RUNNING THE D.C. CIRCUIT GAUNTLET ON COST-BENEFIT ANALYSIS AFTER CITIZENS UNITED: EMPIRICAL EVIDENCE FROM SARBANES-OXLEY AND THE JOBS ACT

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“The more strictly we are watched, the better we behave.”
-Jeremy Bentham

INTRODUCTION

“To require disclosure or not to require disclosure?” That is the question faced by regulators, including the Securities and Exchange Commission (SEC),2 in light of the Supreme Court’s 2010 decision in

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Citizens United v. FEC,\(^3\) which allowed for a new free flow of corporate money into the American political system.\(^4\) Since 2011, a petition by ten law professors asking for transparency of corporate political spending has been pending before the SEC.\(^5\) Over one million people have written to the SEC asking the Commission to act on this petition.\(^6\)

The political spending of publicly traded corporations is significant for two reasons: (1) public corporations tend to be larger, affording them greater potential influence over the political process, and (2) they tend to have more shareholders whose interests will be implicated by campaign spending. Here, “political spending” is meant to encompass all spending in the electoral process, whether directly or indirectly, and not, unless otherwise noted, disclosure of lobbying expenses. This article anticipates the SEC’s eventual promulgation of rules requiring disclosure of corporate political spending.\(^7\) Many of the core questions that we can now study about the market’s reaction to increased regulation of listed companies are likely to be implicated in the debate about corporate political spending disclosures.

Corporations that do not want to disclose their political spending are likely to challenge any rule that the SEC issues on the subject.\(^8\)

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3. Andrew Joseph, Poll: Most Voters Oppose Citizens United Decision, NAT. J. BLOG (Jan. 20, 2012), http://www.nationaljournal.com/blogs/influencealley/2012/01/poll-most-voters-oppose-citizens-united-decision-20 (“The poll found that 62 percent of all voters oppose the Supreme Court’s Citizens United decision (the two-year anniversary of which is tomorrow) and 46 percent of voters strongly oppose it. Meanwhile, 55 percent of voters do not believe that corporations should have the same rights as people.”).


7. 15 U.S.C.A. § 78q-1(b)(8) (West 2014) (authorizing the SEC to adopt “such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest, for the protection of investors”).

Such a legal challenge is destined to be heard by the D.C. Circuit, which examines many federal regulations with an increasingly jaundiced eye. This article addresses the hostility that the D.C. Circuit may harbor against a new SEC rule requiring greater corporate transparency in election activities and provides some data that might assist the SEC in navigating this gauntlet.

Of late, the D.C. Circuit has stuck down new regulations on numerous grounds, including finding that the SEC did not do a sufficiently rigorous cost-benefit analysis, that the rule does not foster market efficiency, or that it somehow conflicts with the First Amendment. If the SEC promulgates a new rule on corporate political spending, then neither the SEC nor the D.C. Circuit will be writing on a blank slate; both will stake a position in a long-running debate over what types of regulations foster efficient markets.

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12. Paul Stephen Dempsey, Market Failure and Regulatory Failure as Catalysts for Political Change: The Choice between Imperfect Regulation and Imperfect Competition, 46 WASH. & LEE L. REV. 1, 3 (1989) (examining “the major philosophical schools, [tracing] the evolution in public policy, and [assessing] some of the principal costs and benefits of regulation and deregulation”); Robert W. Ingram & Eugene G. Chewning, The Effect of Financial Disclosure Regulation on Security Market Behavior, 58 ACCT. REV. 562, 563 (1983) (studying the various views on the disclosure and regulation debate, noting that the “arguments posited as justification for market regulation . . . include (1) the existence of inadequate incentives to disclose information, (2) unequal possession of information, and (3) motivation to suppress unfavorable information in an unregulated environment”); see also Raymond H. Brescia, Trust
one extreme, laissez-faire purists have argued that all regulations burden the invisible hand of the market\(^\text{13}\) and are particularly costly for smaller firms.\(^\text{14}\) The solution for a laissez-faire purist would be no regulation of business, not even modest disclosure requirements.\(^\text{15}\) But for others, timely, robust disclosures and other securities regulations are precisely the reason that the American securities markets are the market of choice for investors around the world.\(^\text{16}\) Regulation, in other words can, if properly designed, produce benefits in the form of

\(\text{in the Shadows: Law, Behavior, and Financial Re-regulation, 57} \text{BUFF. L. REV.} 1361 (2009)}\) (finding generally, that smart regulation instills trustworthiness among investors and the public which would increase economic growth).

\(13. \) E.g., Adam Smith, The Theory of Moral Sentiments 165 (6th ed. 1790) (“[The rich] are led by an invisible hand to make nearly the same distribution of the necessaries of life, which would have been made, had the earth been divided into equal portions among all its inhabitants, and thus without intending it, without knowing it, advance the interest of the society, and afford means to the multiplication of the species.”).

\(14. \) Frank H. Easterbrook, Mandatory Disclosure and the Protection of Investors, 70 VA. L. REV. 669, 687 (1984) (“Mandatory disclosure rules promulgated by the government are one means to achieve standardization, but it does not follow that mandatory disclosure is necessary.”).

\(15. \) Lloyd L. Drury, III, Disclosure Is Speech: Imposing Meaningful First Amendment Constraints on SEC Regulatory Authority, 58 S.C. L. REV. 757, 759–60 (2007) (arguing that the role of the SEC in disclosure rulemaking should be limited because “economic research and related legal scholarship suggest that there is less need for the SEC to protect investors than exists in the case of normal consumer protection, where advertising enjoys full status as commercial speech”); Alan R. Palmer, Toward Disclosure Choice in Securities Offerings, 1999 COLUM. BUS. L. REV. 1, 5–6 (arguing that “U.S. issuers have increasingly shunned public offerings in favor of private offerings to avoid the costs of mandatory disclosure and heightened liability”); Roberta Romano, Empowering Investors: A Market Approach to Securities Regulation, 107 YALE L.J. 2359, 2375 (1998) (“It is difficult to prove what, if any item, among required disclosures is of less value to investors than items voluntarily disclosed, but the great variety in content across disclosure regimes—a recent study identified one hundred SEC disclosure items deemed excessive compared to international standards—suggests that a number of mandates are not cost effective.”).

\(16. \) Cynthia A. Williams, The Securities and Exchange Commission and Corporate Social Transparency, 112 HARV. L. REV. 1197, 1200–07 (1999) (arguing in favor of stronger mandatory SEC disclosure rules in order to increase corporate social transparency); Jesse M. Fried, Firms Gone Dark, 76 U. CHI. L. REV. 135, 150, 152 (2009) (noting that “that public investors’ wealth increased substantially when firms were forced to enter the mandatory disclosure system”); Robert A. Prentice, The Inevitability of a Strong SEC, 91 CORNELL L. REV. 775, 819 (2006) (arguing further that mandatory disclosure provides more benefits to investors because it “reduces search and information processing costs for investors by requiring cheap, readily available, standardized, and relatively reliable disclosure of information”); Edward Rock, Securities Regulation as Lobster Trap: A Credible Commitment Theory of Mandatory Disclosure, 23 CARDozo L. REV. 675, 686 (2002) (arguing that “[t]he existing SEC disclosure system can be understood as . . . serv[ing] a standardization function, both with regard to form and quantity of disclosure, thereby aiding in the comprehension and comparison of different investment options. . . . Second, it provides a mechanism for the adjustment of reporting obligations over time. . . . Third, it provides a credible and specialized enforcement mechanism, which warrants both the comprehensiveness and quality of the information disclosed”).
lower costs of capital for companies.\textsuperscript{17} In brief, wise regulation fosters a market that is trustworthy and efficient.\textsuperscript{18} The goal is not regulation for its own sake, but rather to adopt an ideal level of regulation that provides investors with the optimal level of disclosures and protections at tolerable costs to reporting firms.\textsuperscript{19}

The question of whether a new SEC rule requiring political spending disclosures would be good for the markets is part of the larger debate over which types of disclosures and other securities regulations help rather than harm the market.\textsuperscript{20} This study considers two recently enacted major securities laws that took divergent approaches to regulation: (1) The Public Company Accounting Reform and Investor Protection Act, otherwise known as the Sarbanes-Oxley Act (SOX), and (2) the Jumpstart Our Business Startups Act (JOBS Act).\textsuperscript{21} This study then observes the market’s reaction based upon stock price movement to each law to test the

\textsuperscript{17} Richard B. Freeman, *Reforming the United States’ Economic Model After the Failure of Unfettered Financial Capitalism*, 85 CHI. KENT L. REV. 685, 695 (2010) (“The end result of the experiment in deregulation of finance was thus the opposite of what the aficionados of laissez faire intended. It created a finance sector and real economy more dependent on the government than before. It raised suspicions about competence and honesty not only in banking but in business in general.”); David Brodwin, *The Good Side of Federal Regulations*, U.S. NEWS \\
& WORLD REP. (Mar. 8, 2012, 2:06 PM), http://www.usnews.com/opinion/blogs/economic-intelligence/2012/03/08/the-good-side-of-federal-regulations (“As has been argued by leading business experts for years, thoughtful regulation can reduce waste, boost output, and even create jobs.”).

\textsuperscript{18} Perry E. Wallace, *Disclosure of Environmental Liabilities under the Securities Laws: The Potential of Securities-Market-Based Incentives for Pollution Control*, 50 WASH. \\
& LEE L. REV. 1093, 1129 (1993) (“By requiring disclosure and punishing disclosure violations and other securities-related wrongdoing, securities laws promote the public’s interest in the accuracy of securities prices and the general integrity of securities markets.”); Amy Deen Westbrook, *Sunlight on Iran: How Reductive Standards of Materiality Excuse Incomplete Disclosure Under the Securities Laws*, 7 HASTINGS BUS. L.J. 13, 75 (2011) (“The U.S. federal securities laws have been held up as a model of disclosure-based regulation, of a flexible and effective way to discipline a market and protect investors.”).

\textsuperscript{19} 15 U.S.C.A. § 78c(f) (West 2014).


\textsuperscript{21} Stacie K. Townsend, *The Jumpstart Our Business Startups Act Takes the Bite Out of Sarbanes-Oxley: Adding Corporate Governance to the Discussion*, 99 IOWA L. REV. 893, 896 (2014) (“[T]he general motivations behind SOX were investor protection and corporate governance. In 2012, following the recession caused by the global financial crisis, Congress passed the JOBS Act. Thus, Congress’s general motivation behind the JOBS Act was to spur economic activity.”).
broad question of whether the market prefers or opposes more disclosure.

While there will be distinctions between some of the financial disclosures required by the above laws and those disclosures that would be contained in a new rule on political spending, we do not believe such distinctions are so significant as to derail a meaningful analysis. If the market has a positive reaction to increased financial disclosures or, conversely, a negative reaction to the relaxation of financial disclosures, then it would stand to reason that the market would have a similar reaction to disclosures of corporate political spending.\(^{22}\)

This article first discusses the lack of an SEC rule on corporate political spending and argues that such a rule is needed in light of the Supreme Court’s *Citizens United* decision. It then explains the D.C. Circuit’s requirements of a cost-benefit analysis during the rule making process for federal administrative agencies like the SEC.\(^{23}\) It introduces data on the market’s reaction to SOX and to the JOBS Act, which shows that the market reacted positively to SOX and negatively to the JOBS Act.\(^{24}\) In short, the data demonstrates that the market values transparency and distrusts opaqueness.\(^{25}\) The D.C.

\(^{22}\) See Gary F. Goldring, *Mandatory Disclosure of Corporate Projections and the Goals of Securities Regulation*, 81 COLUM. L. REV. 1525, 1528–29 (1981) (“Corporate disclosure . . . improves informational efficiency because investors and the general market have more relevant information to incorporate into security prices. This, in turn, increases allocational efficiency.”).

\(^{23}\) Pub. Citizen v. Fed. Motor Carrier Safety Admin., 374 F.3d 1209, 1222 (D.C. Cir. 2004) (“Without such a cost-benefit analysis, accounting for benefits as well as costs, we do not understand how the remainder of the agency’s explanation, all of which focuses solely on the costs of the rule, could pass muster in this court on petition for review.”).

\(^{24}\) Additionally, in the case of SOX, the increase in market value for a median S&P 500 firm is about 80 times the increase in auditing expenses, the most cited costs of implementing the new disclosure rules. See Kathy Fogel, Rwan El-Khatib, Nancy Chun Feng, & Ciara Torres-Spelliscy, *The Market Reaction to Disclosure Rules*, RES. ACCT. REG. (under review).

