W. Hardy Callcott

August 3, 2009

By Email to comments@sec.gov

The Commissioners
U.S. Securities and Exchange Commission
100 F. St. NE
Washington, DC 20549

Re: Political Contributions by Certain Investment Advisers, File No. S7-18-09

To the Commissioners:

I submit this comment letter concerning the Commission's proposed rule concerning "pay to play" practices by investment advisers. The U.S. Supreme Court's decision in *Randall v. Sorrell*, 548 U.S. 230 (2006), indicates that the SEC cannot blindly mimic the provisions of MSRB Rule G-37, on which the Commission explicitly patterns the proposed rule. After the Court's decision in *Randall*, which the proposing release does not even mention, the provisions of the proposed rule banning or limiting campaign contributions violate the right to freedom of speech as guaranteed by the First Amendment to the U.S. Constitution.[1]

The proposed rule generally forbids political contributions by an investment adviser or an individual associated with an investment adviser (a "covered associate") who seeks to provide advice to state and local governments, to an elected official in a position to influence the selection of an adviser for those state and local governments. An exception to the rule allows a covered associate to make contributions not in excess of $250 to state or local officials for whom the individual is eligible to vote, although such an individual may not make contributions to state or local political parties.

The proposed rule is modeled on MSRB Rule G-37, which the U.S. Court of Appeals for D.C. Circuit upheld in *Blount v. SEC*, 61 F.3d 938, 941 (D.C. Cir. 1995), *cert. denied*, 517 U.S. 1119 (1996). In that case, the Court held that compelling interests justified the Rule, that the Rule effectively advanced those interests, that (in its view) the Rule was

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[1] I am a partner in the broker-dealer group at Bingham McCutchen LLP, where I advise investment advisers and other financial services firms on compliance with the federal securities laws and rules. I was formerly General Counsel of Charles Schwab & Co., Inc., and previously was Assistant General Counsel for Market Regulation at the SEC. I am currently chair of the ABA Business Law Section's Subcommittee on Trading and Markets. I also have litigated campaign finance cases, *see Common Cause v. FEC*, 906 F.2d 705 (D.C. Cir. 1990). I submit this petition solely in my personal capacity.

narrowly tailored to advance those interests, and thus that the Rule did not violate the First Amendment. *Id.* at 944-48.

However, the *Blount* decision is in significant part inconsistent with the Supreme Court's later decision in *Randall v. Sorrell*. *Randall* holds that "contribution limits that are too low . . . harm the electoral process" in violation of the First Amendment. 548 U.S at 249.[2] The Court applied this holding to invalidate a Vermont statute that limited state campaign contributions to $200. *See id.* at 249-53. The contribution limit contained in the proposed rule -- $250 -- is constitutionally indistinguishable from the $200 limit held unconstitutional in *Randall*, and is far lower than the range of contribution limits the Court suggested might be constitutionally permissible. *Id.* (noting that the Supreme Court had never approved a contribution limit less than $1000 and that no states other than Vermont have limits less than $500).[3]

Moreover, the contribution limits in the proposed rule have a variety of other features that the *Randall* court found to be constitutionally objectionable:

- First, the proposed rule applies to all states, including those in much larger states such as California and New York in which campaigns are substantially more expensive than in Vermont. *See id*. at 251-52 (comparing unconstitutional contribution limits in Vermont with a higher contribution limit in Missouri approved in *Nixon* v. *Shrink Missouri Government PAC*, 528 U. S. 377 (2000)). The Court's ruling indicates that a $250 contribution limit would not be permissible if it applied to a larger state with higher election costs than Vermont.

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[2] The cites in this letter are to the controlling plurality opinion of Justices Breyer, Alito and Roberts. Justices Kennedy, Scalia and Thomas concurred separately -- each of them would have held that all political campaign contribution limits are unconstitutional in all circumstances. In sum, a clear six-vote majority of the Supreme Court would hold the contribution limits in the proposed rule to be unconstitutional violations of free speech.

[3] The Commission cannot distinguish *Randall* on the ground that the statute at issue applied to all state residents, but the proposed rule applies only to investment advisers and covered associates seeking to do business with state and local governments. The Supreme Court has made it clear that the government may not require the waiver of an individual's First Amendment rights to free speech and association as a condition of engaging in that individual's chosen profession. *See, e.g., Elrod v. Burns*, 427 U.S. 347, 357-61 (1976); *Perry v. Sindermann*, 405 U.S. 593, 597-98 (1972); *Pickering v. Board of Education*, 391 U.S. 563, 568 (1968).

