* (Mar. 10, 2012), http://www.washingtonpost.com/wp-srv/politics/polls/postabcpoll_031012.html (question 33).

identical results.⁶⁸ These numbers are comparable to levels that the Supreme Court has already found sufficient to establish an appearance of corruption.⁶⁹ And it is not only a matter of opinion polls; when ordinary people are asked to act as jurors in mock trials, they act in accordance with the same understanding.⁷⁰

III. Conclusion

In recent years, Seattle has taken important steps towards preventing corruption and enhancing democratic self-government by limiting contributions to candidates and providing for citizen-funded elections through the Democracy Voucher Program. However, the prospect of political spending by foreign-influenced corporations and circumvention of contribution limits by massive contributions to super PACs threatens to undermine the work that Seattle has done. Seattle has a golden opportunity to take a principled stand for the benefit of its residents.

If we may be of any further assistance, please do not hesitate to contact us.

Sincerely,

Ron Fein
Legal Director, Free Speech For People
617-244-0234
rfein@freespeechforpeople.org

Enclosure:

Testimony of Prof. John Coates, Harvard Law School, to Massachusetts state legislature regarding similar legislation (currently pending)

⁶⁸ See Elon Univ., *Elon Poll* 6 (Apr. 27, 2012), http://www.elon.edu/docs/e-web/elonpoll/042712_PollMethodology.pdf.

⁶⁹ See *Nixon v. Shrink Missouri Gov't PAC*, 528 U.S. 377, 394 (2000) (finding an appearance of corruption when an “overwhelming 74%” of voters approved an initiative limiting contributions).

⁷⁰ See Christopher Robertson et al., *The Appearance and the Reality of Quid Pro Quo Corruption: An Empirical Investigation*, 8 *Journal of Legal Analysis* 375 (Winter 2016), available at <https://academic.oup.com/jla/article/8/2/375/2502553>.



HARVARD LAW SCHOOL

CAMBRIDGE · MASSACHUSETTS · 02138

John C. Coates IV

*John F. Cogan, Jr. Professor of
Law and Economics*

Phone: 617-496-4420

Fax: 617-495-5156

jcoates@law.harvard.edu

May 14, 2019

Chairman Barry Finegold
Massachusetts State House
Room 507
Boston, MA 02133
barry.finegold@masenate.gov

Chairman John L. Lawn, Jr.
Massachusetts State House
Room 445
Boston, MA 02133
john.lawn@mahouse.gov

RE: An Act to limit political spending by foreign-influenced corporations
S.418 (Montigny), H.640 (Cutler), H.703 (Naughton)

Dear Chairman Finegold and Chairman Lawn,

I am writing to express my support for the proposed law regarding political spending by foreign-influenced corporations. The proposed law would be a critical tool for uncovering foreign influences in our elections. Unlike many commentators, my background is not in constitutional law – I gather my colleague Larry Tribe has endorsed the bill, and he knows far more about those topics than I do. What I may add to this debate is corporate law knowledge – both from study as an academic and perhaps more importantly from extensive practical experience, sketched below. Drawing on that experience, below I explain how corporations could – practically and at reasonable expense -- obtain responsive information about the foreign national status of shareholders, as would be required by the law.

Background

I am the John F. Cogan Professor of Law and Economics at Harvard Law School, where I also serve as Vice Dean for Finance and Strategic Initiatives, Chair of the Committee on Executive Education and Online Learning, and Research Director of the Center on the Legal Profession. Before joining Harvard, I was a partner at Wachtell, Lipton, Rosen & Katz, specializing in financial institutions and M&A. At HLS and at Harvard Business School, I teach corporate governance, M&A, finance, and related topics, and I am a Fellow of the American College of Governance Counsel. I have testified before Congress and provided consulting services to the U.S. Department of Justice (DOJ), the U.S. Department of Treasury, the New York Stock Exchange, and participants in the financial markets, including hedge funds, investment banks, and private equity funds. I have served as an independent consultant for the Securities and Exchange Commission (SEC), and as an independent representative of individual and institutional clients of institutional trustees and money managers, and I currently am serving as a DOJ-appointed independent monitor for one of the Global Systemically Important Financial Institutions. In June 2016, I testified by invitation at a forum on “Corporate Political Spending and Foreign Influence” at the Federal Election Commission.

