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Government Contractors Face Growing Risks from Laws Regulating Political Contributions

The landmark Supreme Court ruling in the *Citizens United* case paved the way for explosive growth in political spending during the 2012 election cycle. However, for government contractors and their principals, a growing number of “pay-to-play” laws restrict political contributions and fundraising, and can result in severe penalties, including the loss of contracts. This alert looks at recent developments with pay-to-play laws and identifies key steps for staying in compliance.

States and Municipalities

So-called pay-to-play laws have proliferated in recent years, with states and municipalities leading the way in imposing limits or even outright bans on political contributions by government contractors, their principal owners, officers, and those employees involved in the contracting process. Many of these laws also restrict political fundraising, as well as require contractors to disclose political contributions in conjunction with bids and during the pendency of a contract.

Pay-to-play laws vary widely, making for a daunting compliance challenge for companies doing business in multiple jurisdictions. For example, some pay-to-play laws extend contribution restrictions to the contractor’s PAC and even the spouses and dependent children of covered individuals. Some require registration or specify the manner in which contractors must notify their covered personnel. Some pay-to-play laws apply only to sole source or no-bid contracts, while others apply to competitively bid contracts.

Beyond the variation and complexity, pay-to-play laws stand apart from other campaign finance laws because penalties can strike at the bottom line. In addition to civil and criminal penalties, violators can find their bids disqualified and contracts voided.

Federal Government

At the federal level, contractors have long been banned from making contributions to federal candidates. A U.S. district court **recently upheld the ban** and ruled that it even bars personal contributions by sole proprietors with government contracts. The Federal Election Commission also announced that government contractors may not donate to independent expenditure-only committees, commonly known as Super PACs.

In addition, the Securities and Exchange Commission has stepped up enforcement of pay-to-play rules governing the financial services industry. In September, **a major Wall Street firm paid \$12 million to settle charges** that one of its investment bankers did campaign work out of firm offices for the Massachusetts State Treasurer, while the firm simultaneously sought lucrative contracts from the state. The SEC has also **warned municipal securities dealers** to implement stronger compliance measures to prevent unlawful intervention in campaigns.

Recent Developments and Things to Keep an Eye On

A number of recent developments involving pay-to-play laws are worth noting, and there are more changes on the horizon.

- **District of Columbia** Mayor Vincent Gray has **introduced a bill** prohibiting the award of contracts if a company, its affiliated entities, or its officers, directors, and others with a controlling financial interest make a political contribution to officials in a position to influence the award of the contract. Misdemeanor charges would carry a penalty of up to \$5,000 or six months imprisonment, while a felony charge could mean a \$10,000 fine and five years in prison.
- **Super PAC contributions** may be the next target of pay-to-play laws. Voters in **Gloucester Township, New Jersey**, overwhelmingly approved a November ballot measure requiring vendors to disclose contributions made to Super PACs.

- The U.S. Supreme Court in June declined to review a **federal appeals court** ruling that upheld **New York City's pay-to-play law**. The city ordinance imposes reduced limits on contributions by entities and individuals "doing business with" the city.
- A federal appeals court will soon hear a challenge to **Hawaii's pay-to-play law**, which bans contractors from making political contributions to any state or local candidate committee after execution and through completion of a state contract. Like many pay-to-play laws, violations of Hawaii's law can result in civil fines or criminal prosecution. A lower court **upheld the law** in March 2012.
- The Municipal Securities Rulemaking Board has **asked the SEC to approve rules** requiring detailed disclosure of contributions to **municipal bond campaigns**, which are used to finance schools, roads, and other projects.

Approaching Compliance

An effective compliance program can dramatically reduce the risks posed by pay-to-play laws. This starts with a risk assessment based on where the company is doing (or expects to do) business, where covered personnel are concentrated, and where laws impose the most severe penalties. Covered personnel should receive training and periodic reminders about pay-to-play laws. Some companies may also need to pre-clear political contributions by certain personnel. Since preventive measures are imperfect, periodic review of campaign contribution databases can catch a problematic contribution so that it can be unwound within a prescribed period.

2013 is certain to bring more pay-to-play restrictions and disclosure requirements. Venable's **Political Law Practice Group** helps clients navigate these complex laws and implement an effective compliance programs. Also, check our blog, www.PoliticalLawBriefing.com, for developments in this area.

If you have any questions or comments, please contact any authors listed for this alert.