\(^{25}\) To test the robustness of our findings, we included three variables that reflect the strength of corporate governance in the regressions. The first variable was a dummy that sets to one if the majority of the firm’s directors satisfies the New York Stock Exchange (NYSE) or NASDAQ listing requirements’ definition of independent directors. See Michael S. Weisbach, *Outside Directors and CEO Turnover*, 20 J. FIN. ECON. 431, 446–47 (1988). The next was the logarithm of board size, the number of directors serving on the board. David Yermack, *Higher Market Valuation of Companies with a Small Board of Directors*, 40 J. FIN. ECON. 185, 197 (1996). The third was the Entrenchment Index developed by Lucian A. Bebchuk, et al., *What Matters in Corporate Governance?* 22 REV. FIN. STUD. 783, 785 (2009), an index ranging from zero to six, with one point for each of the six provisions in the corporate charter or bylaws including the inclusion of staggered boards, poison pills, golden parachute, and supermajority requirements for amendments to the charter, bylaws, and mergers. Taken together, the governance variables do not appear to associate with excess returns due to the SOX or JOBS Act that we found elsewhere in this article.
Circuit should consider these results when it is eventually called upon to determine whether corporate political transparency regulations are allowable.

I. LACK OF AN SEC RULE ON POLITICAL SPENDING

While the SEC requires public firms to divulge many details of their financial health, corporate governance structures, and outstanding liabilities, it does not require public firms to inform investors about their political spending. Before 2010, not having such a disclosure rule made a certain amount of sense, as corporate political spending was generally barred in federal elections and in nearly half of state elections.

The absence of an SEC political spending rule post-Citizens United, however, is not an indication of shareholders’ lack of desire for such a rule. To the contrary, shareholders have launched several

26. John C. Coates, IV, SEC’s Non-Decision Decision on Corporate Political Activity a Policy and Political Mistake, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (Dec. 13, 2013 at 8:51 AM) [hereinafter Coates, Non-Decision], https://blogs.law.harvard.edu/corpgov/2013/12/13/secs-non-decision-decision-on-corporate-political-activity-a-policy-and-political-mistake/ (arguing that the SEC's decision to remove disclosure of political activities from its agenda “is a policy mistake, as it ignores the best research on the point . . . and perpetuates a key loophole in the investor-relevant disclosure rules, allowing large companies to omit material information about the politically inflected risks they run with other people’s money”). Coates also argues it is a political mistake “as it repudiates the 600,000+ investors who have written to the SEC personally to ask it to adopt a rule requiring such disclosure, and will let entrenched business interests focus their lobbying solely on watering down regulation . . . rather than having also to work to influence a disclosure regime.” Id; Dina El Boghdady, SEC Drops Disclosure of Corporate Political Spending from its Priority List, WASH. POST (Nov. 30, 2013), available at http://www.washingtonpost.com/business/economy/sec-drops-disclosure-of-corporate-political-spending-from-its-priority-list/2013/11/30/f2e92166-5a07-11e3-8304-c4af30786cd9_story.html.

27. Life After Citizens United, NAT’L CONF. OF STATE LEGISLATURES (Jan. 4, 2011), www.ncsl.org/default.aspx?tabid=19607 (“While the ruling does not directly affect state laws, there are 24 states that currently prohibit or restrict corporate and/or union spending on candidate elections.”); but see Adam Winkler, “Other People’s Money”: Corporations, Agency Costs, and Campaign Finance Law, 92 GEO. L.J. 871 (2004) (indicating that even before Citizens United, corporations were a source of funds for campaigns and that executives would donate money and receive money in back in the form of “bonuses”).

28. See Bebchuk & Jackson, supra note 2, at 937 (“[P]ublic companies spend significant amounts of shareholder money on politics, and the levels and recipients of the spending are not transparent to investors . . . . in response, shareholders have increasingly expressed strong interest in receiving information on political spending from the companies they own.”); Christopher P. Skroupa, Investors Want Disclosure of Corporate Political Contributions and Lobbying Expenditures, FORBES (Apr. 20, 2012), http://www.forbes.com/sites/christopherskroupa/2012/04/20/investors-want-disclosure-of-corporate-political-contributions-and-lobbying-expenditures-2/ (“A 2011 S&P 500 study found that S&P 500 companies spent a total of $1.1 billion on 2010 political contributions. Of this figure, 87% or $973 million went to federal lobbying expenditure. Note this figure does not include corporate lobbying expenditures for
campaigns to bring corporate political spending out of the shadows. Some campaigns have targeted individual firms, while others have been aimed at the SEC, urging it to require uniform disclosure for all public companies. At four firms in 2014, the majority of shareholders voted for transparency. Several corporations have responded positively to these campaigns, even though the SEC has not. As a result, there is a mix of private ordering, with some corporations


disclosing their political spending while others do not. The SEC should intervene to make disclosures uniform for all public corporations. Although uniformity could also come from Congress, the SEC has the advantage of being able to act on disclosure more quickly than Congress.

II. CONTEXT: DARK MONEY AND THE NEED FOR A POST-CITIZENS UNITED RULE FROM THE SEC

Had the SEC required corporations to disclose political spending pre-2010, there would have been little to report. Corporations were generally forbidden from participating in elections using general corporate treasury funds. Rather corporations could participate through affiliated political action committees (PACs) that raised their own funds from shareholders and others associated with the corporation. That all changed with the Supreme Court’s decision in *Citizens United v. FEC*.


> [O]versight and transparency about spending policies have increased substantially, as boards appear to be responding to intense pressures from investors as well as the changed regulatory landscape since *Citizens United*. But disclosure of what companies spend remains inconsistent—particularly when it comes to indirect spending through trade associations and other politically active non-profit groups.

Id. at 14; see also Bruce Freed & Karl Sandstrom, SEC Should Force Companies to Disclose their Political Spending, REUTERS (June 24, 2013), http://blogs.reuters.com/great-debate/2013/06/24/sec-should-force-companies-to-disclose-their-political-spending/ (“For the fourth year in a row . . . [investors have] backed political disclosure proposals . . . . The number of resolutions has held steady for the past several years. Public polls have shown that disclosure is supported overwhelmingly by shareholders, directors and the public at large.”).


37. Michael Megaris, *The SEC and Mandatory Disclosure of Corporate Spending by Publicly Traded Companies*, 22 Kan. J.L. & Pub. Pol’y 432, 441 (2013) (“Given the inherent difficulties found in passing any form of legislation in Congress, and with the defeat of the [Shareholder Protection Act] and [the] DISCLOSE Act specifically in mind, the SEC is clearly best situated to adopt a policy concerning mandatory disclosure of political spending to shareholders, particularly when compared to Congress.”).

Much to the chagrin of those who believe corporate spending in elections could lead to political corruption, in 2010 the Supreme Court built on precedent that created corporate political speech rights in ballot initiatives. In *Citizens United* the Court allowed corporations (and unions, by implication) to spend their treasury funds on political advertisements in local, state, and federal candidate elections. This grant of a new constitutional right for public corporations to spend in elections is a potentially compelling reason why the SEC should require disclosure of corporate political spending.

The SEC would be on firm constitutional ground in requiring increased political spending disclosure by public corporations. Indeed, in *Citizens United* the Supreme Court presumed that the new corporate political spending would be transparent. Writing for the

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41. *Citizens United*, 558 U.S. at 365 (“[T]he Government may not suppress political speech on the basis of the speaker’s corporate identity. No sufficient governmental interest justifies limits on the political speech of nonprofit or for-profit corporations.”); Benjamin I. Sachs, *Unions, Corporations, and Political Opt-Out Rights after Citizens United*, 112 COLUM. L. REV. 800, 802 (2012) (noting “[a]fter the decision, campaign finance law leaves unions and corporations equally unconstrained and free to use their general treasuries to fund federal electoral expenditures”). This was similar to the Court’s approach in *Bellotti*, where the Court stated that the Constitution protects corporations except for “[t]he Constitution protects corporations except for “[c]ertain ‘purely personal’ guarantees.” *Bellotti*, 435 U.S. at 779 n.14; *Citizens United*, 558 U.S. at 434 (Stevens, J., concurring in part and dissenting in part) (“Over the years, the limitations on corporate political spending have been modified in a number of ways, as Congress responded to changes in the American economy and political practices that threatened to displace the commonweal.”).


43. Richard Briffault, *Two Challenges for Campaign Finance Disclosure After Citizens United and Doe v. Reed*, 19 WM. & MARY BILL RTS. J. 983, 997 (2011) (“Chief Justice Roberts’s opinion effectively linked up electoral integrity and voter information by suggesting an overarching public interest in being able to monitor and understand the workings of the
majority, Justice Kennedy noted:

"With the advent of the Internet, prompt disclosure of expenditures can provide shareholders and citizens with the information needed to hold corporations and elected officials accountable for their positions and supporters. Shareholders can determine whether their corporation’s political speech advances the corporation’s interest in making profits, and citizens can see whether elected officials are ‘in the pocket’ of so-called moneyed interests.”

The Supreme Court has been clear that disclosing the sources of political spending is allowed. A new SEC rule revealing corporate political spending at its source is necessary to give meaning to the Court’s holding. Absent such regulatory action, the money is likely to remain in the shadows. Indeed, despite the clear message from the Supreme Court that disclosure is perfectly constitutional, the 2010 and 2012 federal elections were marred with hundreds of millions of dollars of untraceable funds known colloquially as “dark money.”

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44. *Citizens United*, 558 U.S. at 370 (citations and internal quotation marks omitted).
45. E.g., id. at 319 (“The Government may regulate corporate political speech through disclaimer and disclosure requirements, but it may not suppress that speech altogether.”).
46. Disclosure Comm. Petition, supra note 5, at 7 (“Because the Commission’s current rules do not require public companies to give shareholders detailed information on corporate spending on politics, shareholders cannot play the role the Court described.”).
47. *Citizens United*, 558 U.S. at 369 (“The Court has explained that disclosure is a less restrictive alternative to more comprehensive regulations of speech . . . . And the Court has upheld registration and disclosure requirements on lobbyists, even though Congress has no power to ban lobbying itself.”); Ciara Torres-Spelliscy, *Has the Tide Turned in Favor of Disclosure? Revealing Money in Politics After Citizens United and Doe v. Reed*, 27 GA. ST. U. L. REV. 1057, 1079 (2011) (“*Citizens United* gave a full-throated endorsement of disclosure based on both the voters’ informational interest as well as, in the case of corporations, the shareholders’ interest in holding corporations accountable for their political spending. The Supreme Court also upheld disclosure information about ballot measure petition signatories in *Doe v. Reed* in 2010.”).
Although this dark money was not entirely corporate, corporations are surely a source of some dark money.\textsuperscript{49}

How was some corporate spending able to remain “dark?” In a nutshell, corporations are still legally banned from giving directly to candidates for federal office in the United States.\textsuperscript{50} Instead, corporations have two major avenues for political engagement in American elections: (1) through the corporation’s own corporate PAC, funded by voluntary contributions of up to $5,000 by employees and other persons affiliated with the corporation;\textsuperscript{51} or (2) through the use of corporate treasury funds to buy political ads to support or oppose political candidates.\textsuperscript{52} If the corporation does not wish to spend openly on political ads (for example, Exxon produces and airs an ad urging voters to vote for a particular candidate for president), then the corporation can spend through an intermediary to mask its involvement in the ad’s production and funding.\textsuperscript{53} Typically, the intermediary is a nonprofit organized under §501(c)(4) or §501(c)(6) of the Internal Revenue Code.\textsuperscript{54} These nonprofit organizations do not


\textsuperscript{50} Citizens United, 558 U.S. at 320 (“Before the Bipartisan Campaign Reform Act of 2002 (BCRA), federal law prohibited—and still does prohibit—corporations and unions from using general treasury funds to make direct contributions to candidates or independent expenditures that expressly advocate the election or defeat of a candidate, through any form of media, in connection with certain qualified federal elections.”).

\textsuperscript{51} Cal. Med. Ass’n v. FEC, 453 U.S. 182, 201 (1981) (plurality opinion) (“[T]he $5,000 limitation on the amount that persons may contribute to multicandidate political committees violates neither the First nor the Fifth Amendment.”).

\textsuperscript{52} Craig Holman, The Tension Between Lobbying and Campaign Finance Laws: Rolling Back Gains Made Under the Honest Leadership and Open Government Act of 2007, 13 ELECTION L.J. 45, 56–57 (2014) (“[C]orporations (and, by implication, labor unions) [were] given First Amendment rights to spend unlimited corporate treasury funds in federal, state, and judicial elections.”).

\textsuperscript{53} Richard Briffault, Nonprofits and Disclosure in the Wake of Citizens United, 10 ELECTION L.J. 337 (2011) (“Given the anecdotal evidence that many business corporations interested in electoral activity are reluctant to do so directly and publicly and prefer to channel their money through intermediary organizations, nonprofit (c)(4)s and (c)(6)s in the post-Citizens United regime play a key role as vehicles for collecting, pooling, and spending business corporation funds to influence elections.”).