Foreign corporate spending in American elections

Since the Supreme Court’s 2010 *Citizens United* decision invalidated restrictions on corporate political spending,¹ the possibility that American elections could be influenced by foreign interests via corporations has attracted considerable public and policymaker interest. Foreign governments, foreign-based companies, and people who are neither U.S. citizens nor permanent residents are currently barred by federal law from contributing or spending money in connection with federal, state, or local elections.² Unfortunately, *Citizens United* created a loophole to this ban: these foreign entities can invest money through U.S.-based corporations that can – as a result of the decision – then spend unlimited amounts of money in American elections.

The policy interest in regulating foreign influence need not rest on the idea that foreign investors are tied to hostile governments that are actively trying to

¹ *Citizens United v. FEC*, 558 U.S. 310 (2010).

² 52 U.S.C. § 30121(a). This prohibition was upheld by a unanimous U.S. Supreme Court in 2012. *See Bluman v. FEC*, 132 S. Ct. 1087 (2012).

undermine the democracy or economy of the United States, although there is growing evidence that Russia sought to do just that in the last federal election. In addition, it may separately rest on the observation that foreign nationals (even those in countries that are staunch U.S. allies) are simply not part of the U.S. polity. Democratic self-governance presumes a coherent and defined population to engage in that activity. Foreign nationals have a different set of interests than their U.S. counterparts, as regards a range of policies, such as defense, environmental regulation, and infrastructure. Few dispute the idea that a given government may properly seek to limit foreign influence over, in the words of the U.S. Supreme Court, “activities ‘intimately related to the process of democratic self-government.’”³ There is nothing particularly surprising or pernicious about this fact. Foreign and domestic interests predictably diverge.

Depending on the degree of their influence, foreign governments (or their agents, such as sovereign wealth funds), foreign corporations, or other foreign investors might be able to leverage ownership stakes in U.S. corporations to affect corporate governance. Through that channel, they could influence corporate political activity in a manner inconsistent with democratic self-government, or at least out of alignment with the interests of U.S. voters.

Every country regulates some types of foreign and domestic business activities differently. In many domains of the American economy, long-standing statutes, regulations, and legal traditions treat foreign companies or foreign-influenced companies differently than domestic companies. The United States has specific foreign restrictions across a number of different industries. In shipping, aircraft, telecom, and financial services, laws governing all of these industries limit or regulate foreign ownership or control. Some ban foreign ownership completely, and, for some, foreign ownership or control triggers special government approval procedures.

The same spirit of those bodies of law should inform regulation of election spending by foreign-influenced corporations. Since *Citizens United* opened the door for political activity by corporations, some corporations of which ownership or control is likely held in significant part by foreign entities have devoted considerable financial resources to influencing American elections.

In practice, the policy preferences of foreign-influenced corporations are sometimes clear from public sources. In May 2016, Uber and Lyft spent over

³ *Bluman v. FEC*, 800 F. Supp. 2d 281, 287 (D.D.C. 2011)(quoting *Bernal v. Fainter*, 467 U.S. 216, 220 (1984)), *aff'd*, 132 S.Ct. 1087 (2012).

\$9 million on a ballot initiative in Austin, Texas that would have overturned an ordinance passed by the Austin City Council requiring the companies' drivers to submit to fingerprint-based criminal background checks.⁴ Weeks later, Uber disclosed that the Saudi Arabian government had invested \$3.5 billion in the company, giving the Kingdom over five percent ownership and a seat on its board of directors.⁵ Last year, the multinational "homestay" corporation Airbnb responded to the New York Legislature's growing interest in regulating the industry by arming a super PAC with \$11 million to influence New York's legislative races.⁶ Airbnb – a privately held company – is partly owned by Moscow-based DST Global.⁷

In another striking example, APIC, a San Francisco-based company described as "controlled" and "100 percent owned" by Gordon Tang and Huaidan Chen -- two Chinese citizens with permanent residence in Singapore -- gave \$1.3 million to a super PAC that had supported Jeb Bush's run for president.⁸

⁴ Nolan Hicks, "Prop 1 campaign crosses \$9 million threshold," AUSTIN-AMERICAN STATESMAN, May 9, 2016, <http://atxne.ws/29pbFBk>.

