No. 10-1305

Oral Argument Scheduled for April 7, 2011

IN THE UNITED STATES COURT OF APPEALS FOR
THE DISTRICT OF COLUMBIA CIRCUIT

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BUSINESS ROUNDTABLE and CHAMBER OF COMMERCE OF
THE UNITED STATES OF AMERICA,
*Petitioners*,
v.
SECURITIES AND EXCHANGE COMMISSION,
*Respondent*.

**On Review of an Order of the**
**United States Securities and Exchange Commission**

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# LAW PROFESSORS' BRIEF AS *AMICI CURIAE* IN SUPPORT OF THE SECURITIES AND EXCHANGE COMMISSION

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## GLOSSARY

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| Adopting Release | *Facilitating Shareholder Director Nominations*, 75 Fed. Reg. 56,668 (Sept. 16, 2010) |
| Commission or SEC | U.S. Securities and Exchange Commission |
| Rule 14a-3 | 17 C.F.R. § 240.14a-3 |
| Rule 14a-8 | 17 C.F.R. § 240.14a-8 |
| Rule 14a-11 | 17 C.F.R. § 240.14a-11 |

## INTERESTS OF THE *AMICI CURIAE*

The law professors filing this brief ("Law Professors") have extensive expertise in corporate, constitutional, and securities law.[1] The Law Professors do not hold the same views regarding the merits of or underlying policies behind the proposed Rule. The Law Professors also differ on many issues concerning corporate governance and corporate law policy. The Law Professors agree, however, that Rule 14a-11 as promulgated by the Commission does not violate the First Amendment.

The Law Professors file this brief and accompanying Motion for Leave to File pursuant to Fed. R. App. P. 29(b). No party's counsel authored the brief in whole or in part. No party or a party's counsel contributed money that was intended to fund preparing or submitting the brief. No person—other than the *amici curiae*, its members, or its counsel—contributed money that was intended to fund preparing or submitting the brief.

## SUMMARY OF ARGUMENT

1. Rule 14a-11 is permissible under the First Amendment because it neither compels a company to carry speech by third parties nor restricts a company from engaging in speech. Rule 14a-11 "define[s] how corporations govern themselves" by allowing shareholders who own a significant stake in a corporation

[1] The list of Law Professors filing this brief is attached hereto as Schedule A.

to place director nominees in the corporation's proxy statement. *Pacific Gas & Elec. Co. v. Public Utilities Comm'n of California*, 475 U.S. 1, 15 n.10 (1986).

2. The requirement in Rule 14a-11 that companies place information related to certain shareholder nominees in the company's proxy statement does not violate the First Amendment. Courts have long held that federal securities regulations that compel corporate disclosures are not prohibited by the First Amendment. For over 70 years, the federal government has regulated securities primarily through regulating the speech of corporations, management, and shareholders. Subjecting these laws to strict First Amendment scrutiny would eviscerate the government's ability to enact and enforce regulations that promote market integrity, capital formation, and investor protection.

## ARGUMENT

### I. RULE 14a-11 EMPOWERS SHAREHOLDERS WHO OWN A SIGNIFICANT STAKE IN THE COMPANY TO PLACE DIRECTOR NOMINEES IN THE COMPANY'S PROXY STATEMENT AND DOES NOT COMPEL THE COMPANY TO CARRY SPEECH BY THIRD PARTIES

Petitioners' argument that Rule 14a-11 violates the First Amendment because it compels companies to promulgate speech by third parties is without merit. *See* Petitioners' Br. at 55-57. In *Pacific Gas*, cited by Petitioners, the Court held that a law violated the First Amendment because it required a utility company "to include in its billing envelopes speech of a third party with which the utility

disagrees." 475 U.S. at 4. The Court held: "The essential thrust of the First Amendment is to prohibit improper restraints on the voluntary public expression of ideas.... There is necessarily ... a concomitant freedom not to speak publicly." *Id*. at 11 (internal quotations omitted). Shareholders, however, unlike third parties, have an *ownership interest* that is defined by state and federal laws and have rights and powers that properly are understood to be part of the "internal affairs" of a corporation. As the plurality in *Pacific Gas* explained, such laws do not implicate a company's First Amendment rights:

> [Laws enabling shareholders to place materials in a proxy statement] allocate shareholder property between management and certain groups of shareholders. Management has no interest in corporate property except such interest as derives from the shareholders; therefore, regulations that limit management's ability to exclude some shareholders' views from corporate communications do not infringe corporate First Amendment rights. Second, the regulations govern speech by a corporation to itself . . . . Rules that define how corporations govern themselves do not limit the range of information that the corporation may contribute to the public debate.