\textsuperscript{54} 26 U.S.C.A. § 501(c)(4) (West 2014) (“Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes.”); § 501(c)(6) (“Business leagues, chambers of commerce, real-estate boards, boards of trade, or professional football leagues (whether or not administering a pension fund for football players), not organized for profit and no part of the
have to disclose their underlying donors to the public under most circumstances.\footnote{Ciara Torres-Spelliscy, \textit{Hiding Behind the Tax Code, the Dark Election of 2010 and Why Tax-Exempt Entities Should Be Subject to Robust Federal Campaign Finance Disclosure Laws}, 16 NEXUS: CHAP. J. L. \\& POL'Y 59, 92 (2011) [hereinafter Torres-Spelliscy, \textit{Hiding Behind the Tax Code}] ("Much of this undisclosed spending was done through 501(c)(4)s and 501(c)(6)s."); Briffault, supra note 53, at 338 ("[M]ultiple individuals, multiple corporations, or multiple corporations and individuals may, without monetary limit, pool their funds in nonprofit organizations that finance independent expenditures—and, of course, those independent expenditures may not be subject to a monetary limit either.").}

Hence, when a corporation spends through an opaque and politically active nonprofit, the public viewing the ad cannot discern the true source of the money.\footnote{Pub. Citizen, 12 Months After: The Effects of \textit{Citizens United} on Elections and the Integrity of the Legislative Process 12 (2011), available at http://www.citizen.org/documents/Citizens-United-20110113.pdf (finding that groups that did not provide any information about their sources of money collectively spent $135.6 million, 46.1 percent of the total spent by outside groups during the [2010] election cycle.); Blair Bowie \\& Adam Lioz, Demos, Billion-Dollar Democracy: The Unprecedented Role of Money in the 2012 Elections 5 (2013), available at http://www.demos.org/sites/default/files/publications/BillionDollarDemocracy_Demos.pdf ("For the 2012 election cycle, 31\% of all reported outside spending was \textquote{secret spending},\footnote{Brief of the Center for Political Accountability and the Carol and Lawrence Zicklin Center For Business Ethics Research as Amici Curiae in Support of Appellee at 13, Citizens United v. FEC, 558 U.S. 310 (2010) (No. 08-205), 2009 WL 2349016 at *13 [hereinafter Zicklin Center Amicus Brief] (responding to the appellant\'s brief noting \textquote{shareholders can exercise their important oversight function only if they are aware of the corporation\'s political activities. Eliminating disclosure requirements is tantamount to asking shareholders to conduct oversight while blindfolded}.

58. See Liz Kennedy, Citizens Actually United: The Bi-Partisan Opposition to Corporate Political Spending and Support for Common Sense Reform, DEMOS (Oct. 25, 2012), http://www.demos.org/publication/citizens-actually-united-bi-partisan-opposition-corporate-political-spending-and-support (citing a 2012 poll by Bannon showing that 81 percent of Americans agree that companies should only spend money on political campaigns if they disclose their spending immediately.).

these concurrent broad social interests, the corporate, tax, and campaign finance laws and regulations have largely lagged behind the post-2010 ability of corporations to spend in politics, frustrating investors who seek this basic knowledge.60 For example, at the time of this writing, four years after Citizens United, Congress has failed to pass a single piece of legislation to address the decision;61 nor has the Federal Election Commission (FEC) promulgated a single Citizens United regulation on disclosure.62

Further compounding the problem, 2010 witnessed the advent of new forceful players on the political battlefield: Super PACs. Super PACs are entities that can aggregate unlimited money from unlimited sources, so long as they exclude money from foreign nationals.63 Super PACs arose out of the D.C. Circuit’s decision in SpeechNow.org v. FEC,64 which relied heavily on the reasoning in Citizens United. In the

http://www.brennancenter.org/sites/default/files/legacy/publications/shareholdersvoice2_5_10.pdf (arguing for shareholder disclosure and consent); Taub, supra note 42, at 450 (proposing that “disclosure and consent should travel down the full intermediation chain where ultimate investors can see and sanction or oppose corporate political spending”); Comment Letter from Jack Bogle, Pres., Bogle Fin. Mkts. Research. Ctr., to Ms. Elizabeth M. Murphy, Sec’y, U.S. Sec. & Exch. Comm’n (Jan. 17, 2012), available at http://www.sec.gov/comments/4-637/4637-22.pdf (“I urge the Commission to stand back for a moment from the issue of full disclosure of corporate contributions to decide whether corporate shareholders should not first decide whether a corporation should make any political contribution whatsoever without the approval of its shareholders.”).

60. Brief for AARP, et al. as Amici Curiae Supporting Respondents at 13, Am. Tradition P’ship, Inc. v. Bullock, 132 S. Ct. 2490 (2012), (No. 11-1179), 2012 WL 1853623 at *13 (“Corporations have clear incentives to avoid disclosure and accountability; federal tax and campaign finance laws, as well as state campaign finance laws, have accommodated their desire to do so.”); Torres-Spelliscy, supra note 55, at 77–86.

61. R. SAM GARRETT, CONG. RESEARCH SERV., SUPER PACS IN FEDERAL ELECTIONS: OVERVIEW AND ISSUES FOR CONGRESS 24–25, (2013), available at http://www.fas.org/sgp/crs/misc/R42042.pdf (noting “a policy question for Congress may be whether the implications of the current reporting requirements represent ‘loopholes’ that should be closed or whether existing requirements are sufficient”); but see Jeremy Miller, The DISCLOSE Act, Yet Again No Profiles in Courage, CITIZENS FOR RESPONSIBILITY & ETHICS IN WASHINGTON (July 17, 2012), http://www.citizensforethics.org/blog/no-profiles-in-courage-us-senate-rejects-disclose-act (noting the multiple failed attempts to pass the DISCLOSE Act—legislation which would have brought more transparency to political spending post-Citizens United).


63. ANTHONY CORRADO, COMM. FOR ECON. DEV., HIDING IN PLAIN SIGHT: THE PROBLEM OF TRANSPARENCY IN POLITICAL FINANCE 7 (2013), available at http://www.ced.org/pdf/Hiding_in_Plain_Sight_July_2013.pdf, [hereinafter CORRADO, IN PLAIN SIGHT]. (“Intermediary groups can serve as vehicles for masking the actual donors funding campaign related expenditures. They can function as pass throughs to veil contributions from public view.”).

64. 599 F.3d 686, 697 (D.C. Cir. 2010), cert. denied, 131 S. Ct. 553 (2010) (holding that an FEC provision limiting contributions by individuals to political committees that made only
2012 election, Super PACs raised $828,224,595, including at least some dark money. Thus, although Super PACs themselves are transparent because they are legally required to disclose their donors to the FEC, there is no requirement that the entities that give to Super PACs be similarly transparent. To the extent this money originates from corporate treasuries, this poses a potential problem for investors as scholars have strongly contested the utility of this nonmarket strategy.

Corporations have many stakeholders. These include shareholders, employees, the community, the environment, and even

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67. GARRETT, supra note 61, at 24–25 (noting “[i]n particular, relationships between super PACs and possibly related entities, such as 527 and 501(c) organizations, generally cannot be widely or reliably established based on current reporting requirements[,]”).

68. See 26 U.S.C.A. § 501(c)(4) (West 2014); § 501(c)(6).

69. Michael Hadani, Institutional Ownership Monitoring and Corporate Political Activity: Governance Implications, 65 J. OF BUS. RES. 944, 948 (2012) (“It was also argued that the largest institutional investor will likely oppose CPA [Corporate Political Activity], not only given the covert nature of CPA, but also given the fact that their money may be used for political speech which they may oppose.”). See also John C. Coates, IV, Corporate Politics, Governance, and Value Before and After Citizens United, 9 J. EMPIRICAL LEGAL STUD. 657, 691 (2012) [hereinafter Coates, Corporate Politics] (“Without disclosure reforms, the fact and extent of political activity will remain only partly revealed, with past and prospective investors having to infer the condition of the corporate patient from superficial and often misleading features, such as short-term recent stock-price performance, of the kind that lulled investors into thinking that all was well with Enron and Lehman Brothers until it was too late for them to do anything . . . .”); see also John Coates, Can Shareholders Save Democracy, Remarks at the Accountability After Citizens United Symposium (Apr. 29, 2011), available at http://www.brennancenter.org/content/pages/accountability_after_citizens_united (“Citizens United now means we’ve got a whole new avenue to reinforce the power that corporations have had already through lobbying and through PAC activity, to expand the influence of those two others and to have an additional weapon. And so I think this is only going to get worse over time. I think that shareholders are going to find themselves more and more frequently in conflict with management over this.”). For further scholarly examples of this debate over the utility of corporate political spending, see Rajesh Aggarwal, Felix Meschke, & Tracy Wang, Corporate Political Donations: Investment or Agency?, 14 BUS. & POL., vol. 1, art. 3 (Apr. 2012); Andre Douglas Pond Cummings, Procur[ing “Justice”? Citizens United, Caperton, and Partisan Judicial Elections, 95 IOWA L. REV. BULL. 89, 109 (2010) (“There is little evidence to suggest that these executives will be careful, thoughtful, or responsible with the new ability to spend shareholder funds at their disposal.”).

70. David G. Yosifon, Discourse Norms as Default Rules: Structuring Corporate Speech to Multiple Stakeholders, 21 HEALTH MATRIX 189, 212 (2011) (proposing “an alteration in the discourse norms that govern the firm’s relationship with different stakeholders”).
governments. Here we suggest that, among a corporation’s stakeholders, its shareholders should be most concerned with the cost of corporate political spending and potential new compliance costs that go with it. Shareholders bear the cost of corporate political spending by indirectly subsidizing it through their investments. And similarly, shareholders would bear the indirect costs of compliance with any new disclosure rules.

On the other hand, shareholders may benefit from disclosure rules through added transparency and improved internal controls of political spending once the company implements a system to comply with new rules. Such disclosure should translate to reduced monitoring costs from the shareholder perspective as well.


72. Bebchuk & Jackson, supra note 59, at 97–101 (highlighting the importance of shareholders with respect to corporate political spending); Katharine V. Jackson, Towards a Stakeholder-Shareholder Theory of Corporate Governance: A Comparative Analysis, 7 Hastings Bus. L.J. 309, 312 (2011) (arguing that “the empowerment of stakeholder investors presents the only currently viable means for stakeholders to influence the behavior of the American public corporation”).

73. Sabina Bunt Thaler, Citizens United and Forced Speech: Why Protecting the Dissenting Shareholder Necessitates Disclosure of Corporate Political Expenditures After Citizens United v. FEC, 17 Wash. & Lee J. Civil Rts. & Soc. Just. 591, 622 (2011) (“[S]hareholders are contributing money to a cause from which they expect to realize some benefit. Consequently, shareholders are purchasing a stake in a corporation. . . . Corporations then use shareholders’ money to run the business. Therefore, when corporations spend money on political or ideological electioneering, they are . . . spending their contributor’s money.”).

74. Zicklin Center Amicus Brief, supra note 57, at 17 (“The views of [public corporations and managers] do not mirror those of shareholders and employees, who often represent a diverse cross-section of the public. Though many individual shareholders and directors vocally oppose questionable uses of corporate funds, they lack the means to significantly influence corporate political spending decisions.”).

75. See Coates, Corporate Politics, supra note 40, at 690 (“If Congress, states, or the SEC adopt rules attempting to give shareholders more information or more authority in the political sphere, the evidence presented here should help demonstrate that such legislation serves as a legitimate and compelling purpose separate from the anti-corruption and other purposes that have traditionally justified campaign finance laws.”).

Political spending by corporations heightens the agency problem inherent between shareholders and managers acting ostensibly on shareholders’ behalf because current disclosure rules do not allow shareholders to monitor how corporate managers spend corporate assets on political causes.\(^{77}\) Harvard Professor John Coates has noted that publicly-traded corporations’ political spending raises risks for firms:

At a minimum, it should be clear that political activity creates distinct and difficult-to-model risks. Dozens of studies . . . support the view that political activity can harm shareholder interests. These harms can flow through many channels—from reputational harm to dilution of strategic focus, from politically risky acquisition bets or capital investments to state laws deterring takeovers. To adequately assess those risks, shareholders need basic, standardized information about political activity—before investing, and afterwards, to monitor corporate performance and make informed decisions. Disclosure of such information is squarely within the SEC’s charge, which has long included disclosure of information under Rule 14a-8 relating to social and political issues of general public interest, under executive compensation disclosure requirements that bear on management conflicts of interest that would not directly have a material impact on firm value, and under the FCPA relating to corporate connections to foreign political officials. Disclosure of political activity would deliver significant benefits to investors at a low cost.\(^{78}\)

The Committee for Economic Development (CED), a group of CEOs and other business executives, agrees with Professor Coates’s assessment. In a recently released report, the CED concluded “[p]olitical activity also exposes companies to substantial reputational and legal risks that endanger enterprise and shareholder value. These risks are particularly pronounced in the case of contributions made to third party groups where the donor does not exercise control over the ways that funds are spent.”\(^{79}\)

\(^{77}\) Id. at 4 (“In the [corporate political activity] context, there is considerable potential for personal advantages to corporate executives, particularly prestige, a future political career, and star power . . . or to help political allies . . . .” (citations omitted)).

\(^{78}\) Coates, Non-Decision, supra note 26.

The CED has urged across-the-board transparency for political spending, regardless of the source, arguing “[a]ny organization that spends money advocating candidates or paying for other electioneering activities—whether a political committee, tax-exempt 501(c) organization, or for-profit corporation—should publicly disclose the sources of the funding used to finance these expenditures.” 80

Another recent study, published by the Mercatus Center, reaches similar conclusions.81

Glass Lewis, a leading proxy advisory service, has also noted that corporate political spending is accompanied by reputational risks.

