

Committee on Judiciary
Hawaii State Senate
415 South Beretania Street
Honolulu, Hawaii 96813

RE: SB166 – Proposed SD1 (relating to campaign finance)
Endorse subject to amendment

February 16, 2022

Dear Chair Rhoads, Vice Chair Keohokalole, and members of the committee:

We write in qualified support of SB166, conditioned on one critical amendment.

Free Speech For People is a national nonpartisan non-profit organization, that works to renew our democracy and limit the influence of money in elections. We have helped develop legislation to limit corporate political spending by foreign-influenced corporations. Specifically, we helped develop a law passed by Seattle, Washington in January 2020; a bill that this year passed the New York Senate; a bill recently introduced into the U.S. House of Representatives by Rep. Jamie Raskin; and similar legislation introduced into several state legislatures. The bill as we propose to modify it would be consistent with our current model legislation, which we have developed in partnership with the Center for American Progress, in New York and elsewhere. With these changes, we would be pleased to endorse it.

Most of the amendments to SB166 in proposed SD1 are positive and beneficial. However, we recommend re-inserting the following language from the original draft of SB166, to expand the definition of a foreign-influenced corporation:

- (1) A **single foreign owner** holds, owns, controls, or otherwise has direct or indirect beneficial ownership of **one per cent or more** of the total equity, outstanding voting shares, membership units, or other applicable ownership interests of the corporation;

- (2) **Two or more foreign owners**, in aggregate, hold, own, control, or otherwise have direct or indirect beneficial ownership of **five per cent or more** of the total equity, outstanding voting shares, membership units, or other applicable ownership interests of the corporation . . .

A short explanation for this change follows.

I. Foreign influence and ownership thresholds

As explained in more detail in written testimony submitted by Professor John Coates of Harvard Law School in support of similar legislation elsewhere, and in a recent report by the Center for American Progress,¹ **the thresholds in the original SB166—1% of stock owned by a single foreign investor, or 5% owned by multiple foreign investors—reflect levels of ownership that are widely agreed (including by entities such as the Business Roundtable) to be high enough to influence corporate governance.** Corporate governance law gives substantial formal power to minority shareholders at these levels, and this spills out into even greater unofficial influence. Thus, since the passage of Seattle’s 2020 law, newer bills—pending in states such as New York, Massachusetts, and Minnesota, and in the U.S. Congress—generally follow the Seattle model.

Federal securities law provides powerful tools of corporate influence to investors at these levels. **Seattle’s 1% threshold was grounded in a rule of the U.S. Securities and Exchange Commission regarding eligibility of shareholders to submit proposals for a shareholder vote—a threshold that the SEC ultimately concluded was, if anything, *too high*.**² For a large multinational corporation, an investor that owns 1% of shares might well be the largest single stockholder; it would generally land among the top ten. Conversely, as the SEC has acknowledged, many of the investors *most active* in influencing corporate governance own well below 1% of equity.³

¹ See Michael Sozan, Ctr. for American Progress, *Ending Foreign-Influenced Corporate Spending in U.S. Elections* (Nov. 21, 2019), <https://ampr.gs/2QIiNQT>.

² Until November 4, 2020, owning one percent of a company’s shares allows an owner to submit shareholder proposals, which creates substantial leverage. See *Procedural Requirements and Resubmission Thresholds Under Exchange Act Rule 14a-8*, 85 Fed. Reg. 70,240, 70,241 (Nov. 4, 2020). The SEC proposed to eliminate this threshold, and rely solely on absolute-dollar ownership thresholds that correspond to far *less* than 1% of stock value, because it is fairly uncommon for even a major, active institutional investor to own 1% of the stock of a publicly-traded company. See SEC, *Procedural Requirements and Resubmission Thresholds under Exchange Act Rule 14a-8*, 84 Fed. Reg. 66,458 (Dec. 4, 2019) (proposed rule). In other words, recent advances in corporate governance law suggest that the 1% threshold may, if anything, be *higher* than appropriate to capture investor influence. That said, we believe that 1% remains defensible.