- Second, the proposed rule completely bars covered associates from making any contribution to state or local political parties. Such a bar "threatens harm to a particularly important political right, the right to associate in a political party." *Randall*, 548 U.S. at 256.[4] The proposed rule does not merely limit but in fact completely eliminates the ability of a covered associate to associate with his or her political party of choice. Therefore, this portion of the proposed rule is unconstitutional under *Randall* as well.

- Third, the proposed rule bars contributions not only of cash, but also of "anything of value" such as yard signs, buttons, coffee, doughnuts and other materials essential to volunteering with a political campaign. Such a bar, according to the Court "impede[s] a campaign's ability effectively to use volunteers, thereby making it more difficult for individuals to associate in this way." *Id*. at 260. As such, this portion of the proposed rule also is unconstitutional under *Randall*.

- Finally, the $250 contribution limit in the proposed rule is not indexed for inflation, with the result that "[i]ts limits decline in real value each year." *Id*. at 261. The failure to provide for inflation indexing renders Rule the proposed rule unconstitutional as well.

In sum, if there was any doubt that the $250 contribution limit in the proposed rule is constitutionally indistinguishable from the $200 contribution limit struck down in *Randall*, these other factors would clearly render the proposed rule an unconstitutional violation of free speech rights.[5]

The proposed rule as currently written falls afoul of the constitutional free speech lines drawn in *Randall.* To survive First Amendment scrutiny under *Randall*, the Commission **at a minimum** would have to: (1) raise the contribution limit in the proposed rule to at least $1000, (2) amend the proposed rule to allow for contributions of at least $1000 to political parties, (3) eliminate the "anything of value" restriction on contributions in kind and (4) index these contribution limits to inflation.

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[4] Note that the ban in MSRB Rule G-37(c)(ii) on contributions to political parties had not yet been adopted at the time *Blount* was argued, and thus the D.C. Circuit did not address, and did not approve, that ban.

[5] The interests in promoting a free and open market and just and equitable principles of trade found compelling in *Blount* and asserted in support of the proposed rule here are nearly identical to the interests in "'prevent[ing] corruption' and its 'appearance'" discussed in *Randall*, 548 U.S. at 247. No constitutional distinction in contribution limits could be justified based on this minor distinction in asserted government interests.

In addition, I would argue that the provision in the proposed rule allowing contributions only to a state or local government official for whom the covered associate is entitled to vote -- in other words, imposing a $0 contribution limit as to all other state or local government officials -- also cannot survive *Randall*. The "symbolic expression of support evidenced by a contribution," *Randall,* 548 U.S. at 247 (*quoting Buckley v. Valeo,* 424 U.S. 1, 21 (1975)) has long been deemed to be constitutionally protected free speech, and *Randall* specifically reaffirmed the importance of that right. No court has ever held that a citizen's core associational First Amendment rights could be restricted merely to candidates for whom the citizen is entitled to vote.[6] Whatever the merits of the parallel provision in MSRB Rule G-37 before *Randall*, it cannot survive as constitutional today.

Finally, *Randall* holds that volunteer activities on behalf of candidates enjoy core First Amendment protection, 548 U.S. at 259-60, and political contributions are a constitutionally protected "symbolic expression of support", *id.* at 247. Therefore it is difficult to understand how a ban on a campaign volunteer soliciting a contribution on behalf of his or her favored candidate could survive *Randall.* I urge the Commission to eliminate this ban as well.

With the changes I have outlined above, it is possible that a revised proposed rule, with higher, indexed contribution limits and without many of the accompanying restrictions, could survive constitutional scrutiny. I submit that even if the Commissioners disagree with the Court's opinion concerning the constitutionally protected status of campaign contributions, it is your duty to abide by the Court's ruling in good faith. For these reasons, the Commission should modify the proposed rule in a manner consistent with the constitutional parameters set forth in *Randall*. I would be happy to discuss this issue with the Commission or its Staff.

Sincerely yours,

W. Hardy Callcott

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[6] Unaccountably, the *Blount* decision simply did not address this aspect of Rule G-37. I suggest the Commission direct the MSRB to reconsider Rule G-37 in light of *Randall.* Otherwise, any cases brought under that rule also will be vulnerable to challenge.