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FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

OFFICE OF THE CHAIRMAN

November 1, 1999

BY HAND

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OFFICE OF THE SECRETARY
NOV 02 1999

Jonathan G. Katz
Secretary
Securities Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-0609

S7-19-99

Dear Mr. Katz:

I am writing to submit the following comments in response to the Securities and Exchange Commission's ("SEC") notice of propose rules published at 64 Fed. Reg. 43556 (August 10, 1999).

I. BACKGROUND

The SEC regulates investment advisers under the Investment Advisers Act of 1940. Pursuant to the Advisers Act, the SEC has the authority to adopt rules "reasonably designed to prevent, such acts, practices, and courses of business as are fraudulent, deceptive or manipulative." 15 U.S.C. §80b-6(4). The SEC has proposed a new rule at 17 C.F.R. § 275.206 (hereinafter referred to as "proposed rule 206(4)-5") in order "to prevent advisers from participating in pay to play practices and protect clients from the consequences of pay to play," 64 Fed. Reg. at 43560. That practice involves the making of campaign contributions by investment advisers in return for being considered for, or awarded, advisory contracts. If pay to play is successful, contracts are awarded on the basis of political influence and not merit. The proposed regulations also impose certain recordkeeping requirements on investment advisers who make direct or indirect contributions. Proposed 17 C.F.R. 275.204-2(e)(1).

Proposed rule 206(4)-5 would prohibit investment advisers from providing advice for compensation to a government entity for two years after (i) the adviser, or (ii) any of its partners, executive officers or solicitors, or (iii) any political action committee controlled by the adviser's partners or executive officers had made a contribution to an official of the government entity. 64 Fed. Reg. At 43561. A partner, executive officer, or solicitor of an investment adviser could contribute up to $250 in both the primary and general election campaign of an official for whom the person making the contribution would be entitled to vote. The proposed rule would also prohibit an adviser from soliciting contributions for an official of a government client while providing or seeking to provide advisory services to the government client. *Id.* In addition, the proposed rules would require an investment adviser that has government clients to maintain records of campaign contributions made by the adviser or any of its partners or executive officers.

Under the Federal Election Campaign Act ("the Act" or "FECA"), 2 U.S.C. §§ 431-455, no person may make contributions to any candidate and his or her authorized political committee with respect to any election for federal office which exceeds $1,000. 2 U.S.C. § 441a(a)(1). The Act also prohibits political committees from accepting any contributions in excess of the limitations of 2 U.S.C. § 441a(a)(1)(A). 2 U.S.C. § 441a(f). Pursuant to 2 U.S.C. § 434(a)(1), each treasurer of a political committee shall file and sign reports of receipts (including contributions) and disbursements required under the Act. Under the Commission's Regulations, the treasurer of a political committee is responsible for the accuracy of any information contained in reports filed with the Commission. 11 C.F.R. § 104.14(d).

On September 16, 1999, Commissioner Mason submitted a memorandum to the Commission discussing the instant SEC Notice of Proposed Rules. Federal Election Commission Agenda Document 99-102 (September 16, 1999)(Attachment 1). Commissioner Mason expressed his view that the proposed SEC rules are "directly at variance with the source and amount limitations of the FECA." *Id* at. 2. Commissioner Mason recommended that the Commission "instruct the regulations staff to prepare for Commission approval comments objecting to the rules as they are applied to contributions to Federal campaigns as being in conflict with the FECA." *Id.* at 1.

On September 20, 1999, the Commission's Office of General Counsel submitted a memorandum to the Commission analyzing the SEC's proposed rulemaking. *See* Attachment 2. The General Counsel's memorandum did not recommend that the Commission object to the proposed rules. Although considering "the validity of the proposed rules to be a close question with good arguments on both sides," the General Counsel's memorandum concluded that "the Commission may wish to consider a decision to refrain from commenting on them." *Id.* at 10.

On September 30, 1999, the Commission considered the memoranda submitted by Commissioner Mason and the Office of General Counsel. A discussion was held on whether the Commission should submit comments to the SEC objecting to its proposed rulemaking. Without objection, it was agreed that the Commission would not submit an official comment to the SEC. However, it was understood that individual commissioners would be free to submit their own comments to the SEC representing their own views and not those of the Commission as a whole.