As the line between candidate ads and issue ads has blurred, companies that have donated to some of these groups may face significant reputational risks. While these organizations may be funded through soft money or may legally not be required to disclose their donors, questionable actions on behalf of these groups could cause the release of information regarding their donors. For example, in November 2012, a Montana judge allowed the release of the bank records of the Western Tradition Partnership . . ., a 501(c)(4) organization that had been extensively involved in the recent Montana elections.82

Further, the Conference Board’s Committee on Corporate Political Spending, a business research group, wrote in a 2011 report:

Corporate political contributions are subject to a highly complex web of federal, state and local laws and regulations. Failure to comply can lead to costly lawsuits, civil or criminal charges, and consequent damage to a company’s image and reputation. Corporate political activities are closely scrutinized by public-interest groups and the media. As a result, a corporation’s direct or indirect political spending can put its reputation at risk and could adversely affect its business if the company takes a controversial position or supports a candidate who holds positions that are

80. CORRADO, IN PLAIN SIGHT, supra note 63, at 8.
inconsistent with its corporate values or the views of a significant number of its workers, shareholders or customers.\textsuperscript{83}

Transparency is necessary so that investors can properly weigh these risks before investing.\textsuperscript{84}

III. COST-BENEFIT ANALYSIS: THE LOOMING OBSTACLE TO A NEW SEC RULE ON CORPORATE POLITICAL SPENDING

The open question for policy makers today is how to deal with corporate political spending.\textsuperscript{85} Because other academic papers have dealt with the constitutionality of and various policy questions surrounding disclosure of corporate political spending,\textsuperscript{86} this article addresses the thorny administrative law issue of an agency’s cost-benefit analysis in light of the D.C. Circuit’s inevitable review.\textsuperscript{87} The cost-benefit calculus for SEC disclosures and other regulations is not just an economic matter for regulated companies; increasingly it is a legal matter for the SEC, which is subject to a seemingly endless parade of lawsuits over its rulemaking in the powerful D.C. Circuit.\textsuperscript{88}


\textsuperscript{84} William Alan Nelson, II, Post-Citizens United: Using Shareholder Derivative Claims of Corporate Waste to Challenge Corporate Independent Political Expenditures, 13 Nev. L.J. 134, 167 (2012) (“Corporations can decrease the risk of facing a shareholder derivative complaint by improving the transparency of independent political expenditures and improving policies governing those expenditures. Corporations should have a stated policy for political spending and also a committee that can monitor the political expenditure program.”).

\textsuperscript{85} See Robert Sprague & Mary Ellen Wells, The Supreme Court As Prometheus: Breathing Life into the Corporate Supercitizen, 49 Am. Bus. L.J. 507, 553 (2012) (calling on Congress to “strengthen disclaimer and disclosure requirements”). For various legislative efforts addressing this question, see Iowa Senate File 2354, signed by Governor Chester Culver, April 8, 2010; MD Elec. Law §§ 13–306 and 307, and the statutes cited supra note 36.

\textsuperscript{86} Bebchuk & Jackson, supra note 2, at 954 (highlighting the possibility of First Amendment consequences for the mandatory disclosure of corporate political spending); Torres-Spelliscy, supra note 49, at 411 (discussing political corporate spending post-Citizens United).


\textsuperscript{88} Brad Plumer, The D.C. Circuit is the Court at the Center of the Filibuster Fight. Here’s Why it Matters., WASH. POST (Nov. 21, 2013), http://www.washingtonpost.com/blogs/
The SEC is just one of many regulators that has a claim on regulating corporate money in politics. Now that corporations can spend directly on political ads in all American federal and state elections, the Federal Communications Commission (FCC), the FEC, the SEC, and the Internal Revenue Service (IRS) all have potential jurisdiction.\(^89\) Moreover, a corporation’s spending on state elections implicates state election laws.\(^90\) If corporations use nonprofits as conduits, states may try to regulate this behavior through their charity bureaus just as New York State did in 2013.\(^91\) For the purposes of this

\(^89\) Lucian A. Bebchuk & Robert J. Jackson, Jr., \textit{SEC to Propose Rules on Corporate Political Spending by April 2013}, \textit{Harvard L. Sch. F. On Corp. Governance & Fin. Reg.} (Jan. 9, 2013, 9:30 AM), http://blogs.law.harvard.edu/corpgov/2013/01/09/sec-to-propose-rules-on-corporate-political-spending-by-april-2013/ (articulating that “[t]he Securities and Exchange Commission recently updated its entry in the Office of Management and Budget’s Unified Agenda to indicate that, by April, it plans to issue a Notice of Proposed Rulemaking on requiring public companies to disclose their spending on politics”); Jacob Fenton, \textit{Political Advertisers and TV Stations Ignore Disclosure Rules}, \textit{Sunlight Found.} (Dec. 18, 2013), http://sunlightfoundation.com/blog/2013/12/18/political-advertisers-and-tv-stations-ignore-disclosure-rules (“The most widely-used disclosure form allows [TV] advertisers to check a box saying whether the ads are national or local; additional disclosures are only required for advertisements that are national in scope. The most common response is to leave both boxes blank.”); Robert Kelner, \textit{Is Increased Criminal Enforcement of Election Laws on the Way Because the FEC and DOJ Are Making Nice-Nice?}, \textit{Inside Pol. L.} (July 18, 2012), http://www.insidepoliticallaw.com/2012/07/18/is-increased-criminal-enforcement-of-election-laws-on-the-way-because-the-fec-and-doj-are-making-nice-nice/.\(^90\) For an analysis of how state election laws are implicated, see Ciara Torres-Spelliscy, \textit{Brennan Ctr. for Justice, Transparent Elections After Citizens United} 6 (2011), \textit{available at} https://www.brennancenter.org/sites/default/files/legacy/Disclosure%20in%20the%20States.pdf (“Before \textit{Citizens United}, 24 states barred either union or corporate political expenditures. \textit{Citizens United} rendered these laws unconstitutional. Consequently, corporations and unions have a new right to spend in states where they were previously barred. Therefore, in approximately half of the states, the number of entities that could potentially fund future political ads has jumped significantly, while transparency is on the wane.”).\(^91\) Susan E. Golden, et al., \textit{New York Nonprofit Revitalization Act Signed Into Law, Venable LLP & Minority Corp. Counsel Ass’n}, (Dec. 20, 2013), http://www.mondaq.com/unitedstates/x/282420/Charities+Non-Profits/New+York+Nonprofit+Revitalization+Act+Signed+into+Law (“Its provisions apply to nonprofits that are incorporated in New York, but one significant section—related to financial audits and financial reporting to the state—applies to all nonprofits that are registered in New York for charitable solicitation
article, we focus on the potential regulatory role of the SEC because it is the lead regulator of publicly traded corporations in the United States.92

The D.C. Circuit,93 as the court responsible for reviewing the rules promulgated by federal agencies including the SEC, has become increasingly hostile to novel approaches to business regulations.94 Two common justifications the D.C. Circuit has given for why a particular SEC regulation is inappropriate are: (1) that the SEC did not conduct a sufficient cost-benefit analysis; and (2) that the regulation did not

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94. Bus. Roundtable v. SEC, 647 F.3d 1144, 1154–55 (D.C. Cir. 2011) (ruling the SEC was arbitrary and capricious in promulgating Rule 14a–11, requiring public companies to provide shareholders with information about, and their ability to vote for, shareholder-nominated candidates for the board of directors, and is vacated); Am. Equity Inv. Life Ins. Co. v. SEC, 613 F.3d 166, 177–79 (D.C. Cir. 2009) (finding that a rule exempted federal annuity contracts issued by a corporation and subject to regulation by state insurance laws from federal regulation through the Securities Act of 1933; SEC failed to properly consider the effect of the rule upon efficiency, competition, and capital formation, rule vacated); Fin. Planning Ass’n v. SEC, 482 F.3d 481, 492–93 (D.C. Cir. 2007) (ruling SEC rule exempting certain broker-dealers from Investment Advisers Act (IAA), even if they received special compensation exceeds SEC authority and is vacated); Goldstein v. SEC, 451 F.3d 873, 877–78 (D.C. Cir. 2006) (holding that rule requiring that investors in a hedge fund be counted as clients of the fund’s adviser for purposes of fewer-than-fifteen-clients exemption from registration under IAA was invalid as conflicting with purposes underlying the statute); Bus. Roundtable v. SEC, 905 F. 2d 406, 407 (D.C. Cir. 1990) (holding that SEC exceeded its statutory authority in promulgating rule barring national security exchanges and associations from listing stock of corporations which nullify, restrict or disparately reduce per share voting rights of common, rule vacated); Am. Bankers Ass’n v. SEC, 804 F.2d 739, 755–56 (D.C. Cir. 1986) (ruling SEC rule 3b-9, which requires banks engaging in securities brokerage business for profit to register as broker-dealers under Securities Exchange Act of 1934, is invalid); see also Gordon, supra note 10, at 14 (“the various recent decisions of D.C. Circuit Court of Appeals striking down SEC rules on purported BCA grounds are far more intelligible on a different principle: the Court’s resistance to the SEC’s expansion of its rule-making in areas traditionally dominated by state law.”).
further the SEC’s interest in fostering an efficient market for securities. In an SEC cost-benefit analysis, a regulation’s benefits are intrinsically linked to their effect on the stock market. If the D.C. Circuit is not satisfied that a robust cost-benefit analysis was performed, or that the rule does not further market efficiency, then either reason could be used by a panel of the court inclined to invalidate the rule to do so.

The D.C. Circuit’s approach to cost-benefit analysis has been strongly criticized by many academics, including Professor Coates. Professor Coates wrote, in response to the decision in Business Roundtable v. SEC that, “[t]he D.C. Circuit presented no evidence that there is any available scientific technique for the SEC to ‘assess the economic effects’ of the [SEC’s] rule along the lines that the court

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96. David S. Ruder, Balancing Investor Protection with Capital Formation Needs after the SEC Chamber of Commerce Case, 26 PACE L. REV. 39, 56 (2005) (“The SEC . . . quantified the benefits of the Order Protection Rule. It expressed its belief that although the rule’s price protections of New York Stock Exchange . . . and NASDAQ . . . stocks are ‘difficult to quantify,’ benefits will be substantial.”); Sherwin, supra note 88, at 47 (“Undoubtedly, quantification of costs and benefits, where possible, is one of the most crucial aspects of cost-benefit analysis.”).
97. Bus. Roundtable, 647 F.3d at 1153 (“In weighing the rule’s costs and benefits, however, the Commission arbitrarily ignored the effect of the final rule upon the total number of election contests.”).
98. 15 U.S.C.A. § 77b(b) (West 2014) (“Whenever . . . the Commission is engaged in rulemaking and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.”); Recent Case Commentary, Administrative Law- Corporate Governance Regulation-D.C. Circuit Finds Sec Proxy Access Rule Arbitrary and Capricious for Inadequate Economic Analysis-Business Roundtable v. SEC, 647 F.3d 1144 (D.C. Cir. 2011), 125 HARV. L. REV. 1088, 1089 (2012) (“The [SEC] explained that Rule 14a-11 would increase corporate performance and argued that any costs of the rule were a necessary consequence of enforcing traditional state law rights.”). Cost-benefit analysis is also required of the Office of Management & Budget (OMB) which must report the costs and benefits of federal regulations to Congress on an annual basis. See Exec. Order No. 12,866, 3 C.F.R. 638 (1994), reprinted as amended in 5 U.S.C.A., § 601 app. at 86–91 (West 2014).
99. Fisch, supra note 11, at 712 (“[E]mpirical analysis of proposed rulemaking has obvious limitations. It is difficult to predict the effect that a new rule will have . . . [E]mpirical analysis frequently requires regulators to extrapolate from transactions that are not comparable to those that are contemplated under the proposal. Thus the reliability of empirical evidence… is questionable.”) (citations omitted); James D. Cox & Benjamin J. C. Baucom, The Emperor Has No Clothes: Confronting the DC Circuit’s Usurpation of SEC Rulemaking Authority 3 (Mar. 4, 2012) (unpublished manuscript), available at http://ssrn.com/abstract=2016433 (“What we report here is that the level of review invoked by the D.C. Circuit in Business Roundtable and its earlier decisions is dramatically inconsistent with the standard enacted by Congress. Our conclusion is that it is the D.C. Circuit has assumed for itself a role that is opposed to the one Congress prescribed for courts reviewing SEC rules.”).
seemed to think legally required . . . ." While the D.C. Circuit’s rulings can be appealed to the Supreme Court, the high court is under no obligation to hear the appeal, and takes a relatively small number of regulatory cases each year. This can leave the D.C. Circuit with the final word on the fates of many administrative rules.