*Id*. at 15 n.10.[2]

[2] *See also* Lucian A. Bebchuk and Robert J. Jackson, Jr., *Corporate Political Speech: Who Decides*, 124 HARV. L. REV. 83, 109 (2010) ("Accepting that the corporation independently bears [First Amendment] rights does not suggest that the corporation's wishes should be determined solely, by, say, its executives, and surely the Constitution does not require that result."); Victor Brudney, *Business Corporations and Stockholders' Rights Under the First Amendment*, 91 YALE L.J. 235, 241 (1981) ("[T]he restrictions on government power contained in the First Amendment do not address, or without more inhibit, the government's power to determine whether corporate decisions should be made by officers or directors

Petitioners argue that Rule 14a-11 does not concern "speech by a corporation to itself" because it gives power to individual shareholders – not shareholders in the aggregate – to access the company's proxy materials.[3] The plurality in *Pacific Gas*, however, specifically rejected this argument, recognizing that Rule 14a-8, which has given *individual* shareholders the right to place proposals in a company's proxy statement for decades,[4] did not violate the First Amendment because it merely "defined how corporations govern themselves." 475 U.S. at 15.

Indeed, state and federal law traditionally have granted shareholders *individual* rights with respect to their company.[5] For example, an individual shareholder can bring a derivative suit on behalf of their company. *See Kamen v.*

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without even consulting stockholders, only by stockholders, or only by supermajority or unanimous vote of stockholders.").

[3] *See* Petitioners' Br. at 59 ("Moreover, 14a-11 trumps the interest in corporate property that derives from the shareholders, by forcing shareholders to provide access to a minority of activist investors even if the vast majority of shareholders oppose any access regime, or favor a more restrictive one." (internal citations and quotations omitted)).

[4] *See* Solicitation of Proxies under the Act: Final Rule 7 Fed. Reg. 10655, 10656 (Dec. 22, 1942) (adopting rule requiring company to place shareholder proposals on the company's proxy statement where the proposal concerns "a proper subject for action by the security holders.").

[5] It is hard to imagine how dispersed shareholders of publicly held companies – which number in the millions at some companies, and in the thousands in many companies – could practically exercise speech rights as a collective.

*Kemper Fin. Servs., Inc.*, 500 U.S. 90, 95 (1991) ("[T]he purpose of the derivative action was to place in the hands of the *individual* shareholder a means to protect the interests of the corporation from the misfeasance and malfeasance of faithless directors and managers" (internal quotations omitted) (emphasis added)). As *Pacific Gas* recognized, state and federal law may allocate corporate power between individual shareholders and management without violating the First Amendment. 475 U.S. at 15.

The First Amendment has never been held to restrict state law requiring a company to provide a forum for shareholders to speak. Under Delaware law, for example, companies must hold an annual meeting to provide shareholders with a forum to air their views about management. *See* 8 Del. Code § 211; *Hoschett v. TSI Int'l Software, Ltd.*, 683 A.2d 43, 45 (Del. Ch. 1996) ("[T]he annual meeting may in some instances be a bother to management, or even, though rarely, a strain, but in all events it provides a certain discipline and an occasion for interaction and participation of a kind. Whether it is welcome or resented by management, however, is in the end, irrelevant under Section 211."). Petitioners do not suggest that requiring an annual meeting violates the First Amendment – even though it facilitates speech by individual shareholders who attend the meeting. Rule 14a-11 merely creates another venue, similar to the annual meeting, to foster communication among shareholders to promote more informed voting, and

provides an opportunity for shareholders and management to communicate. As the Commission noted in adopting Rule 14a-11, "[T]he new rules will enable the proxy process to more closely approximate the conditions of the shareholder meeting." Adopting Release[6] at 56670. For companies with dispersed shareholders, Rule 14a-11 provides an effective means for shareholders to speak, to each other and to the board of directors, and to act as owners of the corporation.

It is also important to note that Rule 14a-11 does not prohibit management from expressing its disagreement with nominating shareholders in the company's proxy materials. See Adopting Release at 56770 ("Companies may increase solicitations to vote for their slate of directors, to vote against shareholder director nominees or vote against shareholder proposals."). Indeed, where shareholders include a proposal in a proxy statement under Rule 14a-8, it is customary for management who disagree with the proposal to include a statement in opposition. Rule 14a-11 is no different, and merely prevents management from using the company's proxy statement for a monologue rather than for facilitating a dialogue among different corporate constituents.