II. DISCUSSION

As a general proposition, I do not believe that the FEC should be telling a fellow federal agency how to go about its business. This is particularly true with respect to the SEC which has its own statutory and policy concerns. In the Investment Advisers Act of 1940, Congress authorized the SEC to prohibit "specific evils" that the broad anti-fraud provisions of the statute were incapable of covering. 64 Fed. Reg. at 43560. The SEC has determined that pay-to-play activity constitutes such an evil and has sought to address that threat, in a narrow and limited manner with respect to a closely regulated industry, through proposed rule 206(4)-5.

In my view, a federal agency should be reluctant in objecting to a provision deemed essential by another federal agency to the effective administration of the statute with which it has been charged by Congress. Indeed, the Supreme Court has found that "[w]hen two statutes are capable of co-existence, it is the duty of the courts, absent a clearly expressed congressional intention to the contrary, to regard each as effective." *Morton v. Mancari*, 417 U.S. 535, 551 (1974); *see also Pennsylvania v. ICC*, 561 F.2d 278, 292 (D.C.Cir. 1977)("It is well established that when two regulatory schemes are applicable to a certain subject matter, they are to be reconciled and, to the extent possible, both given effect."). Certainly, if the courts must try to reconcile similar regulatory schemes, so should administrative agencies.

To date, Congress has not expressed its disapproval with SEC regulations which restrict the ability of a regulated entity to do business after it has made campaign contributions. Proposed rule 206(4)-5 is modeled after MSRB rule G-37 which applies a similar regulatory scheme to municipal securities dealers rather than investment advisers. In the years since passage of rule G-37, Congress has not overturned this provision. *See Grove City College v. Bell*, 465 U.S. 555, 568 (1984)("Congress' failure to disapprove the regulations . . . strongly implies that the regulations accurately reflect congressional intent."); *FEC v. Democratic Senatorial Campaign Committee*, 454 U.S. 27, 34-35 (1981)(Congress' failure to disapprove regulation is an "indication that Congress does not look unfavorably" upon FEC's construction of the Act).

Similarly, the courts have not found rule G-37 to be constitutionally or statutorily inappropriate when given the chance. In *Blount v. Securities and Exchange Commission*, 61 F.3d 938 (D.C.Cir. 1995) the United States Court of Appeals for the D.C. Circuit appeared to acknowledge that there is no *per se* prohibition against an SEC regulation in this area. At issue in *Blount* was a challenge brought to the validity of MSRB Rule G-37. In rejecting that constitutional challenge, the court treated the government interests sought to be addressed by the SEC as separate and distinct from the governmental interests addressed by the FECA:

> As we have already noted in *Austin* and *Buckley the legislature was interested*

> *in clean elections, whereas here the SEC is interested in clean bond markets.* Petitioner insists on the importance of this distinction, saying that the latter interest is less compelling than the former. As we see it, however, one of the primary reasons people object to bought elections is that a bought politician tends to make distorted choices, and the public's concern about a particular type of distorted choice (the choice of bond underwriter) does not logically stand on a lower plane than its concern about bought politicians generally.

61 F.3d at 58 (emphasis added). Although the court discussed the FECA contribution limits and their underlying governmental interests, the *Blount* court never found, as it could have,[1] that the SEC was prohibited, as a matter of law, from introducing contribution limits to this carefully regulated industry.