A. The SEC & Cost-Benefit Analysis

Cost-benefit analyses have proven to be the Achilles heel of the SEC’s regulatory power. The D.C. Circuit pointed to an allegedly faulty cost-benefit analysis in invalidating a SEC rule in 2005’s Chamber of Commerce of the United States of America v. SEC. As the court explained:

Uncertainty may limit what the Commission can do, but it does not excuse the Commission from its statutory obligation to do what it can to apprise itself—and hence the public and the Congress—of the economic consequences of a proposed regulation before it decides whether to adopt the measure.

And the Court has continued to build on this precedent. For example, in 2011’s Business Roundtable decision, the D.C. Circuit undid the SEC's Dodd-Frank proxy access rule (which would have allowed shareholders to nominate directors for inclusion on the corporate ballot) in part because the Court held that there had not been a robust cost-benefit analysis. Some subsequent economic

100. Coates, Cost-Benefit Analysis of Financial Regulation, supra note 9, at 29 (citing Bus. Roundtable, 647 F.3d at 1154).
102. Pete Schenkkan, Texas Administrative Law: Trials, Triumphs, and New Challenges, 7 TEX. TECH ADMN. L.J. 287, 341 (2006) (“The administrative law part of the federal court burden is spread widely around the country, all district judges and all circuits. Only the D.C. Circuit and D.C. District Courts see more than a pro rata share of administrative law cases . . . .”).
103. Chamber of Commerce of the U.S. v. SEC, 412 F.3d 133, 136 (D.C. Cir. 2005) (“We agree with the Chamber, however, that the Commission did violate the APA by failing adequately to consider the costs mutual funds would incur in order to comply with the conditions and by failing adequately to consider a proposed alternative to the independent chairman condition.”).
104. Id. at 144; see also Coates, Cost-Benefit Analysis of Financial Regulation, supra note 9, at 7 (citing Chamber of Commerce, 412 F.3d at 144) (“[T]he D.C. Circuit held that the SEC acted arbitrarily and capriciously for failing to undertake some effort to quantify the costs of the mutual fund governance rule changes it had adopted.”).
105. 647 F.3d 1144 (D.C. Cir. 2011).
106. George W. Dent, Jr., Corporate Governance: The Swedish Solution, 64 FLA. L. REV.
analysis seems to indicate that the D.C. Circuit was wrong in its assumptions about the costliness of proxy access.107 But right or wrong, they invalidated the proxy access rule.108 As Bruce Kraus explains, “[c]ost-benefit litigation has substantially slowed the pace of financial reform, and new cost-benefit legislation looms.”109

Claims of insufficient cost-benefit analysis have been raised in other recent challenges. In American Petroleum Institute (API) v. SEC,110 the U.S. Chamber of Commerce and other plaintiffs sued over the SEC rule implementing Dodd-Frank section 1504, arguing the rule was arbitrary and capricious, had a flawed cost-benefit analysis, and violated the First Amendment.111 This rule would have required extractive industries to report payments to foreign governments.112
Notably, in *API*, the D.C. district court held, “[a]s the Supreme Court has recognized, ‘no legislation pursues its purposes at all costs.’”\(^{113}\) After the D.C. Circuit held it did not have jurisdiction, the district court invalidated the extractive industries reporting requirements.\(^{114}\)

Finally, cost-benefit analysis also arose in the D.C. Circuit’s handling of a challenge to the SEC’s Dodd-Frank conflict mineral mining disclosure rule,\(^{115}\) which requires listed firms to inform the public whether their products contain conflict minerals from the Democratic Republic of Congo and surrounding countries.\(^{116}\) The Court upheld the SEC’s cost-benefit analysis finding that doing a thoughtful analysis was particularly challenging in this circumstance:

> An agency is not required “to measure the immeasurable,” and need not conduct a “rigorous, quantitative economic analysis” unless the statute explicitly directs it to do so. Here, the rule’s benefits would occur half-a-world away in the midst of an opaque conflict about which little reliable information exists, and concern a subject about which the Commission has no particular expertise. Even if one could estimate how many lives are saved or rapes prevented as a direct result of the final rule, doing so would be pointless because the costs of the rule—measured in dollars—would create an *apples-to-bricks* comparison.\(^{117}\)

In this case, the D.C. Circuit made a more judicious application of cost-benefit analysis requirement, but only time will tell whether the more forgiving conflict minerals approach to cost-benefit will become the majority rule in the Circuit.\(^{118}\)


\(^{116}\) *Nat’l Assoc’n of Mfrs. v. SEC*, 748 F.3d 359, 368–69 (D.C. Cir. 2014). The Appellee challenged that the Conflict Minerals rule was arbitrary and capricious because the SEC’s cost-benefit analysis failed to determine whether the rule would achieve its intended benefits. *Id.* at 369. The court responded, however, that these benefits were largely qualitative and immeasurable and that the agency was not required do the “impossible.” *Id.* at 370 (quoting *Inv. Co. Inst. v. Commodity Futures Trading Comm’n*, 720 F.3d 379 (D.C. Cir. 2013)). Despite data that did not lend itself to a CBA, the court nevertheless found the SEC’s analysis valid because it was the best that could be expected and the SEC was required to promulgate the rule. *Id.* at 369–70.

\(^{117}\) *Id.* at 369 (internal citations omitted) (emphasis added).

\(^{118}\) Matthew C. Baltay, Dean F. Hanley, & Paul Bork, *Federal Appeals Court Largely*
B. APA’s Arbitrary and Capricious Standard in the D.C. Circuit

As a separate issue, the Administrative Procedure Act (APA) allows a cause of action when any promulgated rule is “arbitrary and capricious.” The Supreme Court has provided some guidance about what constitutes arbitrary or capricious rulemaking. According to the Supreme Court’s Motor Vehicle Manufacturers Association v. State Farm Mutual Automobile, to defeat an arbitrary and capricious challenge, the agency must show that its reasoning in adopting a rule indicated a “rational connection between the facts found and the choice made.”

The D.C. Circuit applies the APA when analyzing the suitability of rules and regulations from federal administrative agencies. As the Court recently explained, “[w]e review the analysis under the statutory standard set by the Administrative Procedure Act . . . . The APA requires the court to set aside agency action that is ‘arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.’”

In 2010 in American Equity Investment Life Ins. Co. v. SEC, the D.C. Circuit applied this standard in vacating SEC rule 151A, which would have regulated indexed annuities as securities rather than insurance products, holding that the SEC’s consideration of the rule’s promotion of efficiency, capital formation, and competition was inadequate. Specifically, the SEC argued that this rule would increase competition and efficiency by introducing “clarity” in an “uncertain area of law.” But the court noted this could be said for...

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120. See, e.g., Motor Vehicle Mnfrs. Ass’n v. State Farm Mut. Auto. Ins. Co., 463 U.S. 29, 43 (1983) (“The scope of review under the “arbitrary and capricious” standard is narrow and a court is not to substitute its judgment for that of the agency. Nevertheless, the agency must examine the relevant data and articulate a satisfactory explanation for its action including a ‘rational connection between the facts found and the choice made.’”).
121. Id.
124. 613 F.3d 166, 179 (D.C. Cir. 2010).
125. Id. at 178.
126. Id.
any rule adopted by the SEC, and the reasons given for adopting this particular rule were no better than adopting any other rule.\footnote{127}

The court held that this defect rendered the SEC’s purported considerations of other components of the analysis similarly flawed: “[T]he SEC’s flawed efficiency analysis also renders its capital formation analysis arbitrary and capricious. The SEC’s conclusion that rule 151A would promote capital formation was based significantly on the flawed presumption that the enhanced investor protections under rule 151A would increase market efficiency.”\footnote{128}

So whether it is the cost-benefit analysis or the APA’s arbitrary and capricious standard, the SEC must navigate a potential minefield of judicial objections to new rules in the D.C. Circuit. To the extent that the D.C. Circuit’s hostility is motivated by an assumption that markets are “burdened” by every type of regulation, our data sets provide empirical evidence to the contrary.

IV. OUR DATASETS

Corporations’ ability to spend in politics post-	extit{Citizens United} raises a host of potential corporate governance problems. Because there is no SEC rule requiring disclosure of such spending to shareholders, and because a new rule would likely be reviewed by a hostile D.C. Circuit, there is a clear need for concrete data on the overall effects of disclosure requirements.\footnote{129}

Our data help illuminate who has the stronger argument in the broader debate over whether disclosure, and other securities regulations, are beneficial to markets. Since there is no present SEC political disclosure rule, we could not measure direct future compliance costs.\footnote{130} Instead, we gauged the market’s reaction to other

\footnotesize{127. Id.} 
\footnotesize{128. Id. at 179.} 
\footnotesize{129. James Kwak, \textit{Corporate Law Constraints on Political Spending}, 18 N.C. BANKING INST. 251, 253 (2013) (“Governance of corporate political activity has become particularly salient since the Supreme Court’s 2010 decision in \textit{Citizens United v. Federal Election Commission}, which . . . made possible unlimited corporate contributions to ‘independent expenditure committees’ that do not contribute to or coordinate their activities with political candidates.”); Stephen A. Yoder, \textit{Legislative Intervention in Corporate Governance Is Not A Necessary Response to \textit{Citizens United} v. Federal Election Commission}, 29 J.L. & COM. 1, 10 (2010) (‘\textit{Citizens United} itself involved a narrower definition of corporate governance; the relationship between a corporation and its shareholders. Specifically, the case raises the issues of whether shareholders should have a say in how their corporations spend corporate funds in the political process . . .’

\footnotesize{130. Disclosure Comm. Petition, supra note 5, at 7–8.}}
analogous securities regulations. Specifically, we offer our analysis of the market’s reaction to two divergent approaches to regulation:\(^{131}\) one that increased the regulation of listed companies, SOX, and one that reduced certain regulation of smaller listed companies, the JOBS Act.\(^{132}\) Through careful examination, our data reinforce the notion that the market values transparency.

This analysis contributes to the debate in two respects. First, using the stock market as a central place for market participants to exchange and aggregate information, we demonstrate what investors collectively perceive to be the net benefits (or costs) of enhanced (or reduced) disclosure requirements. A net positive indicates that the market welcomes the news of the new rules by assigning higher values to the securities affected, after considering the costs of implementation. Second, we believe that market efficiency, defined by Fama and others\(^{133}\) as how quickly the market incorporates the arrival of new information, or by Tobin\(^{134}\) as how efficiently the market


\(^{134}\) See generally ANDREW W. LO, *MARKET EFFICIENCY: STOCK MARKET BEHAVIOR IN THEORY AND PRACTICE*, vols. I & II, (1997); James Tobin, Sterling Prof. of Econ., Yale Univ., On the Efficiency of the Financial System, Fred Hirsch Memorial Lecture (May 15, 1984), in 153 LLOYDS BANK REV. (1984) at 2 (articulating three definitions of “market efficiency”: “first, a market is ‘efficient’ if it is on average impossible to gain from trading on the basis of generally available public information; . . . [a] second and deeper meaning is the following: a market in a financial asset is efficient if its valuations reflect accurately the future payments to which the asset gives title;” and “[t]hird, a system of financial markets is efficient if it enables economic agents to insure for themselves deliveries of goods and services in all future contingencies, either by surrendering some of their own resources now or by contracting to deliver them in specified future contingencies”).
allocates more capital to productive firms (away from unproductive ones), rests on the availability of information to broad participants in the stock markets and the quality, especially the trustworthiness, of the information. Information that can only be obtained by a selected few, or information that is incomplete or murky, on the other hand, compromises the price discovery and adjustment process, and hurts market efficiency.

A. Sarbanes-Oxley (SOX)

1. SOX Background and Data

At the turn of the twenty-first century, the U.S. securities markets suffered from a fundamental, well-nigh existential, problem—a loss of investor trust. Major companies were going bankrupt simultaneously, and the problem was rooted in basic accounting flaws. If a shareholder in a major company, for example, the energy giant Enron, could not trust the financial statements prepared by it and its “Big Four” accounting firm Arthur Andersen, then who

135. BRENT A. OLSON, 2 PUBLICLY TRADED CORPORATIONS: GOVERNANCE & REG. § 14:10 (3d ed. 2014) (“An efficient market is one in which prices reflect available information. The Third Circuit has defined an ‘efficient’ market as one where ‘information important to reasonable investors . . . is immediately incorporated into stock prices.’” (quoting In re Burlington Coat Factory Sec. Lit., 114 F.3d 1410, 1425 (3d Cir. 1997))).

136. Zachary J. Gubler, Public Choice Theory and the Private Securities Market, 91 N.C. L. REV. 745, 798 (2013) (“[L]ess efficient disclosure leads to less efficient stock prices, which in turn leads to less efficient capital allocation. The bottom line is that disappearing disclosure may result in less valuable companies and a less valuable economy.”); Fangliang Huang, Price Discovery, Competition and Market Mechanism Design, 4 ASIAN SOC. SCI., 126 (2008) (“The ill transfer of information or asymmetry of information will affect the formation of prices. The uninformed or ill-informed manufacturers or consumers will possibly form mistaken valuation of goods, which will harm the price discovery efficiency. The distorted price signal will probably cause incorrectly the tendency of production or consumption. Incomplete information may lead to two other phenomena, adverse selection and moral hazard, which will make the market less efficient.”).

