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HIGH COURT CASES MAY SHAPE FIRST AMENDMENT'S APPLICATION TO FEDERAL SECURITIES LAWS

by
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The Supreme Court this term will decide two cases that may clear some of the muddle on commercial speech. *Nike, Inc. v. Kasky*, 27 Cal.4th 939, 45 P.3d 243, 119 Cal.Rptr.2d 296 (2002), *cert. granted,* 534 U.S. 3458, 123 S.Ct. 817 (2003), a California fraud case arising out of Nike's attempt to defend itself in the media and elsewhere against allegations concerning the working conditions in which its shoes are made, will address what types of speech will be treated as "commercial" and entitled only to a lower level of First Amendment protection. *Ryan v. Telemarketing Associates, Inc.,* 763 N.E.2d 289, 198 Ill.2d 345 (2001), *cert. granted* 123 S.Ct. 512 (2002), an Illinois fraud prosecution against a professional fundraising service, will consider the level of constitutional protection to which "commercial" speakers are entitled.

Nike gives the Court the opportunity to affirm Justice Powell's observation in *First Nat'l Bank v. Bellotti,* 435 U.S. 765, 777 (1978), that "[t]he inherent worth of the speech in terms of its capacity for informing the public does not depend upon the identity of its source, whether corporation, association, union, or individual." The Court may limit the commercial speech category to advertising where it has less concern about chilling speech, and ensure that the regulation of such speech is tailored to the public interest. Or the Court might create a separate category of corporate non-commercial speech that receives mid-level protection. Clarifying First Amendment protection of corporate speech would better balance the debate over limits on free enterprise than permitting regulation only of the pro-business side of the debate.

If the Court takes this important step, hopefully it also will lay the groundwork for resolving the closely related issues concerning corporations' communications with shareholders or in investment markets. *See* Butler & Ribstein, *Corporate Governance Speech and the First Amendment*, 43 U. KANS. L. REV. 163 (1994). Specifically, what First Amendment protection does Nike have in defending its manufacturing practices in proxy statements or SEC filings? Analogous cases have involved a firm's proxy response to charges by labor unions about its environmental practices (*United Paperworkers Int'l Union v. International Paper Co.,* 985 F.2d 1190 (2d Cir. 1993)) and a firm's duty to devote some of its proxy materials to the

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national health care debate (*New York City Employees' Retirement System v. Dole Food Co., Inc.*, 795 F. Supp. 95 (S.D.N.Y.), dismissed as moot, 969 F.2d 1430 (2d. Cir. 1992)).

Arguments like those made in favor of protecting Nike's speech to the marketplace about its manufacturing processes can also apply to firms' similar speech to their shareholders. Just as anti-business groups can more easily persuade voters to enact regulation if corporations' response is muted by their concerns about consumer litigation, such groups would like the securities laws to constrain corporate managers' response to shareholder corporate responsibility initiatives. Corporate managers defending the pro-business side of the debate may be as deterred by the threat of shareholder litigation as by the risk of consumer litigation.

In light of the strong analogies between the two situations, the Court should revisit its dictum in *Pacific Gas & Electric Co. v. Public Utilities Commission,* 475 U.S. 1 (1986) seeking to distinguish internal and external corporate speech. The Court there struck down under the First Amendment a state utility commission's requirement that a utility company provide space in its billing envelope for opposing political viewpoints. Justice Stevens noted in dissent that the SEC's shareholder proposal rule "performs the same function as the Commission's rule by making accessible the relevant audience, whether it be shareholders investing in the corporation or consumers served by the utility, to individuals or groups with demonstrable interests in reaching that audience for certain limited and approved purposes." *Id*. at 39-40. Justice Powell wrote for the plurality that "regulations that limit management's ability to exclude some shareholders' views from corporate communications do not infringe corporate First Amendment rights" or "limit the range of information that the corporation may contribute to the public debate." *Id*. at 14, n. 10. This is not easily squared with Justice Powell's statement in *Bellotti* that the First Amendment protects speech regardless of its source. Nor is it obvious that speakers should have less protection when they contend for control of the firm than when they speak for it. In other words, the corporate entity should not obscure the First Amendment interests of individuals within the firm. *See* Ribstein, *Corporate Political Speech*, 49 WASH. & LEE L. REV. 109 (1992).

The First Amendment also should protect non-"political" communications to shareholders concerning management and finance. This speech is not obviously "commercial" in the sense of relating to the sale of the corporation's product. Perhaps the corporation itself is the product, but then the same reasoning would apply to the *Nike* situation, as dissenting Justice Brown observed in that case. Moreover, federal regulation of corporate governance has long been justified on the ground that large corporations wield power comparable to that of governments. If corporations are in effect governments, then their governance would seem inherently to be a political issue. Managers therefore should have as much leeway to defend their financial as they do their "social" performance.

Regulation of the sale of corporate securities under the Securities Act of 1933 is also vulnerable under the First Amendment. To the extent that this is comparable to the sale of a product (and even that is not certain), the regulation should be subject to the same scrutiny as that of charitable fundraisers in the *Ryan* case. Accordingly, if the Court holds that the Illinois regulation at issue in the case was not adequately tailored to the potential harm in that case, perhaps the same careful tailoring should be required of regulation preventing firms from making *truthful* statements about their securities prior to circulating a full prospectus. The Court similarly should scrutinize recent SEC Regulation FD restricting firms' *truthful* statements to analysts prior to full disclosure of the same information. *See* Ribstein, *SEC "Fair Disclosure" Rule is Constitutionally Suspect,* 10 LEGAL OPINION LETTER (Washington Legal Foundation) 17 (Oct. 6, 2000).

In short, clarifying the First Amendment's application to commercial and corporate speech in *Nike* and *Ryan* may force the Court finally to confront the application of the First Amendment to the federal securities laws.

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