Even though the Congress and the courts generally have allowed the SEC to regulate in this area and seek to prevent the deleterious effects of the pay to play practice, we must still consider whether these regulations directly conflict with any specific provisions of the FECA enacted by Congress. In *Galliano v. United States Postal Service*, 836 F.2d 1362 (D.C.Cir. 1988), the court concluded that the specific requirements of the FECA could not be overturned or superseded by more general provisions found in other statutes. With respect to the name identification and disclaimer requirements found in FECA, for example, the court stated, " [i]f FECA requirements are met, then as we comprehend that legislation, *no further constraints* on names and disclaimers *may be imposed by other governmental authorities*." 836 F.2d at 1370 (emphasis added). On the other hand, the court found that solicitations for contributions were subject to "Postal Service scrutiny" where "[n]o provisions of FECA set standards for such representations and there is no reason to believe that the silence of that legislation was meant to exempt uncovered statements from all regulation" *Id.* at 1371. Similarly, in *National Republican Congressional Committee v. Legi-Tech Corp.*, 795 F.2d 190 (D.C.Cir. 1986), the court found that a specific FECA provision concerning dissemination of information from FEC reports must prevail over Copyright provisions of general application. The court stated, "[i]nasmuch as Congress expressly provided in FECA for public dissemination of the precise type of compilation at issue here, the provisions of the Copyright Act relied upon . . . dealing with compilations generally, *must be construed in a manner that will accommodate the Federal Election Campaign Act*." *Id.* at 192 (emphasis added) *citing MacEvoy v. United States*, 322 U.S. 102, 107 (1944).

In my view, it does not appear that the contribution provision of proposed rule 206(4)-5 directly conflicts with the FECA. Section 441a(a)(1)(A) states that "[n]o

[1] The importance of construing federal statutes to avoid constitutional questions when possible is well established. *See Ashwander v. Tennesse Valley Authority*, 297 U.S. 288, 348 (1936)(Brandeis, J., concurring)("When the validity of an act of the Congress is drawn in question, and even if a serious doubt of constitutionality is raised, it is a cardinal principle that this Court will first ascertain whether a construction of the statute is fairly possible by which the question may be avoided"). The *Blount* court could have avoided the constitutional issues raised before it by simply finding that Rule G-37 impermissibly intruded upon the FECA. The court, however, chose not to make such a finding.

person shall make contributions to any candidate and his authorized political committee which, in the aggregate, *exceed $1,000*." 2 U.S.C. §441a(a)(1)(A)(emphasis added). This provision of the FECA only prohibits contributions over $1,000; it does not authorize or guarantee that any person may make contributions up to $1,000. The FECA does not allow every "person," *see* 2 U.S.C. § 431(11), to make contributions up to a certain level. For example, the Act has long prohibited business corporations and labor organizations from making *any* contributions to candidates for federal office. 2 U.S.C. § 441b; 11 C.F.R. § 114.2(a); *FEC v. Massachusetts Citizens for Life,* 479 U.S. 238 (1986). Likewise, the Act prohibits federal campaign contributions by federal contractors, and prohibits all persons from soliciting for federal campaigns from federal contractors. 2 U.S.C. § 441c(a)(1) and (2); 11 C.F.R. § 115.2; *see also* 11 C.F.R. § 7.11 ("Commissioners and employees should be aware that contributing to candidates, political parties, or political committees subject to the jurisdiction of the Commission is likely to result in a conflict of interest.")[2]

Thus, to the extent that proposed rule 206(4)-5 is even considered a $250 limitation on contributions,[3] it is not in conflict with the Act's prohibition on contributions *over* $1,000. Moreover, it does not appear that the proposed SEC rules create a conflict that would preclude persons from carrying out their other responsibilities under FECA. Under the proposed SEC rules, persons still can satisfy the recordkeeping and reporting provisions of FECA, as well as comply with the contribution limits and prohibitions of the Act. There would be a conflict, on the other hand, if the SEC regulation proposed that contributions could be made over $1,000 or if the proposed regulations indicated that certain persons did not have to file reports or keep records required under FECA. This does not appear to be the case with proposed rule 206(4)-5.

At the same time, I would urge the SEC to take into account the existing recordkeeping requirements, reporting provisions, and contribution limits applicable to federal candidates, and consider whether several of these provisions may be sufficient for its purposes. For example, I note that the SEC's definition of "contribution" found at §275.206(4)-5(e)(1) does not appear to incorporate the exemptions to the definition of "contribution" found at 2 U.S.C. § 431(8)(B). Under the Act and Commission regulations, "the term 'contribution' does not include" a number of activities such as the value of services provided without compensation by any individual who volunteers on behalf of a candidate or political committee, 2 U.S.C. § 431(8)(B)(i), 11 C.F.R. §100.7(b)(3). *See also* 2 U.S.C. § 431(8)(B)(ii)(the term "contribution" does not include up to $1,000 worth of food, beverage and invitations given by individuals on behalf of a candidate for each election); 2 U.S.C. §431(8)(B)(iv)(the term "contribution" does not include up to $1,000 worth of travel expenses incurred by individuals on behalf of a

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[2] *See also United States Civil Service Commission v. National Association of Letter Carriers*, 413 U.S. 548, 556 (1973)(Court upheld constitutionality of provisions preventing federal government employees from "actively participating in fund-raising activities for a partisan candidate or political party").