³ See 84 Fed. Reg. at 66,646 & n.58 (noting that “[t]he vast majority of investors that submit shareholder proposals do not meet a 1 percent ownership threshold,” including major institutional investors such as California and New York public employee pension funds).

Of course, this does not mean that *every* investor who owns 1% of shares will *always* influence corporate governance, but rather that the business community generally recognizes that this level of ownership presents that opportunity, and—for a foreign investor in the context of corporate political spending—that risk.

In other cases, no single foreign investor holds 1% or more of corporate equity, but multiple foreign investors own a substantial aggregate stake. To pick one example, at the moment of this writing (it may change later, of course, due to market trades), Amazon does not have any 1% foreign investors, but at least 8.3% of its equity (and possibly much more) is owned by foreign investors.⁴ While presumably foreign investors as a class are not all perfectly aligned on all issues, they can be assumed to share certain common interests and positions that may, in some cases, differ from those of U.S. shareholders—certainly when it comes to matters of Hawaii public policy. As the Center for American Progress has noted:

Foreign interests can easily diverge from U.S. interests, for example, in the areas of tax, trade, investment, and labor law. Corporate directors and managers view themselves as accountable to their shareholders, including foreign shareholders. As the former CEO of U.S.-based Exxon Mobil Corp. starkly stated, “I’m not a U.S. company and I don’t make decisions based on what’s good for the U.S.”⁵

Neither corporate law nor empirical research provide a bright-line threshold at which this type of aggregate foreign interest begins to affect corporate decision-making, but anecdotally it appears that CEOs do take note of this aggregate foreign ownership and that at a certain point it affects their decision-making. The Seattle model legislation selects a 5% aggregate foreign ownership threshold. Under federal securities law, 5% is the threshold that Congress has already chosen as the level at which a single investor *or group of investors working together* can have an influence so significant that the law requires disclosure not only of the stake, but also the residence and citizenship of the investors, the source of the funds, and even in some

⁴ See *Amazon.com*, CNBC, <https://cnb.cx/3HVuWvg> (visited Feb. 15, 2022) (ownership tab). As of the date of writing, at least one foreign investor (Norges Bank) holds 0.9% but no foreign investor is known to hold 1.0% or more. Aggregate ownership data, however, shows 7.6% in Europe (including Russia) and 1.1% in Asia. In fact, the total aggregate foreign ownership could be much higher, as the summary data show only 55.6% of shares owned in North America. CNBC obtains its geographic ownership concentration data from Thomson Reuters, which in turn obtains it from Refinitiv, a provider of financial markets data that has access to some non-public sources.

⁵ Michael Sozan, Ctr. for Am. Progress, *Ending Foreign-Influenced Corporate Spending in U.S. Elections* (Nov. 21, 2019), at 19, <https://ampr.gs/2QLiNQT>.

cases information about the investors' associates.⁶ In this case, while it may not be appropriate to treat unrelated foreign investors as a single bloc for *all* purposes, it is appropriate to do so in the context of analyzing how corporate management conceive decision-making regarding political spending in U.S. elections.

Obviously, some companies do not have substantial foreign ownership. Even of those that do, many probably do not spend corporate money on Hawaii elections. Such companies either would not be covered at all (if they did not meet the threshold) or would not experience any practical impact (if they do not spend corporate money for political purposes).

II. Frequently asked questions

Has any court decided how much foreign ownership of a corporation renders a corporation “foreign” for purposes of First Amendment analysis?