137. Elisabeth Bauman, Not Business as Usual, THE NEWS HOUR (Jan. 30, 2002), http://www.pbs.org/newshour/extra/features/jan-june02/enron.html (“The collapse has made many Americans lose confidence in the stock market. If such a ‘successful’ company abuses the trust of investors, what’s to say other companies aren’t doing the same thing?”).

138. Allison Fass, One Year Later, The Impact of Sarbanes-Oxley, FORBES (July 22, 2003), http://www.forbes.com/2003/07/22/cz_af_0722sarbanes.html (“Sarbanes-Oxley was precipitated by a slew of corporate scandals, including those at Enron, Arthur Andersen, Tyco, Global Crossing and WorldCom.”).

139. The particular failures demonstrated by the actions of Enron and Arthur Andersen are explained well by Jonathan R. Macey, A Pox on Both Your Houses: Enron, Sarbanes-Oxley and the Debate Concerning the Relative Efficacy of Mandatory Versus Enabling Rules, 81 WASH. U. L.Q. 329, 355 (2003) (“Sarbanes-Oxley was a measured and appropriate response to the abject failures in U.S. corporate governance . . . . [T]he corporate governance crisis in America, with Enron as its poster child, represents a failure of both our system of mandatory rules, and of the
could the investing public trust?\textsuperscript{140} Failures in corporate governance were at the heart of these corporate scandals.\textsuperscript{141} Congress worked quickly to pass The Public Company Accounting Reform and Investor Protection Act, otherwise known as the Sarbanes-Oxley Act (SOX), in July 2002 to reassure the markets that it was safe for investors to trust the stock market again.\textsuperscript{142} SOX was subject to a constitutional challenge based on the structure of one oversight board—which was found to be constitutionally flawed—but was otherwise left intact by the federal courts.\textsuperscript{143}

SOX was a multi-dimensional piece of legislation that included reforms in corporate governance, accounting regulations, and SEC reporting.\textsuperscript{144} Sections 302 and 906 were particularly noteworthy, which contracting processes, which, together, constitute the infrastructure of the U.S. corporate governance system.”).

\textsuperscript{140.} R. Preston McAfee, The Real Lesson of Enron’s Implosion: Market Makers are In the Trust Business, 1 THE ECONOMISTS’ VOICE no. 2, art. 3, at ii, (2004) available at http://www.ovc.edu/advance/hamm/EnronImplosion.pdf (“How did Enron, a •rm worth $60 billion, collapse . . . ? Market makers like Enron and Ebay are in the ‘trust’ business, just as banks and insurance companies are. Once trust was lost, the rest of Enron’s value quickly disappeared.”).


\textsuperscript{142.} Representative Michael Oxley, one of the Sponsors of SOX, gave this description of the climate surrounding its passage:

Sarbanes-Oxley was passed during a period in which a majority of Americans had lost faith in the pillars of corporate life: company executives, public accountants, investment bankers, stock and bond analysts, and attorneys. This mistrust, I would point out, was well founded. Too many failed to act ethically. Indeed, we have learned that many violated criminal laws . . . .


\textsuperscript{144.} Robert A. Prentice & David B. Spence, Sarbanes-Oxley As Quack Corporate Governance: How Wise Is the Received Wisdom?, 95 GEO. L.J. 1843, 1909 (2007) (“[T]he strongest empirical evidence supports the conclusion that the executive certification requirements . . . have provided the capital markets with useful information that has already improved their efficiency as allocators of capital and should provide increasing benefits in the future.”); Michael W. Peregrine, Another View: Sarbanes-Oxley and the Legacy of Enron, N.Y. TIMES DEALBOOK (Nov. 25, 2011, 10:30 AM), http://dealbook.nytimes.com
required chief executive officers and chief financial officers to personally certify the accuracy of the firm’s financial statements, where failure to comply subjects corporate officers to civil or criminal penalties.\footnote{145}

Additionally, SOX section 404 tried to rebuild public trust by strengthening the internal controls that underpin the accuracy and reliability of published financial statements.\footnote{146} Section 404 sought to ensure the reliability of the financial reporting process by requiring every public company that files annual reports with the SEC to report on management’s responsibilities to establish and maintain adequate internal controls over the company financial reporting process, as well as management’s assessment of the effectiveness of those controls.\footnote{147} At the same time, section 404 required registered public accountants to attest to those statements.\footnote{148} SOX also created the Public Accounting Oversight Board (PCAOB),\footnote{149} which can require external auditors to conduct a report on management’s assessment, as well as on the effectiveness of a company’s controls.\footnote{150}

\footnote{2011/11/25/another-view-sarbanes-oxley-and-the-legacy-of-enron/?r=0 (noting that SOX included: “the Public Company Accounting Oversight Board, improving corporate financial disclosure, establishing new criminal penalties related to obstruction of justice and addressing conflicts of interest of securities analysts, among other provisions.”).}


\footnote{147. Id.}

\footnote{148. Section 404(b) of Sarbanes-Oxley Act of 2002, Am. Inst. of CPAs, http://www.aicpa.org/advocacy/issues/pages/section404bofsox.aspx (last visited Aug. 17, 2014) (“Section 404(b) requires a publicly-held company’s auditor to attest to, and report on, management’s assessment of its internal controls.”).}


\footnote{150. Public Co. Acct. Oversight Bd., About the PCAOB, http://pcaobus.org/About/Pages/default.aspx (last visited Dec. 23, 2013) (“[SOX] which created the PCAOB, required that auditors of U.S. public companies be subject to external and independent
The primary new cost attributable to SOX was that of section 404 audits. Table 1 reports audit fees per million dollars of revenue from 2002 to 2011, and the year-over-year percentage change, as calculated by Audit Analytics, a firm specializing in audit data collections, dissemination, and analysis. In 2004, the first year section 404 was implemented, the data shows an increase of nearly 50 percent in audit fees. After the initial increase, the percentages trend downward in 2006, 2007, and 2008, with an uptick in 2009 (possibly because of reduced revenue, denominator, in 2009 rather than a increased numerator), followed by a downward trend through 2010 and 2011.

Table 1: Audit Fees (USD) Per Million Dollars in Revenue with Audit Fees over Revenue Percentage Change from Year to Year (2002–2011)

<table>
<thead>
<tr>
<th>Year</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fees/$1m</td>
<td>$370</td>
<td>$405</td>
<td>$590</td>
<td>$597</td>
<td>$579</td>
</tr>
<tr>
<td>Change</td>
<td>—</td>
<td>9.47%</td>
<td>47.29%</td>
<td>0.09%</td>
<td>-2.99%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fees/$1m</td>
<td>$538</td>
<td>$533</td>
<td>$577</td>
<td>$505</td>
<td>$466</td>
</tr>
<tr>
<td>Change</td>
<td>-7.13%</td>
<td>-0.93%</td>
<td>8.41%</td>
<td>-12.52%</td>
<td>-7.75%</td>
</tr>
</tbody>
</table>

oversight for the first time in history. Previously, the profession was self-regulated.


152. See Larry E. Ribstein, Market vs. Regulatory Responses to Corporate Fraud: A Critique of the Sarbanes-Oxley Act of 2002, 28 J. CORP. L. 1, 61 (2002) (“The substantial existing regulatory framework was breached by aggressive outsiders who seemed determined to ignore the risks of their actions, including their personal exposure to punishment. Promoting more independent monitors with lower-powered incentives to scrutinize the actions of highly informed and motivated insiders cannot solve this problem.”).

153. S&P Capital IQ, Compustat Financials, McGRAW HILL FIN., https://www.capitaliq.com/home/what-we-offer/information-you-need/financials-valuation/compustat-financials.aspx (last visited July 9, 2014) (“Academic and quantitative researchers, hedge funds, and investment professionals around the world use Compustat’s unrivaled historical fundamental and market data for in-depth historical research and analysis.”). For the universe of companies covered by the Compustat database, the most comprehensive financial database on the publicly traded companies in the U.S., the average firm saw its revenue decline by 6.39 percent and the median, by 9.96 percent.

154. Don Whalen & Mark Cheffers, Audit Fees and Non-audit Fees, A Ten Year Trend, AUDIT ANALYTICS 11 (2012) (on file with author) (defining audit fees as those related to “perform the audit or review in accordance with the GAAS [Generally Accepted Auditing Standards, developed by the Public Company Accounting Oversight Board of the U.S.],” but could also include fees related to providing “comfort letters, statutory audits, attest services, consents and assistance with and review of documents filed with the SEC”.)
### Table 2: Audit Costs

<table>
<thead>
<tr>
<th>Calendar Year</th>
<th>Total Fees ($bn)</th>
<th>Total Revenue ($bn)</th>
<th>Total Fees as a % of Revenue</th>
<th>Audit Fees</th>
<th>Non-Audit Fees</th>
<th>Audit Fees per Firm</th>
<th>Non-Audit Fees per Firm</th>
<th>Median CEO Compensation</th>
<th>Median CFO Compensation</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>6,259</td>
<td>8,314</td>
<td>0.08%</td>
<td>3,073</td>
<td>3,186</td>
<td>1.23</td>
<td>1.27</td>
<td>2.86</td>
<td>1.00</td>
</tr>
<tr>
<td>2003</td>
<td>6,368</td>
<td>9,246</td>
<td>0.07%</td>
<td>3,742</td>
<td>2,626</td>
<td>1.49</td>
<td>1.05</td>
<td>2.74</td>
<td>0.98</td>
</tr>
<tr>
<td>2004</td>
<td>8,533</td>
<td>10,498</td>
<td>0.08%</td>
<td>6,258</td>
<td>2,276</td>
<td>2.50</td>
<td>0.91</td>
<td>3.26</td>
<td>1.16</td>
</tr>
<tr>
<td>2005</td>
<td>8,851</td>
<td>11,732</td>
<td>0.08%</td>
<td>7,000</td>
<td>1,851</td>
<td>2.79</td>
<td>0.74</td>
<td>3.48</td>
<td>1.16</td>
</tr>
<tr>
<td>2006</td>
<td>9,438</td>
<td>13,152</td>
<td>0.07%</td>
<td>7,612</td>
<td>1,826</td>
<td>3.04</td>
<td>0.73</td>
<td>3.44</td>
<td>1.24</td>
</tr>
<tr>
<td>2007</td>
<td>9,846</td>
<td>14,611</td>
<td>0.07%</td>
<td>7,854</td>
<td>1,991</td>
<td>3.13</td>
<td>0.79</td>
<td>3.55</td>
<td>1.19</td>
</tr>
<tr>
<td>2008</td>
<td>10,121</td>
<td>15,309</td>
<td>0.07%</td>
<td>8,153</td>
<td>1,968</td>
<td>3.25</td>
<td>0.79</td>
<td>3.51</td>
<td>1.18</td>
</tr>
<tr>
<td>2009</td>
<td>9,568</td>
<td>13,485</td>
<td>0.07%</td>
<td>7,785</td>
<td>1,803</td>
<td>3.11</td>
<td>0.72</td>
<td>3.37</td>
<td>1.17</td>
</tr>
<tr>
<td>2010</td>
<td>9,626</td>
<td>15,141</td>
<td>0.06%</td>
<td>7,647</td>
<td>1,980</td>
<td>3.05</td>
<td>0.79</td>
<td>4.26</td>
<td>1.14</td>
</tr>
<tr>
<td>2011</td>
<td>9,936</td>
<td>16,919</td>
<td>0.06%</td>
<td>7,883</td>
<td>2,054</td>
<td>3.14</td>
<td>0.82</td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>

To put the SOX audit numbers in perspective, we compared the costs of audits to the cost of CEO or CFO compensation in Table 2. Total compensation of the CEOs and CFOs were obtained from the Compustat-Executive Comp database including salary, bonus, total values of restricted stock grants and option grants, and the payout of long-term incentive plans. The median of total CEO or CFO compensation was then calculated based on the sample of S&P 1500 firms.

In a separate study conducted in 2009, the SEC tallied the total cost of SOX 404 compliance by surveying firms about the shares of audit and non-audit fees directly attributable to the compliance rule, adding in internal labor hours and non-labor costs, as well as outside vendor costs. As opposed to scaling by total revenue in the Audit Analytic study cited earlier, the SEC’s report showed that, scaled by total assets, small firms, those with a public share float from $50 million to $150 million, experienced on average, a cost of 0.79 percent of total assets, whereas the cost for large firms, those with over $700 million of public float, was 0.14 percent. In addition, the SEC’s

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155. Samples include the 2,507 accelerated filers for audit and no-audit fees, and S&P 1500 companies for CEO and CFO compensation figures. Both samples represent the largest publicly traded companies in the U.S. capital markets and significantly overlap.


157. Id. at 53.
report found that compliance costs move in an inverse direction to years of experience. Firms with three years of compliance experience see their costs go down to 0.55 percent for small firms, and 0.11 percent for large firms.