[3] The SEC notice of proposed rulemaking maintains that "[p]roposed rule 206(4)-5 would not be a ban on political contributions, but rather a ban, or 'time-out,' on conducting advisory business with a government client for two years after a contribution is made." 64 Fed. Reg. at 43561.

candidate for each election). In my view, such activities—specifically exempted from the statutory definition of contribution—are protected under FECA.

For the convenience of the SEC, I have enclosed copies of the FECA and the Commission's Regulations.

Thank-you for your consideration of these comments.

Sincerely,

Scott E. Thomas
Chairman

Attachment:
1. Agenda Document No. 99-102 (September 16, 1999)(Commissioner Mason)
2. Agenda Document No. 99-103 (September 20, 1999)(Office of General Counsel)

Enclosures
1. Federal Election Campaign Laws (November, 1997)
2. Title 11, Federal Elections, Code of Federal Regulations (January 1, 1999).

AGENDA DOCUMENT NO. 99-102

Attachment 1

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FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

AGENDA ITEM
For Meeting of: 9-23-99

MEMORANDUM TO CHAIRMAN SCOTT THOMAS

CC: COMMISSION SECRETARY

FROM: COMMISSIONER MASON DM

DATE: SEPTEMBER 16, 1999

SUBJECT: PENDING SEC RULEMAKING

This is to request that you place on the agenda for the Commission's next open session a discussion of whether the Commission should submit comments on a pending rulemaking by the Securities and Exchange Commission proposing to extend the reach of the G-37 and G-38 rules, which restrict certain campaign contributions made by securities firms, regulated professionals, and consultants.

I. Recommendation

My recommendation is to instruct the regulations staff to prepare for Commission approval comments objecting to the rules as they are applied to contributions to Federal campaigns as being in conflict with the FECA.

II. Background

In 1994, the Municipal Securities Rulemaking Board adopted a rule governing "pay to play" in the municipal bond underwriting. The Securities and Exchange Commission approved the MSRB rules. While the rules generally govern contributions by regulated entities to the campaigns of state and local officials who have authority over bond issues, they have been interpreted to apply to contributions to Federal campaign committees of any affected state or local officials. The rule was challenged on constitutional grounds and upheld by the DC Circuit (*Blount v. SEC*, 61 F.3d 938 (D.C. Cir. 1995)). The plaintiff did not raise and the court did not consider any arguments regarding statutory conflicts with the FECA.

On August 11, 1999, the SEC published a notice proposing to extend the G-37 rules to cover firms and professionals who offer investment advisory services to state and local governments (most frequently related to the management of employee pension funds). Comments on the rulemaking are due on or before November 1, 1999.

More information is available at the SEC web site (http://www.sec.gov/rules/proposed/ia-1812.htm). I may submit supplemental information for Commissioners' consideration, time permitting. I did bring this issue to the attention of the General Counsel and regulations staff several weeks ago.

III. Discussion

The FECA is a comprehensive statutory scheme intended to regulate the financing (including disclosure) of campaigns for Federal office for the purpose of preventing corruption and the appearance of corruption in those campaigns. As such, it is clear that Congress intended the FECA to occupy the field, explicitly pre-empting state law which may conflict, but also implicitly pre-empting common law claims, and private actions (except as provided in the statute). In enacting FECA, Congress purposefully moved certain pre-existing provisions of Federal law affecting Federal campaigns into the new comprehensive Act.

The effect of the G-37 and G-38 rules as applied to Federal campaigns is to establish a new prohibited class (bond underwriting and investment advisory firms, including their SSFs) and to establish different (and lower) contribution limits for certain individuals (generally employees of and consultants to affected firms) in conflict with the FECA limits.