⁵ See Elliot Hannon, "Saudi Arabia Makes Record \$3.5 Billion Investment in Uber," SLATE, June 1, 2016, <http://slate.me/1UvvM3x>. Uber also spent roughly \$600,000 on a 2015 voter referendum in Seattle. See Karen Weise, "This is How Uber Takes Over a City," BLOOMBERG, June 23, 2015, <http://bloom.bg/1Ln2MaN>.

⁶ Kenneth Lovett, "Airbnb to spend \$10 on Super PAC to fund pre-Election day ads," N.Y. DAILY NEWS, Oct. 11, 2016, <http://www.nydailynews.com/news/politics/airbnb-spend-10m-super-pac-fund-pre-election-day-ads-article-1.2825469>.

⁷ See Dan Primack, "Yuri Milner adds \$1.7 billion to his VC war chest," FORTUNE, Aug. 3, 2015, <http://fortune.com/2015/08/03/yuri-milner-adds-1-7-billion-to-his-vc-warchest/> (DST Global is Moscow based); Scott Austin, "Airbnb: From Y Combinator to \$112M Funding in Three Years, The Wall Street Journal, July 25, 2011, <http://blogs.wsj.com/venturecapital/2011/07/25/airbnb-from-y-combinator-to-112m-funding-in-three-years/> (DST Global is a major investor in Airbnb).

⁸ Jon Schwartz & Lee Fang, "The Citizens United Playbook," THE INTERCEPT, Aug. 3, 2016, <http://bit.ly/2auW75p>.

Though the story made headlines, it echoes similar, yet less publicized, efforts to influence high-profile state and national races. For example, in 2012, a Connecticut-based subsidiary of a Canadian insurance and investment corporation gave \$1 million to the pro-Mitt Romney super PAC Restore Our Future.⁹ In 2013, a New Jersey-based subsidiary of a Chinese-owned business contributed \$120,000 directly to Terry McAuliffe’s gubernatorial campaign in Virginia.¹⁰

Ballot initiatives have been particularly strong magnets for spending by multinational corporations. American Electric Power, Limited Brands, and Nationwide Insurance spent a combined \$275,000 against a municipal initiative aimed at reconfiguring the Columbus City Council.¹¹ In 2012, a Los Angeles County ballot measure, the “Safer Sex in the Adult Film Industry Act,” attracted over \$325,000 from two companies tied to a Luxembourg corporation that ran adult webpages.¹² The company’s then-CEO was a German national.¹³ That same year, a statewide ballot initiative in California that would have required all foods containing genetically modified organisms to be labeled as such attracted \$45 million in spending by multinationals such as Monsanto and

⁹ Michael Beckel, “Foreign-Owned Firm Gives \$1 Million to Romney Super-PAC,” MOTHER JONES, Oct. 5, 2012, <http://www.motherjones.com/politics/2012/10/canadian-foreign-donation-super-pac-restore-our-future>.

¹⁰ John Schwartz, “Va. Gov. Terry McAuliffe Took \$120K from a Chinese Billionaire—but the Crime Is That It Was Legal,” THE INTERCEPT, June 1, 2016, <http://bit.ly/1XPvuXN>.

¹¹ Lucas Sullivan, “Follow the money flowing to ward initiative campaigns in Columbus,” THE COLUMBUS DISPATCH, July 22, 2016, <http://bit.ly/2ahlSpq>.

¹² See Ciara Torres-Spelliscy, “How a Foreign Pornographer Tried to Win a U.S. Election,” THE BRENNAN CENTER FOR JUSTICE, Nov. 6, 2015, <http://bit.ly/29pesu2>.