2. The Market Reaction to the Adoption of SOX

The implementation of SOX did not happen in a day; rather, its adoption was a multi-stage event, which gave the market a prolonged time period to react to the new law. Thus we analyzed the adoption of SOX as a multi-stage event that took twenty-two days from the time the conference committee reported the legislation to both houses of Congress on July 24, 2002 to when President Bush signed the legislation into law on July 30, 2002 to the first reporting deadline under the new law on August 14, 2002.

Investors reacted positively to SOX and other signs that the government would step in to discipline perpetrators of corporate fraud. For example, on June 26, 2002, the day that the SEC announced it was filing a lawsuit against WorldCom for financial reporting fraud, the average stock market price rose by 3.6 percent.

158. Id. at 41–42; see also Townsend, supra note 21, at 904 (“These costs [of audit compliance] have decreased largely because companies became more knowledgeable about SOX regulation and more experienced with their internal compliance procedures.”).

159. SEC, SOX STUDY, supra note 156, at 41–42.

160. Joseph A. Castelluccio III, Sarbanes-Oxley and Small Business: Section 404 and the Case for a Small Business Exemption, 71 BROOK L. REV. 429, 451 (2005) (“[SOX was] passed by a nearly unanimous vote in both the House of Representatives and the Senate only seven months after Enron declared bankruptcy. In the same month [that] it was introduced in both chambers of Congress, President Bush signed Sarbanes-Oxley into law.”).

161. The joint conference committee of the House and the Senate reported on July 24, 2002. The bill passed the House on July 25, 2002 and the Senate on the same day.


164. UI Researchers Find Positive Market Reaction to Sarbanes-Oxley Act, UNIV. IOWA NEWS SERVS. (Feb. 20, 2007), http://news-releases.uiowa.edu/2007/February/022007sox-reaction.html (“While corporate executives say their businesses are groaning under the weight of complying with Sarbanes-Oxley regulations, two University of Iowa business professors have found that most investors cheered the law during its early days.”).

165. Id. (“Stock prices began to rebound almost as soon as the SEC announced its actions on June 26, as stock returns increased by 3.6 percent by the end of the trading day June 27 from their lows of the day before.”).
Similarly, on July 24, 2002, when investors learned that the Sarbanes-Oxley Act was under review by the House and Senate for approval, the market stock value increased by 5.4 percent. On July 29, 2002, when the SEC stated that it would publicly name CEOs and CFOs who did not certify their financial statements, stock prices increased by another 5 percent. Overall, stocks of companies that investors believe were using the most deceitful financial reporting tactics rebounded the most after the aforementioned announcements, rising on average by an additional 5 percent.

Examining the S&P 1500 firms as our data set, we used an event study methodology to measure the market reaction surrounding the enactment of SOX on July 30, 2002, when it was signed into law. We used the OLS (Ordinary Least Square) regression model with robust standard errors which allowed us control for confounding factors such as macroeconomic and industry level shocks as well as specific firm characteristics. Expected returns are estimated based on the standard market model: \( R_{it} = \alpha_i + \beta_i \times R_{mt} + \epsilon_t \). The left hand side is the stock return of security \( i \) at time \( t \), to be regressed on the return of the overall market over the same time period, represented by the market index composed of the largest 1,500 publicly traded companies in the U.S., with data obtained from the Center for Research in Security Prices (CRSP) equally weighted index. The estimated slope coefficient, \( \beta_i \), or beta, is then used to estimate the expected return of a security using the Capital Asset Pricing Model (CAPM). The

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166. Id. at 123 n.aa1 (“The stock price effects . . . on July 24, are positive and highly significant (Market CAR = 5.4 percent, \( t = 3.62 \)).”).

167. Id. (“Untabulated results indicate that the positive reaction occurred on July 29, the day the SEC announced it would publicly identify CEOs and CFOs who failed to certify their firms’ financial reports (July 29 Sample CAR = 5.3 percent, \( t = 3.40 \), with 95.3 percent of firms having positive returns).”).

168. Morton Pincus, Sonja Rego, & Haidan Li, Market Reaction to Events Surrounding the Sarbanes-Oxley Act of 2002 and Earnings Management, 51 J.L. & ECON. 111, 122 n.aa1 (2008) (“We find positive abnormal returns (3.6 percent marketwide) associated with E2, the event that spans the opening of trading on June 26 to the close of trading on June 27 and includes the SEC’s actions against WorldCom and its mandating of CEO/CFO certifications.”).

169. We did not utilize a difference in difference (DID) analysis because DID is not appropriate in analyzing the effects of regulation on different types of firms because the assignment of placebo and treatment groups (firms subject to the new disclosure rule or not) cannot be randomized. For additional critique on this DID see Marianne Bertrand, Esther Duflo, & Sendhil Mullainathan, How Much Should We Trust Differences-in-Differences Estimates?, 119 Q.J. ECON. 249 (2004). Moreover, using standard event study methodology sidesteps any concern of endogeneity, since the event of federal disclosure laws being passed (or repealed) is not considered a direct consequence of a firm’s specific actions.

regression also contains an intercept, $a$, and a residual term, $e$. Practically, to estimate the model parameters for each company, we use a period of 255 days with the last day being the 46th day prior to the Act’s enactment date. Such estimates provide a calculation of the expected return of a security, which serves as a baseline figure to capture the “normal” returns when there is no news. The variables that we controlled for in the model are (1) a firm size’s (2) a firm’s research and development expenses, (3) a firm’s profitability, (4) a firm’s market to book ratio, and (5) a firm’s leverage. In addition, we included dummies to control for the different industry types based on the firms’ Standard Industrial Classification System (SIC) codes, as well as dummies to note whether the firm was a small cap firm as defined by Standard and Poors.

We expect the effect of a surprise, such as the arrival of new information about a new disclosure law, to be incorporated in the cumulative abnormal returns (CARs), stock returns in excess to the expected returns predicted by the market model. Because we are interested in both the short term and longer term effects of the enactment, we calculate CARs over the (-6, +1) and (-6, +15) event windows. The reason behind our choice of windows is that the investors knew that the SOX legislation was under review by both houses of Congress on July 24, 2002, six days before the event date. In addition, the due date for certifications of financial statements by CEOs and CFOs at SEC was on August 14, fifteen days after the event date. Hence, in order to capture the full effect of market reaction surrounding SOX we use the longer windows. Consistent with previous research on SOX, we found that the S&P 1500 firms on average reacted positively towards the enactment of SOX. The mean (median) of CARs is 3.3 percent (4.7 percent) and 4.6 percent (6.7 percent) in the event windows (-6, +1) and (-6, +15) respectively, and both means and medians are significantly different from zero at
the 1 percent level. Note that such returns are in excess to the overall market including all stocks traded on the New York and American stock exchanges and NASDAQ, and tracked by the Center for Research in Security Prices (CRSP), per definition of cumulative abnormal returns. In summary, we found that the market reacted positively to the adoption of SOX.

The effects are highly significant economically. After controlling for industry wide factors and firm specific characteristics detailed above, we found that for an average firm in the S&P 1500 index with a market capitalization of approximately $7.9 billion, shareholders received an accumulated elevated valuation of $261 million between July 24 and July 31, 2002. The gains ballooned to $364 million if we expand the time window to August 14.

Although the majority of public firms initially opposed the new SOX requirements, Christopher Cox, Chairman of the SEC, said that four years after its implementation, companies reported that their business processes had improved in terms of risk management, the accuracy of financial information and internal and external data integration. A survey by business consulting firm Protiviti confirms Cox’s statement, showing that more than two thirds of large firms have achieved significant or moderate improvements in their internal control systems—at the same time finding that the cost of compliance remained at manageable levels of $1 million or below.

Another noteworthy piece of evidence for the effectiveness of SOX is the proliferation of similar legislation internationally. Four...
years after SOX, SEC Chairman Cox reported that other developed markets such as the United Kingdom, Hong Kong, Australia, France, and Canada adopted similar reforms.\textsuperscript{176} To a lesser extent, SOX also indirectly improved corporate governance in developing markets like China and Mexico.\textsuperscript{177} Investors around the globe cherish more auditor independence and improved accuracy of financial reports, where management assesses and certifies the financial report’s quality and completeness.\textsuperscript{178}

B. The JOBS Act

1. JOBS Act Background and Data

The motivation for the passage of the Jumpstart Our Business Startups Act (or JOBS Act) by Congress was far different from what motivated the passage of SOX.\textsuperscript{179} After the financial collapse in 2008,\textsuperscript{180} a long lasting global recession stagnated the U.S. and world...
The unemployment rate in the U.S. remained high for years after the 2008 financial crash, which put enormous pressure on American policy makers to facilitate job creation. One suggested solution to spurring job creation was to lessen regulations of various kinds. In particular, the election year enactment of the JOBS Act, among other changes, reduced certain SEC reporting requirements for certain classes of companies and allowed for general solicitations for investors in private companies. Stupid had congressmen from both sides of the aisle not been so desperate for the more than $1 billion in campaign contributions given by individuals and groups affiliated with these firms . . . (‘‘Finally, another criticism has recently surfaced in relation to the concerns about risk-taking, particularly in the financial sector. Many scholars and policymakers have laid responsibility for the recent financial crisis at the doorstep of bankers’ pay structures’’).


Jed S. Rakoff, The Financial Crisis: Why Have No High-Level Executives Been Prosecuted?, NY REV. OF BOOKS (Jan. 9, 2014), http://www.nybooks.com/articles/archives/2014/jan/09/financial-crisis-why-no-executive-prosecutions/?pagination=false (“Five years have passed since the onset of what is sometimes called the Great Recession. While the economy has slowly improved, there are still millions of Americans leading lives of quiet desperation: without jobs, without resources, without hope.”).

AMY TRAUB, DAVID CALLAHAN, & TAMARA DRAUT, DEMOS, MILLIONS TO THE MIDDLE 14 BIG IDEAS TO BUILD A STRONG & DIVERSE MIDDLE CLASS 20 (2012), available at http://www.demos.org/sites/default/files/publications/MillionsToTheMiddle-DemosFinal_0.pdf (“The [2008] recession merely widened the already growing earnings shortfall: during the downturn, 60 percent of jobs lost nationwide were middle-income positions, yet most employment growth since the official end of the recession has been in low-wage occupations.”).

Brian Bodine, The JOBS Act: Reducing the Regulatory Burden on Small Businesses, NAT'L CTR. POL'Y ANALYSIS (Oct. 11, 2012), http://www.ncpa.org/pub/ba776 (“One piece of legislation, the Jumpstart Our Business Act (JOBS Act), was recently passed and signed into law. It should improve small business access to start-up capital by reducing the burden of some federal regulations.”).

James E. Bitter & Todd B. Skelton, Reforms for Hire: The JOBS Act Legislation, 14 TRANSACTIONS: TENN. J. BUS. L. 13, 31 (2012) (“Perhaps the broadest overhaul of the IPO process for EGCs [companies with annual revenues of less than $1 billion for its most recent fiscal year] is effectuated through the JOBS Act’s reduced reporting and disclosure requirements. These reduced requirements operate during the EGC’s five-year ‘transition period.’”).
The bipartisan JOBS Act\textsuperscript{187} was intended to increase capital formation, spur the growth of startups and small businesses and create more jobs.\textsuperscript{188} A major component of the Act reduces the costs of going public by providing “emerging growth” companies (ECGs) with a temporary reprieve from SEC regulations by phasing in certain regulations over a five-year period (including SOX Section 404, discussed above).\textsuperscript{189} Proponents argued that this would allow smaller companies to go public sooner, which in turn, could lead to more job creation within those companies.\textsuperscript{190} In addition, the Act allows companies offering securities under Regulation D to utilize advertisements or solicitations to reach investors and obtain capital.\textsuperscript{191}

\textsuperscript{187} Dina El Boghady, \textit{JOBS Act Falls Short on Grand Promises}, WASH. POST (Mar. 28, 2013), [hereinafter El Boghady, \textit{JOBS Act Falls Short}] http://www.washingtonpost.com/business/economy/jobs-act-falls-short-of-grand-promises/2013/03/28/5a66aa14-8675-11e2-98a3-b5d6b9ac586_story.html (“The legislation was built on the premise that regulation constrains the growth of small businesses and their potential for explosive job growth—an assertion that has been hotly debated by economists for decades”).

\textsuperscript{188} Whether the JOBS Act has succeeded in creating more jobs is beyond the scope of this paper. Other authors have been skeptical. \textit{Id}. (“Now, nearly a year after its enactment, major portions of the act are in limbo, and other parts have failed to measure up to the grandiose job-creation promises”).

\textsuperscript{189} See, e.g., 15 U.S.C.A. § 77g(a)(2) (West 2014) (requiring ECGs to provide only two years of audited financial statements instead of 3); Lori Schock, \textit{Outline of Dodd Frank Act and JOBS Act}, SEC (Jun. 9, 2012), http://www.sec.gov/News/Speech/Detail/Speech/1365171490596#.UtrG7LQo7De (“In terms of disclosure, the Act provides for reduced requirements for up to five years after the IPO”); James D. Cox, \textit{Strengthening Financial Reporting: An Essay on Expanding the Auditor’s Opinion Letter}, 81 GEO. WASH. L. REV. 1036, 1039–40 (2013) (“In 2012, with the JOBS Act, Congress returned to the topic again and further reduced the reach of section 404(b) [of the Sarbanes-Oxley Act of 2002]. First, and most directly, the JOBS Act lifts the auditor attestation requirements for emerging growth companies for five years after going public.”); Townsend, \textit{supra} note 21, at 895 (“Ten years after SOX’s enactment, Congress enacted section 103 of the JOBS Act (‘section 103’), which removed SOX section 404(b)’s outsider-audit requirement for essentially all companies. Specifically, through the JOBS Act, Congress removed SOX section 404(b)’s requirement for 98% of all companies that have gone public since 1970.”).