[6] Facilitating Shareholder Director Nominations, 75 Fed. Reg. 56,668 (Sept. 16, 2010) will be referred to as the "Adopting Release."

## II. THE FIRST AMENDMENT PERMITS THE GOVERNMENT TO REGULATE THE MARKET FOR SECURITIES BY COMPELLING DISCLOSURES

The First Amendment does not prohibit the government from adopting securities regulations such as Rule 14a-11 that compel disclosure. In *Ohralick v. Ohio State Bar Ass'n*, 436 U.S. 447, 456 (1978), the Supreme Court stated,

> [I]t has never been deemed an abridgment of freedom of speech or press to make a course of conduct illegal merely because the conduct was in part initiated, evidenced, or carried out by means of language, either spoken, written, or printed. Numerous examples could be cited of communications that are regulated without offending the First Amendment, such as the exchange of information about securities, corporate proxy statements, the exchange of price and production information among competitors, and employers' threats of retaliation for the labor activities of employees. Each of these examples illustrates that the State does not lose its power to regulate commercial activity deemed harmful to the public whenever speech is a component of that activity.

(internal citations omitted).

Subsequent Supreme Court cases have confirmed that disclosure-based regulation pertaining to securities is permissible under the First Amendment. In *Dun & Bradstreet, Inc. v. Greenmoss Builders, Inc*, the Supreme Court reiterated that the securities laws can regulate speech without offending the First Amendment. 472 U.S. 749, 758 n.5 (1985) (quoting *Ohralick*, 436 U.S. 447, 456). In *Paris Adult Theatre I v. Slaton*, 413 U.S. 49, 61 (1973) the Court stated that Congress "strictly regulated public expression by issuers of and dealers in securities" without violating the First Amendment. Unsurprisingly, Petitioners

have cited no cases standing for the proposition that laws regulating securities through disclosure requirements are not permitted under the First Amendment.

This Court also has long recognized that the regulation of corporate disclosures in a proxy statement does not implicate First Amendment concerns. In *SEC v. Wall Street Publ'g Inst., Inc.*, 851 F.2d 365, 373 (D.C. Cir. 1988) the Court held, "If speech employed directly or indirectly to sell securities were totally protected, any regulation of the securities market would be infeasible-and that result has long since been rejected." Indeed, numerous provisions of federal securities laws regulate "speech" but have never been considered by this Court or by the Supreme Court as raising a First Amendment concern. *See, e.g.*, 15 U.S.C. § 77e (prohibiting communications in interstate commerce relating to unregistered securities); 15 U.S.C. § 78m (requiring registered companies to make periodic disclosures); 15 U.S.C. § 78n and Rule 14a-3 (prohibiting solicitation of proxies prior to distribution of proxy statement specifying information that must be provided to shareholders). Subjecting securities regulation to strict First Amendment scrutiny would disrupt the financial markets, impede the ability of corporations to raise capital, and undermine the integrity of our financial system.[7]

[7] *See* Michael R. Siebecker, *Corporate Speech, Securities Regulation, and an Institutional Approach to the First Amendment*, 48 WM & MARY L. REV. 613, 672 (2006) ("Considering the extraordinary importance of the securities regulations regime to American society and the inextricability of the link between speech regulations and the basic functioning of that institution, a strong institutional

Inconsistencies in Petitioners' argument illustrate the confusion that will be created if securities laws are subject to strict scrutiny under the First Amendment. For example, Petitioners concede that Rule 14a-8 is permissible under the First Amendment (Petitioners' Br. at 58), but argue that Rule 14a-11 is not. Yet, Petitioners offer no principled rationale for why the First Amendment should treat these two rules that require companies to include shareholder statements in proxy materials differently. Like Rule 14a-11, Rule 14a-8 requires a company, in certain circumstances, to include in its proxy statement material provided by shareholders, regardless of whether the company's board or management agrees with the shareholders' position.

Likewise, while Petitioners complain that Rule 14a-11 violates the First Amendment merely because it compels speech, they are silent as to why the alternative – requiring separate solicitation materials – does not. In either case, the Commission's rules compel certain disclosures. Rule 14a-11 merely establishes additional disclosure requirements for a corporation in the event a qualifying shareholder nominates a candidate for election as a director.

