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Political Law Update

Covington & Burling LLP

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INTRODUCTION

Momentum is building behind the federal and state efforts to impose a complex web of "pay-to-play" laws restricting political contributions by those who do business with state and local governments. In this Political Law Update, we summarize some of those recent developments, including the SEC's decision to jump on the pay-to-play bandwagon. Covington is advising numerous clients on the legal and business implications of pay-to-play laws and steps that corporations can take to adopt practical pay-to-play compliance systems.

If current trends hold, it seems likely that at some point consideration will be given to a federal pay-to-play law applicable to federal government contractors. Federal law currently does not restrict federal campaign contributions made by federal government contractors' executives or PACs (apart from contribution limits and other rules that apply to contributors generally). For the moment, attention is focused on state and local government contracting. Such state and local contracts are an important source of revenue for thousands of corporations.

CONTENTS

SEC ANNOUNCES PROPOSED FEDERAL PAY-TO-PLAY RULE. On August 3, the SEC released a proposed rule that would impose "pay-to-play" restrictions on political contributions by investment advisers. A decade ago, the SEC attempted to enact a pay-to-play rule but the proposal did not survive the rulemaking process. Covington issued a detailed summary of the proposed rule in an e-alert to clients. The proposed rule generally subjects investment advisers to restrictions on political contributions akin to those imposed on municipal securities dealers in the 1990s. The SEC has sought comments on a wide array of issues raise by the proposed rule. Comments are due on October 6, 2009.

TEXAS TEACHER RETIREMENT SYSTEM ADOPTS PAY-TO-PLAY. The sixth-largest public pension fund in the U.S. (with $77 billion in assets) now requires that companies seeking contracts to manage investments disclose (a) certain contacts with state officials and board members, (b) campaign contributions to elected state officials, and (c) the names of placement agents and placement fees, according to a new questionnaire the state agency is now requiring from all investment managers. This is part of the recent proliferation of "pay-to-play" restrictions on the political activity of corporations that do business with state and local governments.

REFORM STUMBLES IN HI, NV. Governor Lingle recently killed a bill that would have recodified Hawaii's campaign finance law. She did so explaining that it would have reduced the governor's power to appoint members to the state campaign finance board, relaxed the state pay-to-play law, permitted contributions from mainland residents to rise from 20 to 30% of a campaign's total, and allowed candidates to contribute excess campaign funds to the state party. The Nevada legislature also closed out its session without adopting campaign finance reform, despite both houses of the legislature passing similar versions of the reform law.

COLORADO PAY-TO-PLAY DECISION ISSUED. In July, a Colorado trial court finally issued a written decision, enjoining enforcement of much of the state's pay-to-play law, which was passed by voter initiative last year. The court blocked enforcement of those provisions in the new law that prohibit companies and unions with single source government contracts from making contributions to state or local candidates. The court left in place the reporting mechanism that requires sole source contractors to report information about their contracts to state officials. The Colorado Secretary of State's office has begun a rulemaking that will exempt certain types of contracts that are not competitively bid, though that office has shown some trepidation about whether it still has the authority to do so after the court's decision.

CITIZENS UNITED V. FEC

With over 40 supplemental briefs now on file and oral argument set for September 9, 2009, the prospect is growing that the Supreme Court will relax the rules on corporate spending in time for the 2010 mid-term election. According to recent news reports, Democrats face unexpected trouble in Senate races in Connecticut, Illinois, Pennsylvania, and New York, and House Democrats in swing districts sense that they are being asked to walk the plank on vote after vote. Targeted corporate spending in selected districts could have a disproportionate impact on election results next year.

Instead of issuing a decision in *Citizens United v. FEC* in June, the Supreme Court asked for more briefing and argument on the question of whether it should reverse its 2003 decision that Congress may restrict corporate spending on issue ads in the days before an election (*McConnell v. FEC*) or its 1990 decision that the government may prohibit

corporations from funding independent ads that call for citizens to vote for or against a particular candidate (*Austin v. Michigan Chamber of Commerce*).