The FECA prohibits contributions to Federal campaigns from national banks, corporations, labor unions, government contractors and foreign nationals, but it explicitly permits banks, corporations, unions and government contractors to establish SSFs, which may so contribute. The FECA also explicitly permits partnerships and other non-incorporated entities to contribute to Federal campaigns. The G-37 rule identifies a different class of contributors (generally investment banks, which are treated entirely differently from national banks) and prohibits certain contributions from them even if they are partnerships rather than corporations, and prohibits contributions from SSFs established by this new class of contributors.

Certain employees and consultants of affected firms are limited to making maximum \$250 contributions to candidates for whom they are eligible to vote (conflicting with the FECA's \$1,000 limit on individual contributions and its rule allowing contributions from any non-foreign national person to any Federal candidate).

Not only are these restrictions directly at variance with the source and amount limitations of the FECA, but they are justified with reference to the same purpose (prevention of corruption). Regardless of the public policy merits of the proposal, application of these new limits to Federal campaigns would require amendment of the FECA, and this agency should not let pass without comment this encroachment on its exclusive jurisdiction under that Act.

AGENDA DOCUMENT NO. 99-103

Attachment 2

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FEDERAL ELECTION COMMISSION

Washington, DC 20463

September 20, 1999

MEMORANDUM

AGENDA ITEM

For Meeting of: 9-23-99

SUBMITTED LATE

TO: The Commission

THROUGH: James A. Pehrkon
Staff Director

FROM: Lawrence M. Noble
General Counsel

N. Bradley Litchfield
Associate General Counsel

Rosemary C. Smith
Acting Assistant General Counsel

Jonathan Levin
Senior Attorney

SUBJECT: SEC "Play-to-Pay" Rules: Its Impact with Respect to FECA

I. Background

On August 10, 1999, the Securities and Exchange Commission ("SEC") published proposed rules aimed at ensuring that political contributions by investment advisers do not influence the award of contracts to advise State and local governmental agencies with respect to public pension plan assets. The rules would not directly prohibit contributions by investment advisers. Instead, they prohibit advisers from providing investment advisory services for compensation to a government entity within two years after they have contributed to an official of the government entity. The rules would more directly prohibit such advisers from soliciting contributions to the official, and also require such advisers to keep records with respect to such contributions. These rules, when applied to Federal elections, would impose direct and indirect prohibitions that intersect with, or extend beyond, the requirements of the Federal Election Campaign Act of 1971, as amended ("the Act"), and, thus, their implementation may be problematic under an interpretation of 2 U.S.C. §437c(b)(1) granting the Commission exclusive jurisdiction with respect to the civil enforcement of the Act's provisions. The purpose of this memorandum is to discuss the issues presented with respect to contributions to the Federal campaign of such a State or local governmental official, e.g., a State comptroller running for the U.S. Senate. If the Commission concludes that the proposed regulations pose a problem under section 437c(b)(1), it may wish to file comments with the SEC.

II. Description of Proposed Rules

The SEC proposes to amend 17 CFR Part 275, which is entitled "Rules and Regulations, Investment Advisers Act of 1940. (The provisions of this law are found in Chapter 2D of Title 15 of the U.S. Code, 15 U.S.C. §§80a-1 through 80b-21.) The prohibitions are added to 17 CFR 275.206, and the recordkeeping requirements are added to 17 CFR 275.204-2. The statutory authority cited in the notice of proposed rulemaking ("NPRM") is 15 U.S.C. §§80b-4 (reporting by investment advisers), 80b-6(4) (prevention of fraud by investment advisers), and 80b-11(a) (SEC rulemaking powers). The prohibitions are modeled after Municipal Securities Rulemaking Board ("MSRB") rule G-37, which was approved by the SEC in 1994 to end "pay-to-play" practices by broker-dealers in the municipal securities market.

a. Prohibitions

It is noteworthy that the text of the proposed prohibition regulations begins by stating a statutory authority, i.e., that they are "a means reasonably designed to prevent fraudulent, deceptive or manipulative acts, practices, or courses of business within the meaning of [15 U.S.C. §80b-6(4)] ..."[1] Violations of 15 U.S.C. §80b are subject to civil penalties under section 80b-9.