Furthermore, Petitioners' broad reading of the First Amendment would eviscerate state laws that promote the shareholder franchise. The Court has

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argument supports carving out from the First Amendment's reach the system of mandatory disclosure and reporting embedded in the U.S. securities laws.").

recognized that shareholders have "the ability to exercise their right – some would say their duty – to control the important decisions which affect them in their capacity as stockholders and owners of the corporation." *Med. Comm. for Human Rights v. SEC*, 432 F.2d 659, 680-81 (D.C. Cir. 1970), *vacated on other grounds*, 404 U.S. 403 (1972). To ensure that shareholders are informed when voting on corporate issues, state law requires the board to make full disclosure to shareholders of "all material information in the corporation's possession." *Blasius Indus., v. Atlas Corp.*, 564 A.2d 651, 659 n.2 (Del. Ch. 1988); *see also Malone v. Brincat*, 722 A.2d 5, 10 (Del. 1998) ("The duty of disclosure obligates directors to provide the stockholders with accurate and complete information material to a transaction or other corporate event that is being presented to them for action."). Indeed, this Court has recognized that "proxy materials which failed to make reference to the fact that a shareholder intended to present a proposal at the annual meeting rendered the solicitation inherently misleading." *Med. Comm.*, 432 F.2d at 677.

Petitioners' argument that all regulation of speech is subject to strict scrutiny under the First Amendment would require unprecedented court intrusion in Congress's ability to regulate broad areas of economic activity. *See* Petitioners' Br. at 56 ("Regulations compelling the content of speech must be narrowly tailored to serve a compelling governmental interest."). As the Court in *Ohralick*

recognized, numerous speech-based regulations do not implicate the First Amendment, including laws regulating employment law and antitrust law. *Ohralick*, 436 U.S. at 456. Adopting Petitioners' broad construction of the First Amendment would preclude Congress from passing laws in areas that it traditionally regulates by compelling disclosures or prohibiting speech, such as antitrust, labor relations, consumer protection, health and safety, and commercial transactions.[8]

Finally, Rule 14a-11 does not regulate "core political speech" so as to implicate the concerns identified by the Court in *Citizens United v. FEC*, 130 S.Ct. 876, 929 (2010) (internal quotations omitted). At most, it regulates disclosures that a company must make to shareholders related to the governance of the corporation. In this regard, it *facilitates* "corporate democracy", which the Court in *Citizens United* recognized is an important tool for shareholders to prevent abuses by management. *See id*. at 911. Nevertheless, even in the context of core political speech, the "[g]overnment may regulate corporate political speech through

[8] *See* Frederick Schauer, *The Boundaries of the First Amendment: A Preliminary Exploration of Constitutional Salience*, 117 HARV. L. REV. 1765, 1768, 1771 (2004) ("many . . . categories of 'speech' remain uncovered by the First Amendment" including "the Sherman Antitrust Act, the National Labor Relations Act, the Uniform Commercial Code, the law of fraud, conspiracy law, the law of evidence, and countless other areas of statutory and common law do not, at the least, present serious First Amendment issues.").

disclaimer and disclosure requirements." *Id*. at 886. Thus, to the extent that Rule 14a-11 requires corporate disclosures, it is permissible under the First Amendment.

## CONCLUSION

For the forgoing reasons, Rule 14a-11 does not violate the First Amendment.

January 27, 2011

Respectfully Submitted,

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## CERTIFICATE OF COMPLIANCE

I certify that this brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because it contains 3,198 words, excluding the parts exempted by Fed. R. App. P. 32(a)(7)(B)(iii) and Circuit Rule 32(a)(1).

I also certify that this brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because it has been prepared in a proportionally-spaced typeface using MS Word in 14-Point Times New Roman.

January 27, 2011

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## CERTIFICATE OF SERVICE

I hereby certify that on January 27, 2011, I electronically filed the foregoing LAW PROFESSORS' BRIEF AS *AMICI CURIAE* IN SUPPORT OF THE SECURITIES AND EXCHANGE COMMISSION with the Clerk of Court for the United States Court of Appeals for the District of Columbia Circuit by using the appellate CM/ECF system. I also hereby certify that within the allowed time period, I will serve the Clerk's Office with four (4) copies of the motion and eight (8) copies of the related brief via overnight delivery with a commercial carrier service.

Service was accomplished on all counsel via the Court's CM/ECF system

January 27, 2011

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