

# POLITICAL LAW UPDATE

Covington & Burling LLP

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In this issue of our Political Law Update, we report on significant recent developments in campaign finance law. These include an important decision by the US Court of Appeals for the DC Circuit in the *Emily's List* case, which should be of great interest to anyone engaged in issue advocacy, and proposed new SEC rules governing "pay-to-play" by investment advisers. We also note that the Municipal Securities Rulemaking Board is seeking to amend Rule G-37, which governs pay-to-play by municipal finance professionals.

Another notable recent development is the enforcement action undertaken by New York's Public Integrity Commission concerning very low dollar gifts to public officials. New York is a leader among the states on regulatory matters, and this may reflect a trend toward enforcement of the strict gift rules that are on the books in many states but sometimes have been weakly enforced.

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## BULLETS

- **AN FEC FINE WAS THE LEAST OF HIS PROBLEMS.** In August, a Missouri state senator pleaded guilty to two counts of obstruction of justice for lying to the FEC during an investigation into whether he illegally coordinated with an outside group during his 2004 congressional campaign. The sentencing guidelines provide for 15 to 21 months in prison. This highlights the fact that in a number of areas (FEC investigations, GAO audits of lobbying reports), a sometimes lax statutory enforcement scheme is backed up by

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criminal laws that prohibit “false statements” to a federal official, which can include false statements on disclosure reports.

- **ILLINOIS GOVERNOR VETOES CAMPAIGN FINANCE REFORM AS TOO WEAK.** The political fall out from the Blagojevich scandal continues. On August 27, Illinois Governor Quinn vetoed a campaign finance reform bill (H.B. 7) he had previously testified in support of, saying “I think we can do better.” With elections next year, many incumbents are afraid of being seen as not tough enough on “corruption.” This is a state to watch closely when the October 2009 legislative session opens.
- **CLARIFICATIONS MAY BE COMING TO ILLINOIS’ PAY-TO-PLAY RULES.** On May 22, 2009, the Illinois legislature passed a package of reforms, including revisions to the state’s “pay-to-play” rules. Illinois law currently requires that state contractors register with the Illinois Board of Elections and disclose information about certain affiliated persons and affiliated entities. The bill would amend the definition of “affiliated persons” to remove the obligation to disclose minor children. It would amend the definition of “affiliated entities” to remove the confusing “unitary business group” concept, instead requiring disclosure of certain parent and subsidiary entities. The deadlines for reporting changes to registration information would also be amended. On August 18th, the Governor used his amendatory veto power to reject the measure as currently drafted, suggesting various changes to the legislation. The bill will not become law unless the Governor’s proposed changes are accepted by both houses of the legislature by majority vote, or unless the legislature passes the original bill by 3/5th majority.

## ARTICLES

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### DC CIRCUIT STRIKES DOWN FEC REGULATIONS GOVERNING ISSUE AD GROUPS

On Friday, a three judge panel of the U.S. Court of Appeals for the D.C. Circuit struck down regulations the FEC had adopted in 2004 to curb the activities of issue ad groups operating under Sections 527 and 501(c) of the Internal Revenue Code. [Emily’s List v. FEC](#). This decision will make it easier for outside groups to raise and spend money on hard hitting ads in the days and weeks before an election.

The FEC regulations at issue in the case required many outside groups to allocate a certain amount of “hard money” (funds raised from individuals or federal PACs in increments of \$5,000 or less) to pay for get-out-the-vote activities, voter registration drives, advertising, and administrative expenses, even if those activities did not mention federal candidates. Emily’s List asked a federal district court in Washington to vacate those regulations. The district court ruled against Emily’s List. Although a three-judge DC Circuit panel unanimously reversed that ruling and vacated the FEC regulations, only Judges Kavanaugh and Henderson did so on constitutional grounds. The third member of the DC Circuit panel, Judge Janice Rogers Brown, wrote a concurring opinion deciding the case on purely statutory grounds and strongly criticizing the majority for its sweeping constitutional opinion.