\textsuperscript{190} El Boghady, \textit{JOBS Act Falls Short}, \textit{supra} note 190 (describing SOX as “a grab bag of ideas cobbled together for greater impact[”] and noting that “it allows private firms to raise money by advertising to the general public for the first time in decades, raise up to $1 million in capital from investors via the Internet, and temporarily skirt some of the federal disclosure and accounting rules as they go public”).

\textsuperscript{191} \textit{See} Jumpstart Our Business Startups Act, Pub L. 112–106, § 201(a), 126 Stat 306 (2012) (to be codified in scattered sections of 15 U.S.C.); Susanne Craig & Ben Protess, \textit{Wall Street Examines Fine Print in a Bill for Start-Ups}, N. Y. TIMES (Apr. 4, 2012 8:43 PM), http://dealbook.nytimes.com/2012/04/04/wall-st-examines-fine-print-in-a-new-jobs-bill/ (“[T]he JOBS Act appears to loosen financial communication more broadly. For instance, the bill will relax rules on how investment firms can market themselves to the public, reversing regulations that restrict what hedge funds and private equity firms can say publicly about their investment strategy.”); Paci, \textit{JOBS Act Passes}, \textit{supra} note 132 (“[T]he JOBS Act effectively overrides [quiet period rules] that currently apply to the publication of research reports by underwriters during specified time periods after public offerings and during the 30-day period extending from 15
The Act also removes SEC restrictions that prevent “crowd funding” so entrepreneurs can raise equity capital from a large pool of small investors who may or may not be considered “accredited” by the SEC;\footnote{192} Further, the Act makes it easier for small businesses to go public by increasing the offering threshold for companies exempted from SEC registration from $5 million to $50 million;\footnote{193} removes barriers to capital formation for small companies by raising the shareholder registration requirement threshold from 500 to 2,000 shareholders;\footnote{194} and last increases the number of shareholders permitted to invest in a community bank from 500 to 2,000; arguably enabling banks to better deploy their capital.\footnote{195}

days prior to and until 15 days after the expiration date of lock-up periods.”); Steven Rattner, A Sneaky Way to Deregulate, N.Y. TIMES DEALBOOK (Mar. 3, 2013), http://opinionatorblogs.nytimes.com/2013/03/03/a-sneaky-way-to-deregulate/ (“Investment funds] will [now] be able to advertise—and thereby separate inexpert individuals from their savings. Until now, only a small percentage of Americans who qualified to invest this way [those making more than $200,000/year or with more than $1 Million in net worth] did so.”); Ruth Simon & Angus Loten, Fundraising Rules Murky Despite JOBS Act, WALL ST. J. (Nov. 13, 2013 8:15 PM), http://online.wsj.com/news/articles/SB10001424052702304868404579194061455051506 (“The new marketing freedoms are part of the [JOBS] Act of 2012. It ended the 80-year-old ‘general solicitation’ advertising ban designed to protect investors from get-rich-quick scams, making it easier for nascent firms to raise capital to grow.”).

\footnote{192} 15 U.S.C.A. § 77d(a)(6) (West 2014); Lori Schock, Outline of Dodd Frank Act and JOBS Act (Jun. 9, 2012), www.sec.gov/News/Speech/Detail/Speech/1365171490596#UtrG7LQo7De (“Companies cannot crowdfund on their own, but will have to engage an intermediary that’s registered with the SEC as a broker or funding portal. These intermediaries will be required to do some vetting of the company seeking funding.”); Andrew A. Schwartz, Keep It Light, Chairman White: SEC Rulemaking under the Crowdfund Act, 66 VAND. L. REV. EN BANC 43, 44 (2013) (“Title III of the JOBS Act, known as the CROWDFUND Act, authorizes the ‘crowdfunding’ of securities, defined as raising capital online from many investors, each of whom contributes only a small amount.”).

\footnote{193} § 77c(b).

\footnote{194} § 78(g)(1)(A); House Expected to Vote on Package of Capital Formation Bills This Week, SMALL BUS. & ENTREPRENEURSHIP COUNCIL (Mar. 6, 2012), http://www.sbecouncil.org/2012/03/06/house-expected-to-vote-on-package-of-capital-formation-bills-this-week/ (“H.R. 2167 removes barriers to capital formation for small companies by raising the shareholder registration requirement threshold from 500 to 1,000 shareholders.”).

\footnote{195} § 78(g)(1)(B); Ernst & Young LLP, TO THE POINT PERSPECTIVE: THE SEC’S OPPORTUNITY TO CONSIDER DISCLOSURE OVERLOAD, (2012), available at http://www.ey.com/Publication/vwLUAssets/TothePoint_CC0359_DisclosureOverload_4October2012/$FILE/TothePoint_CC0359_DisclosureOverload_4October2012.pdf (“The [JOBS Act] requires the SEC to review the public registration requirements in Regulation S-K and report to Congress on how to make them less burdensome for emerging growth companies (EGCs), which have less than $1 billion in annual gross revenues.”).
From an accounting point of view, the JOBS Act allows emerging companies to follow the SEC’s private company reporting deadlines, which often allows a longer time to comply with accounting disclosure requirements, rather than those required of public companies. According to Lori Schock, Director of the Office of Investor Education and Advocacy for the SEC, an emerging company must delineate whether it wants to take advantage of this accounting disclosure rule or not. While the JOBS Act was welcomed in some quarters, others worried that the reduced financial disclosures allowed by the JOBS Act could cause serious problems.

2. The Market Reaction to the JOBS Act

We use an event study methodology similar to the one used above with SOX to measure the market reaction surrounding the enactment of the JOBS Act on April 5, 2012, the day President Obama signed this act into law. Cumulative abnormal returns (CARs) were

196. § 78g(a)(2).
197. Schock, supra note 189 (explaining that the JOBS Act allows “emerging growth companies” to have the same amount of time to comply with accounting standards as private companies, rather than the reduced amount of time for compliance generally allowed to public companies).
198. Townsend, supra note 21, at 902 (“The supporters of section 103 commonly argue that it will increase job creation, reduce the cost of regulatory compliance, and improve the competitiveness of the U.S. capital market.”).
199. Benjamin P. Siegel, Title III of The JOBS Act: Using Unsophisticated Wealth To Crowdfund Small Business Capital or Fraudsters’ Bank Accounts?, 41 HOFSTRA L. REV. 777, 797 (2013) (“Crowdfunding requires the use of the general, unsophisticated public to be an effective means to raise capital. By requiring less issuer disclosures, as compared with those of registered public offerings, the CROWDFUND Act is essentially reducing the transparency of crowdfunding issuers.”); Bitter & Skelton, supra note 186 at 31–32 (“A major criticism of the JOBS Act is that investors in EGCs [firms with less than $1 billion in annual revenues] will no longer be getting an adequate amount of information to enable a comparison with other potential investments, and the reduced requirement for providing financial data is a prime example.”); Craig & Protess, supra note 191 (“The new legislation passed through Congress over the objections of regulators, past and present, who warned of the potential risks to investors. ‘It is a bad sequel to a bad movie,’” said Eliot Spitzer . . . it should be called the Bring Fraud Back to Wall Street Act”); Cox, supra note 189, at 1046 (“In a regulatory realm of less to no paternalism, the touchstone for securities regulation should nonetheless remain the information needs of investors. As seen in the case of section 404(b), many nonaccelerated filers voluntarily chose to comply with the internal control requirements.”); ROBERT A. FRIEDEL & ODIA KAGAN, PEPPER HAMILTON LLP, IF THREE’S A CROWD, THOUSANDS ARE . . . AN INVESTMENT ROUND? JOBS ACT PRESENTS SIGNIFICANT CHANGES TO THE FEDERAL SECURITIES LAWS 1 (2012), available at http://www.pepperlaw.com/pdfs/CorpSec032912.pdf (“[C]ritics of the act, including the [SEC], state securities regulators, institutional investors and investor protection groups, have expressed concern that the JOBS Act will harm investors by reducing transparency and investor protection.”).
200. Landler, supra note 179 (“President Obama . . . signed a bill on Thursday that will roll back restrictions on the way start-up companies can raise money from individual investors. Mr.
calculated using a CRSP equally weighted index as the market portfolio over the one day event window (-1,+1) and five days event window (-5, +5). On average, the S&P 1500 companies responded negatively towards the enactment of the JOBS act, with a mean (median) CARs of -0.1059 percent (-0.0578 percent), and -0.5539 percent (-0.5105 percent) over the one day and five days event respectively. Although the mean and median of the CARs over the one day window as well as the mean and median of the CARs over the five days window are statistically different from zero, the magnitude of those CARs tend to be small. But since the JOBS Act was particularly directed towards the small firms, we divided the mean and median CARs based on the firms’ market capitalization to investigate the market reaction of the Small Cap (SMCAP), Medium Cap (MIDCAP), and Large Cap (LGCAP) firms around that date. Looking at the CARs of those different subsamples, we witnessed that the SMCAP firms were the firms that had a significant negative market reaction towards the enactment of the JOBS Act. The mean/median of CARs around the one day event window, and five days event window was -0.3126 percent (-0.2805 percent), and -0.2401 percent (-1.1732 percent) respectively. All mean and median CARs for the SMCAP firms were significantly different from zero at the 1 percent levels. Furthermore, when we calculate the difference in means (using the t-test) and difference in medians (using the Wilcoxon rank test) to compare the difference in means/medians between the SMCAP group and the two other groups (MIDCAP and LGCAP), we find that the difference in means and medians is negative and highly significant across those two groups. Thus, the negative market reaction towards the JOBS Act was driven by the SMCAP firms, while the MIDCAP and LGCAP firms did not significantly react to the JOBS Act.

In summary, the results of the event analysis indicates that the stock market adversely reacted to the news of the signing of JOBS Act, indicating that at a minimum, the detrimental effects from lax

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- Townsend, *supra* note 21, at 896.
- 203. Valerie J. Easton & John H. McColl, **Wilcoxon Signed Ranks Test**, STATISTICS GLOSSARY 1.1, http://www.stats.gla.ac.uk/steps/glossary/nonparametric.html (“The Wilcoxon Signed Ranks test is designed to test a hypothesis about the location (median) of a population distribution.”).
disclosure outweighs the benefits of cash savings for small firms. After controlling for the same industry wide factors and firm specific characteristics detailed above, we found that for a median publicly traded small firms with $809 million in market capitalization, investors estimated an average one-day of loss of $7.9 million due to the enactment of JOBS Act.204

CONCLUSION

Again, before the SEC is a pending petition by ten law professors asking for more transparency of corporate political spending.205 This transparency is needed in light of the hundreds of millions of dollars of dark money flowing through the political system at present.206 When the SEC acts on this petition, they should craft the rule mindfully to survive the D.C. Circuit’s review process.207 The data provided here may assist the Commission in crafting and justifying such a new rule. As explained herein, the issue of the cost-benefit analysis is not merely of interest to economists;208 this is a key legal question for the SEC as it navigates the D.C. Circuit.209

We conclude from our datasets on SOX and the JOBS Act that there are real benefits for a company that is perceived by the market as being transparent with functioning internal controls. We surmise that this will be true of transparency about corporate political spending as well. However, we will not be able to test that theory until the SEC acts to bring transparency to corporate political spending.

204. Our conclusions are consistent with a new working paper on the impact of the JOBS Act, Mary E. Barth, Wayne R. Landsman, & Daniel J. Taylor, The JOBS Act and Information Uncertainty in IPO Firms (Stanford Univ. Grad. School of Bus. Res. Paper No. 14-16, July 1, 2014) (manuscript at 24), available at http://ssrn.com/abstract=2465927 (“Taken together, the findings indicate that the JOBS Act’s eased disclosure requirements increased information uncertainty in IPO firms.”).
206. Brief for Walter Dellinger & James Sample as Amici Curiae Supporting Respondents’ Opposition to Summary Reversal, Am. Tradition P’ship, Inc. v. Bullock, 132 S. Ct. 2490 (2012), (No. 11-1179), 2012 WL 1853625. (“Notwithstanding this Court’s assurance that disclosure would ‘provide shareholders and citizens with the information needed to hold corporations and elected officials accountable for their positions and supporters . . . corporations spending money to influence candidate elections have predictably denied shareholders and citizens such information.’”).
207. See, e.g., Fisch, supra note 11, at 701 (“The D.C. Circuit’s substitution of its policy judgment for that of the SEC both differs from this traditional deference and poses a threat to future agency rulemaking efforts . . . .”).