¹³ *Id.*

DuPont.¹⁴ Opponents of the measure spent five times more than its supporters, and ultimately defeated it by a 53-47 margin.¹⁵

Of course, not all politically active corporations are owned or controlled in significant part by foreign entities. Many privately held companies are owned directly by one or a small number of U.S. citizens. Among U.S. public companies, foreign ownership varies. I have carefully researched foreign ownership of large U.S. companies (see the short paper attached as an appendix to this letter) finding that, among publicly traded corporations in the Standard & Poor's (S&P) 500 index, one in eleven (~9 percent) has a foreign institutional investor with more than five percent of the company's voting shares. (Five percent was chosen for the study because it is the threshold at which federal securities law requires public disclosure of large stockholdings of US public companies.¹⁶)

But other corporations may have foreign ownership at substantial levels that would make unaffiliated foreign investors theoretically capable of exerting influence on the corporate political spending, even at levels below five percent of total stock. One such method is by presenting proposals for a vote by the shareholders. Any investor who can present a shareholder proposal (either alone, or by working with a group of other investors) has substantial leverage. Indeed, in recent proxy seasons, the New York City Pension Fund, despite owning less than one percent of outstanding shares in the target companies, led

¹⁴ Suzanne Goldenberg, "Prop 37: food companies spend \$45m to defeat California GM label bill," THE GUARDIAN, Nov. 5, 2012, <http://bit.ly/29I3SE7>.

¹⁵ *Id.*

¹⁶ Under Section 13(d) of the Securities Exchange Act of 1934 (as amended by the Williams Act), any person or group of persons who acquire beneficial ownership of more than five percent of the voting class of the equity of a corporation that is listed or otherwise required to register as a "public" company under that law, must, within ten days, report that acquisition to the Securities and Exchange Commission (SEC) via Schedule 13D (or, in some cases, Schedule 13G). *See* 15 U.S.C. § 78m(d); 17 C.F.R. §§ 240.13d-1, 240.13d-101.

successful shareholder proposal campaigns regarding proxy access.¹⁷ Furthermore, this type of influence is not limited to actually presenting shareholder proposals; the ability to do so creates indirect means of influence, such as *threatening* a shareholder proposal, and it means that, in many cases, an investor at that level can get upper management, including the CEO, on the phone.

Under current federal law, the threshold for presenting a shareholder proposal at a publicly-traded company is owning either 1% of voting shares or \$2,000 in market value.¹⁸ Interestingly, while there is a political debate as to whether to raise or eliminate the \$2,000 qualification, virtually *no one* questions that owning 1% of voting shares should continue to qualify an investor for this method of influence. For example, one of the first bills proposed in 2017 in the U.S. House of Representatives was the Financial CHOICE Act of 2017, which proposed to eliminate the \$2,000 market value threshold, but retain the 1% ownership threshold.¹⁹ In committee markup debate over the CHOICE Act, then-Rep. Jeb Hensarling (R-Tex.) explained that “we have something fairly reasonable and that is, you know, if you are going to put forward these proposals, have some real significant skin in the game. And what we say is 1 percent. One percent to put forward a shareholder proposal.”²⁰

Indeed, as part of those same political discussions, the Business Roundtable, a group of chief executive officers of major U.S. corporations formed to promote pro-business public policy, even proposed a threshold *below* 1% for shareholder proposals:

¹⁷ See Paula Loop, “The Changing Face of Shareholder Activism,” Harvard Law School Forum on Corporate Governance and Financial Regulation, Feb. 1, 2018, <https://corpgov.law.harvard.edu/2018/02/01/the-changing-face-of-shareholder-activism/>.

¹⁸ 17 C.F.R. 240.14a-8(b).

¹⁹ See Financial CHOICE Act of 2017, H.R. 10 (115th Cong.), § 844. <https://www.congress.gov/bill/115th-congress/house-bill/10/>.

²⁰ House Financial Services Committee, remarks of Rep. Jeb Hensarling, May 3, 2017.

