

Due Diligence Regarding PACs During Mergers and Acquisitions

May 12, 2016

Election and Political Law

Corporate mergers and acquisitions often overlook political law compliance issues—including whether the acquired company has a PAC—until after the transaction is complete and Day One has come and gone. We recommend considering PAC issues during the due diligence review to ensure there are no legal issues to be addressed in the acquired entity, and to prepare for how the FEC will treat the two PACs immediately after the merger. This alert provides information and resources for the necessary due diligence and for preparations to integrate the PACs after the acquisition is complete.

The Legal Issues

When an acquisition involves multiple PACs, there are three important legal issues to consider.

First, the company must ensure it complies with FEC requirements for contributions from affiliated entities. As of the day of control, the FEC will treat the two PACs as affiliated. This means that all of the contributions of the two PACs will be treated as if made by one entity. The FEC will evaluate whether contributions made by the acquiring company's PAC comply with the contribution limits (e.g., \$5,000 per candidate per election) based on all past contributions by the acquired and the acquiring companies' PACs. So after Day One, the FEC will treat all past contributions as well as future ones as if made by a single entity.

Second, the company must consider what structure it will want the PACs to assume after the acquisition. Affiliated PACs, in addition to being treated as a single unit for the purposes of measuring contributions, will now be allowed to make unlimited transfers of funds between them. This ability will leave the company with a choice as to how it wants to structure the two PACs going forward. Some companies leave the two entities in existence, with one serving as a collecting agent for the other, receiving contributions from employees of a subsidiary entity and transferring those funds to the parent company's PAC for use in campaign contributions. Other companies choose to disband the acquired company's PAC, which may involve organizational changes, such as dissolving a PAC board. If the PAC to be terminated is registered as a state PAC anywhere, is incorporated or has its own Taxpayer Identification Number, the dissolution may require legal work to resolve. Lastly, if the PAC is to be dissolved, the issue of whether the payroll deduction cards remain valid for the parent company's PAC should be considered.

Third, the company must ensure it is not acquiring any liabilities with the assets of the acquired company's PAC. In order to be terminated, the FEC will insist on the acquired company's PAC resolving any outstanding issues or enforcement proceedings. After Day One, sloppiness or errors by the acquired company's staff will become the company's compliance responsibility.

Due Diligence

To ensure smooth integration and to predict potential problems, you should be able to answer the questions below before signing off on a deal.

- Does the company you are acquiring have any outstanding campaign finance compliance issues with either federal or state regulators? Is there a history of such problems that might show further inquiry is warranted?
- Have you reviewed and reconciled the PAC's bank records with its FEC reports?
- Has the PAC been subject to an audit by regulators (which is generally only done if the agency has cause to perceive a problem exists) or as part of an internal compliance program (which should be standard practice)?
- Is there an adequate compliance program in place, including written policies on contributions by the company or its PAC?
- Is the acquired company's PAC registered in any states that may present integration issues or raise pay-to-play concerns?
- Has the company to be acquired received warnings, inquiries, or complaints from federal or state regulators in the past five years?

Documents Needed

In order to conduct due diligence on PAC acquisition, plan on obtaining the following documents:

1. Copies of PAC bank records for at least the preceding year.
2. Copies of any political law policies, procedures or training material related to political contributions, lobbying, or gifts to government officials.
3. Copies of any pending or resolved warnings, inquiry letters, complaints, fines or penalties from federal or state regulators related to political or lobbying activities in the past five years.
4. Copies of PAC solicitation material.
5. A list of all states in which the company has registered a political committee or PAC.
6. Any tax returns or information returns filed related to the company's political activity in the past three years, including any 1120-POL filed by the PAC in that period.

Integration—Day One and Beyond

On Day One, federal and state political law regulators will generally treat your two companies as a single entity. The following checklist is designed to avoid the largest pitfalls in PAC integration. While non-exhaustive, this checklist should provide PAC managers with some important steps necessary to avoid federal elections law issues.

- Amend both PACs' Form 1 to identify them as affiliated entities within 10 days of the date the acquiring entity takes effective control of the target company.

- Integrate data about the acquiring and acquired companies' PACs' contribution history to ensure future contributions comply with applicable limits.
- Establish a process to ensure neither PAC makes a contribution without confirming that it does not exceed the limits of the two PACs' prior giving.
- Develop a plan to integrate the two companies' political programs, including whether to seek formal approval from the FEC to merge federal PACs. This integration should be consistent with the FEC regulations covering PAC affiliation and termination.
- If the plan involves termination of an acquired entity's PAC and the transfer of remaining assets to the acquiring PAC, plan to:
 - Close the target PAC's bank account.
 - File a termination report for the target PAC.
 - Notify the IRS of EIN/TIN termination.
 - Develop a plan for the terminating PAC to continue filing FEC reports until agency approves termination.
 - Terminate any state registrations or incorporation as needed.
 - Once termination is approved, store terminated PAC records for three years.
 - Once the FEC approves termination, amend the acquiring PAC's Form 1 to remove target PAC as an affiliated entity.

Identifying and addressing any compliance issues before a merger or acquisition can help reduce costs and particularly the administrative burden of resolving problems that may have gone unaddressed in the acquired company.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our firm:

Robert Kelner	+1 202 662 5503	rkelner@cov.com
Bob Lenhard	+1 202 662 5940	rlenhard@cov.com
Zack Parks	+1 202 662 5208	zparks@cov.com
Derek Lawlor	+1 202 662 5091	dlawlor@cov.com

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