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Election Law Compliance for High Net Worth Individuals and Family Offices

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Election and Political Law

With less than one month to go before the 2018 elections, the ground is shifting for major political donors. Developments over the last several years, and especially in the last few months, show that the rules of the road are changing with respect to many of the common election law issues faced by high net worth individuals. These complex rules present an array of compliance traps for the unwary. To help high net worth individuals and their family offices navigate this thicket, this advisory describes steps high net worth individuals can take to ensure compliance.

Vetting Contributions to Political Organizations

The most common election law compliance issues faced by high net worth individuals and family offices involve vetting personal political contributions. Recipient groups take many forms: federal, state, or local political candidates; political parties; political action committees; Super PACs; section 527 political organizations; 501(c)(4) social welfare organizations; 501(c)(6) trade associations; ballot measure committees; and LLCs and other for-profit entities, to name a few. Before writing a check or wiring funds to one of these groups, however, donors should know that the mere act of contributing to a political cause can expose them to legal liability, business losses, enforcement proceedings, and reputational harm. It is therefore essential that donors and their family offices implement a process to vet proposed contributions in order to identify these concerns before the contribution is made. Areas of special attention should include the following.

Contribution limits. The federal government, most states, and many localities impose limits on the amounts individuals may contribute to candidates and other political groups. To avoid an inadvertent excessive contribution, donors should establish a review process that ensures proposed contributions are within the limits. That review process should take into account prior contributions to the same recipient to ensure that the contributions, in the aggregate, do not exceed the applicable limit. Donors should be especially cautious about contributions to "joint fundraising committees," which allow donors to contribute to multiple candidates and committees with a single check. Before donating to such a committee, donors should ensure they have not previously contributed to any of the recipient committees in a manner that may cause the contribution limits to be exceeded when aggregated with the new contribution made through the joint fundraising committee.

Contribution Chains. Major donors should be wary of circumstances suggesting that a recipient group will simply serve as a conduit, passing the donor's contribution along to another entity. At the federal level and in many states, it is unlawful to make a contribution in the name of another by, for example, funneling a contribution to a Super PAC or campaign through another entity. In recent years, those involved in making contributions to political committees through nonprofit organizations have been the targets of major state enforcement actions. For additional analysis of recent enforcement activity in this area, please see our recent client advisory concerning "earmarked" contributions to politically active organizations here.

"Major Donor" Reporting. Occasionally, the mere act of making a political contribution can trigger a requirement that the donor file a report with state regulators. In California, for example, "major donors" that make California state or local contributions totaling $10,000 or more in a calendar year must file reports. High net worth individuals should be aware of these reporting requirements before they make a state or local contribution.

Disclosure. If individuals care about public disclosure of their contributions, then it is important to clarify in advance of making the contribution whether the recipient will be required to disclose it. This is not necessarily the same thing as asking whether the recipient *intends* to disclose it. Many tax-exempt organizations routinely tell donors that their contributions will not be disclosed. It may nonetheless turn out that the recipient uses the funds in a manner that *requires* public disclosure. This summer, a federal judge in *CREW v. FEC* held that non-profits and other groups that pay for certain advertisements expressly advocating the election or defeat of a federal candidate must disclose the names of donors who contributed for the purpose of influencing federal elections. Although questions still remain about the contours and scope of this newly-imposed disclosure requirement, the FEC recently issued interpretative guidance. In that guidance, the FEC stated that, when these non-profit and other groups make federal independent expenditures, they should report the names of those who made a contribution of more than $200 during the reporting period and specifically indicate the names of those donors who made those contributions for the purpose of furthering any independent expenditures. Reportable "contributions" are those "earmarked for political purposes, which contributions are intended to influence elections." Donors should therefore now be aware that contributions to 501(c)(4) social welfare organizations and other groups that pay for independent expenditures are more likely to be subject to disclosure requirements. These issues are best explored and resolved before a contribution is made.

Pay-to-play concerns. Over the past 25 years, regulators at the federal and state level have adopted so-called "pay-to-play" laws that restrict political contributions to state or local officeholders, candidates for state or local office, political parties, and other groups by entities that seek to do business with state or local government agencies. These rules also sometimes restrict contributions made by owners, partners, executives, directors, and employees of these businesses, as well as by the family members of these individuals and their affiliated political committees. Those who work in the municipal securities industry have been dealing with the Municipal Securities Rulemaking Board's pay-to-play restrictions since the mid-1990s. In 2010, the SEC adopted its own pay-to-play rules, as did the Commodity Futures Trading Commission. And a range of states, localities, and individual state or local public pension funds have adopted their own rules.

The SEC rule, which is the most prominent, restricts political contributions by certain executives and other "covered associates" of investment advisers. If political contributions are made by these covered associates to state or local officials who are in a position to influence the award of public fund business (or candidates for such offices) or to officials who can appoint such individuals, then the covered associate's firm could be barred for two years from accepting compensation from that public fund. The SEC rule also restricts soliciting or coordinating contributions to state parties and to individuals who seek or hold certain state or local offices.