For proposals related to topics other than director elections, a truly reasonable standard could be to use a sliding scale based on the market capitalization of the company, with a required ownership percentage of **0.15 percent for proposals submitted to the largest companies and up to 1 percent for proposals submitted to smaller companies.**

Additionally, if a proposal were submitted by a group or by a proponent acting by proxy, the ownership percentage sliding scale could be increased to up to 3 percent.²¹

In other words, the Business Roundtable recognizes that investors can *and should* have significant influence over corporate decision making at ownership levels between 0.15% to 1%, or 3% for groups of investors.

Regulating foreign corporate spending

The Commonwealth can simultaneously welcome foreign investment without exposing itself to the risk of foreign money influencing their elections. The proposed law addresses this issue through a requirement that prohibits a corporation from spending certain types of money in state elections if it is a “foreign-influenced corporation” – a definition based, in part, on the extent of foreign ownership of corporate stock.²² The proposed bill is a reasonable response to an increasingly localized problem, and is constitutional under the Court’s decision in *Citizens United*. The remainder of this letter details how this certification requirement could operate.

The mechanics of the bill’s foreign-influenced-corporation requirements

1. Ownership of corporate stock

To begin, as a general matter, corporate stock may be “owned” in three different forms. First, many companies that have one or a relatively small number of shareholders hold paper stock certificates. Among larger, stock exchange listed companies, with numerous owners, such direct ownership is

²¹ Business Roundtable, “Responsible Shareholder Engagement & Long-Term Value Creation,”

<https://www.businessroundtable.org/archive/resources/responsible-shareholder-engagement-long-term-value-creation> (emphasis added).

²² The three types of prohibited spending for foreign-influenced corporations are independent expenditures, electioneering communication expenditures, or contributions to independent expenditure PACs (often called super PACs). The bill does not change the existing definitions of these terms in state law.

rare, and increasingly so. At such companies, shares are more commonly held in “street name” through a broker (e.g., Fidelity or Charles Schwab). In these instances, the name on the stock certificate is actually the broker, but the broker keeps track in a database of how many shares belong to each client. Clients who hold shares in street name are “beneficial owners” under SEC rules, can direct brokers how to vote or sell shares, and can participate in corporate governance.

Most shares of large, listed companies, however, are now held by separate legal entities, such as mutual funds, pension funds, insurance companies, and hedge funds. As an economic matter, these entities hold stock on behalf of their clients or beneficiaries. However, as a legal matter, the investment entities themselves are the owners of the stock, and they do not pass through to beneficiaries either the right to vote or the right to sell the shares of the stock that the entity purchases. Individuals whose wealth is invested through these types of institutional investments cannot exercise voting rights associated with the shares. Instead, those rights are exercised by the management of the institutions.

2. Determining shareholders

Most corporate stock is not traded on public markets. As of 2012, more than five million corporations filed U.S. income tax returns. Only about 4,000 corporations were listed on a U.S. stock exchange – less than 0.1 percent of corporations that filed tax returns. Of the rest, many are owned by a single shareholder, or are beneficially owned by up to 500 individual owners. (SEC rules generally require public registration and disclosure for companies with more than 500 owners and \$10 million in assets.) Companies without public markets are still large and have substantial numbers of shareholders. Examples include Cargill, with revenues exceeding \$130 billion and over 200 shareholders, and Mars, with revenues exceeding \$33 billion and over 45 shareholders. Because shares of such companies do not trade freely in the public markets, such companies generally can and do track the identity of their shareholders directly.

For corporations listed on public markets, shares trade in significant volume—thousands of shares per day. However, publicly traded corporations have the ability to ascertain the exact ownership of their shares as of any arbitrary “record date.” In fact, this happens at least annually, because companies are required by corporate law to have annual shareholder meetings, for which they must set a record date to determine which shareholders are eligible to attend and vote at the meeting. In fact, record dates are set and shareholder lists are

created more frequently than that at many public companies, to allow for votes on off-cycle events, such as a merger proposal or charter amendments, which are brought to a vote at special meetings. Consequently, the ability to determine record stock ownership as of a given date is essential to the basic governance of corporations.