The proposed regulations provide that an investment adviser that is eligible for registration with the SEC cannot provide advisory services for compensation to a government entity within two years after the adviser, or any of its partners, executive officers, or solicitors, make a contribution to an official of that government entity. Proposed 17 CFR 275.206(4)-5(a)(1)(i)-(ii).[2] This prohibition also applies to any political action committee ("PAC") controlled by the investment adviser or any of its partners, executive officers, or solicitors. Proposed 17 CFR 275.206(4)-5(a)(1)(iii). Contributions to a political party would not trigger the prohibitions unless the contribution is earmarked for, or known to be provided to, an official. 64 Fed. Reg. 43556, 43562, n.81 (August 10, 1999).

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[1] That provision states that it is unlawful for an investment adviser to use the mails or any means of interstate commerce to engage in any fraudulent, deceptive, or manipulative act, practice, or course of business, and that the SEC shall, through rules and regulations, prescribe means reasonably designed to prevent such fraudulent practices.

[2] Included in this group is anyone who becomes a partner, executive officer, or solicitor within two years after the contribution is made.

The regulations would prohibit an investment adviser that is eligible for registration with the SEC, or any of its partners, executive officers, or solicitors, from soliciting any person or PAC to make or "coordinate" a contribution to an official of a government entity to which the adviser is providing, or seeking to provide advisory services; or (as a loophole closer) "to do anything indirectly which, if done directly, would result in a violation" of the new rules. 17 CFR 275.206(4)-5(a)(2)(i)-(ii). The prohibition on solicitation or coordination is aimed at a number of practices, including "bundling" contributions from employees or by making contributions through a third party, such as in a "swap," i.e., where a soliciting person arranges that the adviser of Plan A give to the trustee of Plan B, while the adviser of Plan B gives to the trustee of Plan A. 64 Fed. Reg. at 43563. The proscription on indirectly doing what cannot be done directly is also aimed at investment advisers who compel contributions by persons who are not covered or who fund contributions made by others. *Id.*

There are a number of exceptions or exemptions to these prohibitions. The prohibitions at (a)(1) would not apply with respect to contributions made by any individual who was entitled to vote for the official at the time of the contribution and which, in the aggregate, do not exceed $250 to any one official, per election. Proposed 17 CFR 275.206(4)-5(b). In addition, upon application, the SEC would be able to exempt an advisor from the prohibition at (a)(1) upon consideration of a number of factors including whether the investment adviser had no actual knowledge of the contribution, had instituted procedures (prior to the contribution) reasonably designed to ensure compliance with that section, and had taken all steps to obtain a return and taken other remedial measures. Proposed 17 CFR 275.206(4)-5(d).

The proposed rules also define a number of the key terms. "Contribution" is defined as "any gift, subscription, loan, advance, or deposit of money or anything of value made for: (i) [t]he purpose of influencing any election for federal, state, or local office; (ii) [p]ayment of debt incurred in connection with any such election; or (iii) [t]ransition or inaugural expenses of the successful candidate for State or local office. "Government entity" means any State or political subdivision of a State, including: (i) any agency, authority, or instrumentality of the State or subdivision; (ii) a plan or pools of assets controlled by any entity listed in subsection (i); and (iii) officers, agents, or employees of any entity listed in subsection (i), acting in their official capacity. "Official" means "any person (including any election committee for that person) who was at the time of the contribution, an incumbent, candidate, or successful candidate for an elective office of a government entity: (i) if the office is directly or indirectly responsible for, or can influence the outcome of, the use of an investment adviser by a government entity; or (ii) if the office has authority to appoint any person who can influence the use of a government adviser. Proposed 17 CFR 275.206(4)-5(e)(1), (3), and (4).[3]