These pay-to-play rules are extremely complex, not least because of the overlap among the SEC's rules, applicable state and local laws, and the policies of particular public pension funds. To ensure compliance with these rules, high net worth individuals should work closely with their compliance departments or legal counsel to vet all proposed contributions and fundraising activities for pay-to-play concerns. Questions to consider in the process include the following:

- Would the contribution violate applicable pay-to-play restrictions or foreclose future business opportunities with state and local government agencies or instrumentalities?
- Would an "assurance letter" from the recipient organization reduce the risk by making clear that the recipient organization will not directly or indirectly use the contribution in a manner that could potentially result in pay-to-play restrictions?
- Even if the contribution does not technically violate a pay-to-play rule, would the attention surrounding the contribution make it less likely that a state or local government entity would do business with the donor's employer? For example, contributions to Super PACs are frequently permissible. Nevertheless, a contribution to a Super PAC that supports a candidate to whom the donor could not contribute directly might deter a government agency from doing business with the donor's company.

Compliance Red Flags. Donors should vet political contributions like they do investments, looking out for red flags before donating. Questions to consider include:

- Is there any indication that the organization is merely serving as a conduit for contributions to other groups?
- How does the organization spend its money?
- Has the organization received negative press?
- Do any politicians or public officials serve on the board of the organization or among its officers?
- Is there a history of complaints and enforcement actions against the organization?
- If the organization pays for independent expenditures, are appropriate firewalls adopted to ensure that it does not illegally coordinate its activities with campaigns or political parties?
- Will the donor be required to pay the gift tax?
- Do the individuals who sit on the organization's board have a track record of compliance?
- Is the organization advised by experienced legal counsel?

Hosting Fundraisers

Compliance traps for high net worth individuals often arise when hosting fundraisers for candidates. At the federal level, with some important exceptions, corporate resources may not be used to host candidate fundraisers. Use of corporate conference rooms, caterers, customer lists, and support staff can result in an illegal corporate contribution to the benefiting campaign. Over the years, the Federal Election Commission has several times pursued enforcement cases against CEOs and other corporate executives who tasked their secretaries or other corporate support staff with helping to organize campaign fundraising events attended by individuals outside the company. Even paying for these costs personally can raise compliance issues unless the campaign is notified of the payment so that it can be treated and reported as an in-kind contribution, which counts against the donor's contribution limits. Corporate executives should therefore consult with their compliance team before engaging in campaign fundraising activity.

High net worth individuals should also be careful about using corporate resources to actually make contributions. The Commission has pursued fines against corporations that used paid lobbyists or other consultants to physically convey corporate executives' personal contribution checks to federal candidates.

Avoiding Coordination

Following the Supreme Court's *Citizens United* decision and related decisions from other courts, high net worth individuals can make unlimited contributions to Super PACs that make independent expenditures in support of or opposition to federal candidates. Super PACs, however, cannot coordinate their activities with campaigns or their agents. Otherwise, the Super PAC loses its independence and its expenditures become impermissible and excessive in-kind contributions to the benefitting campaigns.

Because high net worth individuals are often aggressively pursued for contributions and fundraising by both Super PACs and candidates, these individuals are ripe targets for allegations that they have facilitated coordination between candidates and Super PACs. It is, therefore, important that high net worth individuals do not become a conduit for confidential information flowing from the campaigns to the Super PACs (or vice versa). Many high net worth individuals avoid coordination concerns by limiting their involvement with Super PACs to simply writing a check. If individuals with close ties to campaigns do more than that—by, for example, advising the Super PAC on its media buys or advertisement strategies—they risk unwittingly passing along confidential campaign information gleaned from the campaigns and undermining the Super PAC's independence.

Gift Concerns

Federal, state, and local laws often restrict the giving of gifts to government officials. High net worth individuals, who may have friendships and professional relationships with public officials, should be mindful of these rules. While many gift rules exempt gifts given on the basis of personal friendship, that exception is often a narrow one and may not apply where, for example, there is not a history of *mutual* gift-giving of comparable amounts. Prior to providing any gift to a public official, including meals, travel, and entertainment, high net worth individuals should ensure that the proposed gift is reviewed by their compliance department or legal counsel.

STOCK Act

In 2013, Congress passed the Stop Trading on Congressional Knowledge Act, which clarifies that insider trading cases can be brought on the basis of *government* inside information, including information from Congress. This means that a case can potentially be brought against *anyone* who buys or sells securities on the basis of material, non-public information obtained from the government. When high net worth individuals and other investors meet with government officials, they should consider taking steps before the meeting to ensure that the government official does not share material non-public information. And, if there is any question about whether the high net worth individual received material non-public information during the meeting, this information should be conveyed to legal counsel before making any trading decisions based on that information.

If you have any questions concerning the material discussed in this client advisory, please contact the following members of our Election and Political Law practice:

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