Few if any publicly traded corporations engage in the process of determining their record shareholders for a given record date themselves. They use an intermediary – most commonly, American Stock Transfer (AST) – that is dedicated to this function. Under state law, shareholders seeking to file a derivative suit or solicit shareholder support for a shareholder resolution or proxy contest can also obtain the list of shares using the same method. A corporation that needs the list of shareholders as of a specific date would engage AST to produce the list of shareholders as of that date. Under SEC rules, public companies also reach out beyond their record holders to the beneficial owners of broker- or bank-owned stock, and engage AST to contact banks, brokers or other intermediaries that are nominally record owners. Those firms, in turn, provide information about non-objecting beneficial owners to AST, which then compiles it and provides it to the corporation. Typically, banks, brokers and other intermediaries provide AST (and the corporation) with non-objecting client names, addresses, shares held, and purchase dates (which could be multiple blocks if a given shareholder bought multiple blocks of shares over time).

In addition to these basic corporate and securities law mechanisms, Section 13 of the federal Securities Exchange Act of 1934 requires any person or group of persons who acquire beneficial ownership of more than five percent of the voting class of a listed corporation’s equity to within ten days report that acquisition to the SEC on a Schedule 13D (or, in some cases, Schedule 13G).²³ These acquisitions are, in turn, made public by the SEC, and available through the SEC’s EDGAR online database.

3. Determining whether shareholders are “foreign owners”

The bill requires a corporation that plans to engage in political spending to ascertain whether it meets the threshold of “foreign-influenced corporation.” As just described above, acquisitions of five percent or more of the stock of public U.S. companies must already be disclosed under SEC rules, including the

²³ See 15 U.S.C. § 78m(d); 17 C.F.R. §§ 240.13d-1, 240.13d-101.

identity of the purchaser's citizenship.²⁴ Thus, the information is already publicly available (and readily available on commonly used search web sites such as Yahoo Finance or MSN Finance) for five percent blockholders of public companies. For ownership at lower thresholds,²⁵ the information is not publicly available, but can be ascertained. Outside of the blockholder context, for most purposes, corporations typically do not inquire into the citizenship or permanent residency status of shareholders. Many brokerage firms impose restrictions on non-citizens, or specifically limit their customers to citizens or permanent residents. A 2012 sampling of major brokers by financial markets reporter Matt Krantz found divergence in practices:

For instance, at Fidelity, the company says only U.S. citizens may open an account. . . . Over at TD Ameritrade, investors do not need to be a U.S. citizen to open an account. With that said, the stipulations and requirements vary dramatically based on the country the resident lives in and the potential customers' nationality, the company says. . . . Similarly at E-Trade, the brokerage has different rules based on the country. . . . The rules vary widely based on the nationality of the person wanting the account TradeKing requires investors, including U.S. citizens, to be U.S. residents to establish the account. It makes an exception for customers who are living abroad and have a valid U.S. military or government address. Investors who are not U.S. citizens, yet reside legally in the U.S., may open an account if they have a Social Security number and aren't from 27 specific [prohibited] countries²⁶

The process of ascertaining the foreign owner status of shareholders would be simple in many cases. If a publicly traded corporation asks American Stock Transfer to produce its list of shareholders (or just those shareholders who are foreign nationals), and AST in turn asks Fidelity, Fidelity's citizens-only customer policy would enable it to truthfully and simply answer that zero

²⁴ See 17 C.F.R. § 240.13d-101 (item #6, requiring reporting of "Citizenship or place of organization").

²⁵ Obviously, if a corporation determines from publicly available information that it has a 5% foreign owner, then it already meets the definition of foreign-influenced corporation and the inquiry is over; there is no need to *further* ascertain whether it *also* has additional foreign owners at lower ownership levels.

²⁶ Matt Krantz, USA TODAY, "U.S. online brokerage options are limited for foreigners," <http://usat.ly/KXpDan> (May 16, 2012).

percent of the company's shares held through Fidelity are held by foreign nationals.