The majority opinion not only rejects the FEC’s allocation formula but also appears to hold that nonprofit organizations using funds raised from individuals can advocate for the election or defeat of federal candidates, without restriction. If this holding survives, it will constitute a major sea change in campaign finance law. But this story is not over. First, only federal district courts in DC are required to treat the DC Circuit panel’s decision as controlling law. Courts elsewhere in the country may reach different conclusions. Second, the FEC might seek review of the DC Circuit panel’s decision by the full Court of Appeals, or by the Supreme Court. It is by no means certain that the FEC will seek further review, however, as at least four of the six FEC Commissioners would have to vote in favor of doing so.

The 2010 election will see many groups taking advantage of this and other recent decisions that permit them to engage in election related activities, without having to comply with all of the rules that hampered their operations in the 2006 and 2008 elections. But with campaign finance law in great flux at the moment, it may be some months before the ground rules for 2010 become clear.

### **FEDS INCREASINGLY PROSECUTING INDIVIDUALS FOR FCPA OFFENSES**

On Friday, September 11, a jury found two Los Angeles film executives guilty of violating the Foreign Corrupt Practices Act ("FCPA"), money laundering, and filing false federal income tax returns as a result of improper payments they made to a Thai government official in an effort to win government contracts, including a contract to manage and operate Thailand's yearly film festival.

The executives made the payments through a variety of companies they owned (including shell companies) and numerous off-shore bank accounts, some of which were in the names of a family member or a friend of the Thai official. According to the Department of Justice, through this scheme, the defendants won contracts generating more than \$13.5 million in revenue. The defendants will be sentenced in mid-December.

This case highlights a trend of the U.S. government targeting individuals for FCPA violations. Earlier in September a former director of sales and marketing for Pacific Consolidated Industries LP settled criminal FCPA charges relating to bribery of a United Kingdom official for \$70,000. In late July, the Chief Executive Officer and former Chief Financial Officer of Nature's Sunshine Products separately settled civil claims related to improper payments in Brazil for \$25,000 each. (The company settled claims against it for \$600,000.)

The FCPA prohibits companies, their employees and representatives from giving "anything of value" to a non-U.S. government official for an improper purpose, such as inducing the official to grant special treatment to a company. Virtually any government employee or representative can be considered a government official under the statute, as can employees of international organizations, political parties and others. The FCPA also requires public companies to keep accurate books and records and to establish and maintain a system of internal accounting controls. If you or your company deal with non-U.S. governments, you should consider how the FCPA may affect you.

### **SEC PROPOSES PAY-TO-PLAY RULES FOR INVESTMENT ADVISERS**

In August 2009, the SEC proposed a new rule under the Investment Advisers Act of 1940 designed to eliminate pay-to-play practices by investment advisers managing public funds. Closely resembling the Municipal Securities Rulemaking Board ("MSRB") Rule G-37 pay-to-play restrictions, as well as a failed 1999 SEC proposal, proposed SEC Rule 206(4)-5 would significantly limit the contribution and solicitation activities of advisers and certain other covered persons. The rule would apply to both SEC-registered advisers and "private advisers" that are exempt from registration, including private equity funds and hedge funds. In addition, the rule would cover advisers to pooled investment vehicles, including government-sponsored savings and retirement plans. A detailed summary of the proposed SEC rule is contained in a recent Covington client advisory, which is available [here](#). Comments on the SEC's proposed rule are due on October 6, 2009. Implementation of a final rule likely will not occur until 2010.

## **MSRB PROPOSES CHANGES TO TREATMENT OF PACs UNDER PAY-TO-PLAY RULE FOR MUNICIPAL SECURITIES DEALERS**

On September 16, 2009, the MSRB issued a request for comments on proposed amendments to Rule G-37, which regulates “pay-to-play” political contributions by municipal securities broker-dealers and so-called “municipal finance professionals.” The proposed amendments are intended to address what the MSRB perceives as a risk that banks might be using their PACs to enable affiliated broker-dealer entities to circumvent Rule G-37.