Nothing more dramatically captures the ideological shift on the Supreme Court that has resulted from replacing Chief Justice Rehnquist and Justice O'Connor with Chief Justice Roberts and Justice Alito. Citizens United raised the issue of reversing *Austin* for the first time in its merits brief to the Supreme Court, devoting no more than 10% of the argument in its brief to the issue. Then, during oral argument, Citizens United appeared to concede that *Austin* was good law. Despite all of that, the Court has teed up the question of whether it should reverse these cases limiting corporate spending on political speech.

With the question now squarely before the court, a familiar cast of characters has appeared, briefs in hand. The Solicitor General argues that, absent a record or argument below, this is a poor case with which to radically revise the law. Citizens United focuses on the vast gulf between Justice Marshall's reasoning in *Austin* and the present Supreme Court's more constrained view of the power of the government to restrict political spending. Senators McConnell, McCain, and Feingold and now former Representatives Shays and Meehan have submitted briefs pro and con. In addition, the Chamber of Commerce, the AFL-CIO, the DNC, Common Cause, the ACLU, and Cato Institute (among others) have all filed briefs.

The potential impact of this case on corporations, trade associations, public advocacy groups, candidates—virtually everyone who puts money into the political process—is enormous, both in this election cycle and beyond.

SON OF HLOGA

Often legislators pass laws, imposing obligations on others, and go on their merry way. In adopting new congressional ethics rules in 2008, the Members of the House of Representatives may begin to feel the consequences of that "feel good" vote. In July, the newly created, independent and bi-partisan Office of Congressional Ethics (OCE) issued its first report. The OCE accepts complaints against members of the House of Representatives from the public. Only four of the OCE's eight board members need to vote to find probable cause in order for the OCE to refer the matter to the House Ethics Committee (which is formally known as the Committee on Standards of Official Conduct). The House Ethics Committee can conduct a full investigation and mete out whatever punishment or remedial measures are warranted. According to the OCE's report, the OCE already has taken in 64 complaints. In at least 5 cases it has referred the matter to the House Ethics Committee.

One of those referrals involved two trips to the Caribbean funded by the Carib News Foundation. Watchdog groups alleged the trips were actually funded by corporations that were registered under the Lobbying Disclosure Act and, consequently, were barred from funding the trips directly. In response to these allegations, the members involved have pointed to the facts that the House Ethics Committee pre-approved their participating on the trips and that the members involved believed the trips to be funded by the Carib News Foundation.

All of this goes to show that oversight of congressional trips, meals, and gifts will continue to earn close scrutiny. At least on the House side, this citizen-complaint driven investigatory body will be an easy tool for outside groups to use to trigger at least a preliminary investigation.

Organizations registered under the LDA (and hence covered by the travel restrictions) should closely review funding requests by outside groups for events involving members of Congress. Carib News is an example of the reputational risk of being drawn into an investigation where the outcome depends on how carefully Hill staff and outside groups have complied with the law.

Massachusetts Adopts Sweeping Reform

Massachusetts adopted a major overhaul of its ethics, lobbying, and campaign finance laws. This will bring stricter rules on gifts and campaign contributions, and expand the regulation of lobbying. The new provisions take effect at various times.

Specifically, the new law defines a lobbyist as anyone who spends over 25 hours or $2,500 of compensable time in a six month period on lobbying. "Lobbying" is defined to include any act to influence legislation or an executive employee's decision, including time spent strategizing, planning, and researching in preparation for a lobbying communication. Lobbyists will be required to undergo an annual seminar put on by the Secretary of State. Contingency fee lobbying contracts will be banned.

The law includes strict new gift rules, which include a prohibition on gifts from lobbyists. It permits gifts of less than $50 from non-lobbyists. The prohibition on campaign contributions by corporations also will be extended to include professional corporations, partnerships, and LLC's doing business in Massachusetts. Finally, heightened civil penalties and new enforcement powers for the Secretary of State are part of the package.

Upcoming Events

In September, 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 *Citizens United* on funding advocacy in the run up to the mid-term election.

On February 8, 2010, we will host our day long seminar on corporate political activity, including government ethics, lobbying disclosure, 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.

If you have any questions concerning the material discussed in this Political Law Update or any other election or political law matter, please contact the following members of our Election and Political Law Practice Group:

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