Similarly, where stock is held by a non-human shareholder, such as another corporation, the "foreign" status of that corporation can be ascertained readily by examining its place of incorporation and principal place of business.

The proposed law counts stock owned by domestic subsidiaries of foreign parent corporations the same as stock owned by foreign corporations. (In the terms of the law, either would be defined as a "foreign owner.") To the extent that a U.S. subsidiary of a foreign corporation has the potential to influence U.S. portfolio companies in which it invests, it has the potential to do so at the foreign parent's bidding or with the foreign parent's approval.

However, the law does *not* require "piercing" through the beneficial ownership of institutional entities such as mutual funds. For the ordinance's purpose, corporate stock owned by a mutual fund is not corporate stock held by a foreign national, even if many of the mutual fund's customers are themselves foreign nationals, as long as the advisor to the fund is a U.S. entity (a fact that can be readily determined with public information). This is a reasonable approach, because customers of mutual funds cannot themselves directly participate in governance of the corporation actually spending money in a city election. Instead, it is the management of the advisory firm that plays that role.

4. "Due inquiry"

Importantly, the law addresses any remaining possible difficulties that U.S. corporations might have in certifying as to whether they are foreign-influenced. As noted above, some brokerage firms allow foreign investors to buy stock of U.S. companies through them, and they may not report citizenship information about such customers to the corporations in which they invest. Thus, it may not be possible for every corporation to verify the U.S. or foreign national status of all of its shareholders with complete confidence. (Note, however, that the law does not actually require a corporation to verify *all* of its shareholders' statuses: Given the 5 percent, "aggregate" threshold, verifying that just over 95 percent of shareholders are not foreign owners would be sufficient.)

However, given this possibility, it is reasonable for the proposed law to impose a certification requirement that specifies that the chief executive officer of the corporation certify that the information is provided after "due inquiry." The

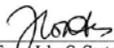
“due inquiry” standard is familiar from securities law,²⁷ as well as from other areas of law with which corporate executives are acquainted.²⁸ It imposes only the customary obligation to make such reasonable inquiry as the corporation would do in any event. Thus, the law does not impose a meaningful additional information-gathering cost beyond what it would already be required to do under existing law.

Conclusion

The law is a reasonable solution to the risk of foreign influence in local elections through corporate political spending. The law is constitutional under *Citizens United*, and reasonable from a corporate and securities law perspective. The law would only apply to corporations that spend money on independent expenditures, electioneering communications, or make contributions to “super PACs” in candidate elections. The law imposes no obligations on corporations that do not spend money on candidate elections. For those corporations that do engage in such spending, the requirement that corporations certify that they are not foreign-influenced is practicable and reasonable for both privately and publicly traded corporations, conditioned as it is on corporations engaging in “due inquiry,” a standard that will not add material costs to the information-gathering and record-keeping corporations already engage.

If you have any further questions, please let me know.

Sincerely,



John C. Coates IV
John F. Cogan, Jr. Professor of Law and Economics
Harvard Law School

²⁷ See, e.g., 17 C.F.R. § 275.206(4)-2(a)(3).

²⁸ See, e.g., *SRI Int’l, Inc. v. Advanced Tech. Labs., Inc.*, 127 F.3d 1462, 1464–65 (Fed. Cir. 1997) (in patent law, standard for whether infringement was “willful” is “whether the infringer, acting in good faith and upon due inquiry, had sound reason to believe that it had the right to act in the manner that was found to be infringing”); *Black Diamond Sportswear, Inc. v. Black Diamond Equip., Ltd.*, No. 06-3508-CV, 2007 WL 2914452, at *3 (2d Cir. Oct. 5, 2007) (“A trademark owner is “chargeable with such knowledge as he might have obtained upon [due] inquiry.”) (quoting *Polaroid Corp. v. Polarad Electronics Corp.*, 182 F. Supp. 350, 355 (E.D.N.Y. 1960)) (alteration in original).