[3] The NPRM states that "[g]enerally, executive or legislative officers who hold a position with influence over the selection of an investment adviser are government officials under the proposed rule," and then states that the definitions of officials are substantively the same as those in MSRB rule G-37. 64 Fed. Reg. 43556, 43561 (August 10, 1999). In a conversation with one of the attorneys named as a contact in the

b. Recordkeeping obligations

The proposed regulations contain recordkeeping requirements on investment advisers. These records are to be maintained for a period of five years after the end of the fiscal year during which the last entry was made, including two years of maintenance in an appropriate office of the investment adviser. Proposed 17 CFR 275.204-2(e)(1). The regulations would require the maintenance of records of all direct or indirect contributions or payments by the investment advisor, any of its partners, executives, or solicitors, or PAC controlled by any of the aforementioned persons, to an official, a political party of a State or political subdivision, or a PAC. Proposed 17 CFR 275.204-2(l)(1)(iv). These must be chronological records of the name and title of each contributor, the name and title (including city, county, State or other subdivision) of the recipient, and the amount and date of the contribution or payment. Proposed 17 CFR 275.204-2(l)(2)(i)-(iii).

III. Intersection of Proposed Rules with FECA-regulated Conduct

As indicated above, the proposed SEC regulations would create prohibitions and requirements, with respect to a discrete group of persons, that do not exist in the Act. The Act, at 2 U.S.C. §437c(b)(1), states as follows: "The Commission shall administer, seek to obtain compliance with, and formulate policy with respect to, this Act and chapter 95 and chapter 96 of title 26. The Commission shall have exclusive jurisdiction with respect to the civil enforcement of such provisions." A broad interpretation of this provision may result in a conclusion that the SEC does not have the power to apply these regulations with respect to contributions to Federal candidates and committees because it would thereby attempt to regulate in an area that is exclusively under the Commission's jurisdiction. See the proposed definition of contribution above which includes elections to Federal office.

The first area of concern is the indirect prohibition on contributions. Since Federal elections are covered, these regulations would affect contributions with respect to a Federal candidacy of a covered official. Under 2 U.S.C. §441a(a)(1)(C), a person (such as an unincorporated investment advisor or an individual partner, executive officer, or solicitor) may contribute up to $1,000 per election to that candidate's authorized committee(s). Under 2 U.S.C. §441a(a)(2)(A), a multicandidate PAC may contribute up to $5,000 per election to the candidate's committee. The prohibition on providing advice

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Federal Register notice for the proposed regulations, the attorney informed this office that, as far as she knows, the MSRB rule has not been used with respect to legislators, such as members of a committee that has oversight over State pension funds affairs. She indicated that, in view of the fact that a committee itself cannot appoint a pension fund official, and that appointment by a legislature would more likely result from a vote by a whole legislative house or both houses, an individual legislator would not meet the definition of "official" by virtue of his office. She also stated that the fact that a legislative committee would be able to block an appointment would not be sufficient to conclude that a committee member is covered.

for compensation within a specific time window after a contribution may be viewed as a prohibition on contributions by a specific class of individuals that is not prohibited from contributing by the Act.

It may be argued that this is not a prohibition *on contributions*, and that the adviser or related individual or PAC is free to contribute but that there would merely be consequences on the ability of the investment adviser to deal with one particular client or group of clients. Nevertheless, the Commission's treatment of a similar question in the context of preemption of a State law may be illustrative of an approach that treats such a provision as a contribution prohibition. Advisory Opinion 1989-12 involved the question of whether the Act, under 2 U.S.C. §453, would preempt the application of two provisions of a State lottery law. One prohibited a vendor-contractor with the State Lottery Commission from contributing to any statewide candidate for a period of three years from the most recent awarding or renewal of the contract. The second provided that the Lottery Commission could not enter into contracts with a vendor who had contributed to a statewide candidate within the previous three years. The Commission concluded that the Act would preempt the second, as well as the first, provision with respect to contributions to statewide Federal candidates. The Commission stated that the adverse consequences of the second provision on vendors contributing to Federal candidates and the inevitable restraint upon vendors' political activity to avoid such consequences were not incidental or tangential results but, instead, resulted from the statute's specific and broad language and effectively acted as a contribution limitation. Advisory Opinion 1989-12.