If the MSRB’s proposal is adopted, PACs that are connected to banks would have to disclose on filings with the MSRB any contributions made by the PACs to officials of issuers (state and local officials who are in a position to influence the awarding of municipal securities business). The MSRB underscored, however, that it is not at this time advocating extending Rule G-37’s strict prohibitions on political contributions to PACs that are connected to banks. (It has always been the case that a municipal finance professional cannot make prohibited contributions indirectly through a PAC, but PACs themselves are not subject to a flat ban on contributions to officials of issuers.) Because PAC contributions to state and local officials are already subject to disclosure under existing campaign finance laws, it seems that the MSRB’s proposal is intended merely to facilitate the MSRB’s supervisory role by making data more readily and immediately available to the MSRB. Comments on the proposed amendments are due on October 30, 2009.

## **NEW YORK TAKES ACTION AGAINST ALLEGED GIFT RULE VIOLATORS: MORE ENFORCEMENT COMING?**

Lobbyists may wish to think twice next time they invite a state legislator to a reception in Albany. Although state ethics commissions traditionally have been somewhat lax in their enforcement of rules prohibiting “gifts” to state employees, that may be changing.

In August, New York’s Commission on Public Integrity initiated enforcement actions against prominent New York lobbying associations representing police, firefighters, and trial lawyers. The charge? Hosting receptions where they gave public officials refreshments that cost more than an ordinary cup of coffee.

Previously, New York state ethics rules allowed lobbyists to offer gifts valued at \$75 or less. That exception was scrapped in 2007. Now, any refreshment of more than “nominal value” is presumptively prohibited unless one of the law’s narrow exceptions applies. “Nominal value” means the cost of an ordinary cup of coffee, not, according to the Commission’s spokesman, “a \$6 latte.”

While these violations may seem minor, the consequences can be substantial. “Knowing and willful” violators of this provision can expect more than just a slap on the wrist. The law provides that violators must pay a civil fine up to the greater of \$25,000 or three times the value of the gift.

Organizations should take this opportunity to review their state gift rule compliance policies. A number of states have very low limits or prohibitions on seemingly inconsequential gifts to government officials. Sometimes reminding employees of organizational policies may be all it takes to prevent them from offering that pricey latte.

## TREASURY DEPARTMENT ISSUES NEW POLICY FOR COMMUNICATIONS ABOUT TARP FUNDS

On September 11, 2009, the Treasury Department released [a new policy](#) that will govern communications with Treasury Department officials about the Emergency Economic Stabilization Act ("EESA") process (also known as the Troubled Asset Relief Program or "TARP"). For those familiar with the administration's restrictions on lobbying over Recovery Act funds, these new rules will seem very familiar.

Treasury's policy prohibits anyone outside of the executive branch, whether a registered federal lobbyist or not, from orally communicating with Treasury officials about pending EESA applications. And like the Recovery Act policy, communications regarding EESA policy or proposed applications made by federal lobbyists (but not by non-lobbyists) are subject to public disclosure.

We summarize the new policy's key points in our [September 15, 2009 E-Alert](#).

### UPCOMING EVENTS

On September 30, 2009, Covington's Election and Political Law Practice Group will hold a seminar entitled "Outside Groups – Making an Impact in 2010," in which we will discuss the effect of recent cases, including *Citizens United* and *Emily's List*, on funding advocacy in the run up to the mid-term election, as well as the tax law and disclosure issues associated with these groups.

On February 4, 2010, we will host our day long seminar on corporate political activity, including government ethics, lobbying disclosure, "pay-to-play," and campaign finance law topics. This bi-annual event provides both a deep grounding in the fundamentals of the law and a refresher on the latest developments. Although space is limited, attendance at this compliance training conference is free of charge.

For more information about these events, contact Julia Merkin at [jmerkin@cov.com](mailto:jmerkin@cov.com).

### WHO WE ARE

Covington's Election and Political Law practice is one of the oldest in the Nation. In addition to our high-profile election law litigation and FEC enforcement practice, we advise numerous Fortune 500 corporations, trade associations, financial institutions, political party committees, PACs, candidates, and lobbying firms concerning compliance with the increasingly complex array of laws governing the political process. These include federal and state campaign finance, lobbying disclosure, and government ethics laws. For more information on Covington's Election and Political Law practice, please click [here](#).

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