No. That issue was not before the Supreme Court in *Citizens United*, and the Court expressly decided *not* to decide that question.⁷ The majority opinion did make a passing reference to corporations “funded predominately by foreign shareholders” as the type of issue that the decision was *not* addressing. This is what lawyers call “dictum”—something mentioned in a judicial opinion that is not part of its holding. Similarly, in *Bluman*, Judge Kavanaugh wrote that “[b]ecause this case concerns individuals, we have no occasion to analyze the circumstances under which a corporation may be considered a *foreign* corporation for purposes of First Amendment analysis.”⁸ For purposes of political spending, the question of how much foreign ownership is “too much” has not yet been decided by any court.

Our January 28, 2022 testimony shows how arguably *any* foreign ownership renders the entire pool of corporate funds foreign. However, the bill focuses narrowly on corporations where foreign holdings exceed thresholds, established from empirical corporate governance research, where investors can exert influence on executives' decisions. Notably, the Seattle Clean Campaigns Act (the model upon which this bill is based) has been in effect since February 2020, including the vigorously contested 2021 city election with an expensive mayoral race, yet none of the many multinational corporations in Seattle were impelled to challenge it.

⁶ 15 U.S.C. §§ 78m(d)(1)-(3).

⁷ See *Citizens United*, 558 U.S. at 362.

⁸ *Bluman*, 800 F. Supp. 2d at 292 n.4.

How many companies would be covered by the bill at 1%/5% thresholds?

Foreign investment in U.S. companies has increased dramatically in recent years: “from about 5% of all U.S. corporate equity (public and private) in 1982 to more than 20% in 2015.”⁹ By 2019, that figure had increased to 40%.¹⁰

However, foreign ownership is not evenly distributed. The Center for American Progress found that the original 1%/5% thresholds in SB166 would cover 98% of the companies listed on the S&P 500 index, but only 28% of the firms listed on the Russell Microcap Index—among the smallest companies that are publicly traded.¹¹ By contrast, the threshold in proposed SD1 would cover only 9% of the S&P 500.¹²

It is much more difficult to obtain data regarding ownership of privately-held companies. Intuition suggests that the vast majority of small local businesses have zero foreign ownership.

III. Other information

We also share with you, and incorporate by reference, written testimony prepared by leading national experts in support of the Massachusetts legislation, to which SB166 would be extremely similar if amended as discussed above:¹³

Commissioner Ellen Weintraub, Federal Election Commission
<http://bit.ly/WeintraubMALtr>

Professor Laurence Tribe, Harvard Law School
<http://bit.ly/TribeMALtr>

Professor John C. Coates IV, Harvard Law School; former General Counsel of U.S. Securities and Exchange Commission
<http://bit.ly/CoatesMALtr>

⁹ John C. Coates IV, Ronald A. Fein, Kevin Crenny, & L. Vivian Dong, *Quantifying foreign institutional block ownership at publicly traded U.S. corporations*, Harvard Law School John M. Olin Center Discussion Paper No. 888 (Dec. 20, 2016), Free Speech For People Issue Report No. 2016-01, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2857957.

¹⁰ See Steve Rosenthal and Theo Burke, *Who’s Left to Tax? US Taxation of Corporations and Their Shareholders*, Urban-Brookings Tax Policy Ctr., paper presented at NYU School of Law (Oct. 27, 2020), <https://bit.ly/3uLjVqE>.

¹¹ Michael Sozan, Ctr. for Am. Progress, *Ending Foreign-Influenced Corporate Spending in U.S. Elections* (Nov. 21, 2019), at 42-45, <https://ampr.gs/2QIiNQT>.

¹² See Coates et al., *supra* note 9.

¹³ These links are included only for informational purposes regarding the experts’ support of the Massachusetts legislation.

If you have any questions about particular policy or drafting choices (some of which may be subtle) made in the development of the draft, we would be happy to discuss. (And please see our January 28, 2022 written testimony for discussion of other issues.)

Sincerely,

Ron Fein, Legal Director

Courtney Hostetler, Senior Counsel

John Bonifaz, President

Ben Clements, Board Chair and Senior Legal Advisor

Free Speech For People