The proposed SEC regulations contain direct prohibitions on solicitations by a discrete group of persons or individuals associated with investment advisers. The Act proscribes solicitation of contributions in specific, limited cases. These include limitations on the solicitable class for contributions to separate segregated funds ("SSFs"), and prohibitions of solicitations of Federal contractors and foreign nationals. 2 U.S.C. §§441b(b)(4), 441c, and 441e. Thus, the proposed regulations add prohibitions with respect to Federal elections that are not found in the Act. In addition, the explicit prohibition on doing anything indirectly that cannot be directly done overlaps with the Act's prohibitions on contributions in the name of another and, possibly, with the prohibition on coercing contributions by employees to an SSF (where the contribution is earmarked for or otherwise directed to a candidate). 2 U.S.C. §§441f and 441b(b)(3). Both the proposed solicitation prohibition and the prohibition related to indirect actions make unlawful certain activities that may not necessarily be proscribed by the Act. These include bundling, which may or may not result in excessive contributions, depending upon whether the bundler exercises direction or control over the contributions; and the above-described "swap," where a mere arrangement to contribute to each other's desired recipients might not quite qualify as a contribution in the name of another, if there is no direct or indirect reimbursement. See 11 CFR 110.6(d) and 2 U.S.C. §441f; compare the situation in Advisory Opinion 1996-33.

The proposed recordkeeping provisions, as they pertain to Federal contributions would impose obligations on entities (investment advising companies) that do not have to keep such records under the Act. Compare 2 U.S.C. §432(c) and (d); 11 CFR 102.9 and 102.6(c)(6). In addition, they impose a longer retention period and a restriction on the location of the records. Compare 2 U.S.C. §432(d); 11 CFR 102.9(c) and 102.6(c)(6).[4]

IV. Discussion of Validity of Proposed Regulations as Applied to Federal Elections

The "exclusive jurisdiction" granted to the Commission in 2 U.S.C. §437c(b) is arguably more ambiguous than the preemption provision of 2 U.S.C. §453 which provides that the Act's provisions and Commission regulations "supersede and preempt any provision of State law with respect to election to Federal office." The legislative history of section 453 is quite emphatic and prescriptive. On the other hand, the legislative history underlying section 437c(b), as well as the language of the section itself, is marked by a certain ambiguity.

The concept of "exclusive" jurisdiction for civil enforcement first appeared as "exclusive primary" jurisdiction in the 1976 Amendments (amended from the 1974 language of merely "primary" jurisdiction for civil enforcement at a time when many of the Act's provisions were still in the criminal code). Congress explained that the purpose of such exclusive jurisdiction was to "centralize the civil enforcement of the Act in the [Commission]," and that this concept was taken from *San Diego Building Trades Council, Millmen's Union, Local 2020 v. Garmon,* 359 U.S. 236 (1959). H.R. Rep. No. 94-917, 94th Cong., 2d Sess. 4 (1976). The House Committee described *Garmon*, stating:

> There the Court recognized that Congress, in enacting the National Labor Relations Act, "entrusted administration of the labor policy for the nation to a centralized administrative agency, armed with its own procedures, and equipped with its specialized knowledge and cumulative experience" (*Garmon*, 359 U.S. at 242). On that basis the Court stated that all complaints bottomed on an alleged violation of the NLRA are within that Agency's "exclusive competence" (*id* at 245) and that all other tribunals must therefore "yield to the primary jurisdiction of the National Board" (*id*). The Court's ruling in *Garmon* captures the essence not only of the NLRA's administrative scheme, but of this Act's enforcement procedures as well.

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[4] This list of interactions with the Act probably does not reveal the full extent of the interpretations of various activities in connection with Federal elections that are usually determined by the Commission. An indication of such issues may be gleaned from reading the "Interpretive Notice to Rule G-37" which is found on the MSRB's website; as stated above, the newly proposed investment adviser rules are patterned after Rule G-37. Some of the issues discussed are appropriate remedial or preventive measures, joint contributions, what constitutes volunteer activity (so as not to be covered by the proposed regulations), and variations on earmarked contribution concepts that may not coincide with conclusions as to earmarking that would be reached by the Commission.

Id. This interpretation was adopted by the House and Senate conferees for the 1976 Amendments. H. Conf. Rep. No. 94-1057 94th Cong., 2d Sess. 35 (1976)

In addition, during the post-conference report floor debate on the 1974 Amendments, which established the Commission and provided that it had "primary" jurisdiction, Congressman Hays, Chairman of the House Conferees, stated as follows:

> In order to assure that civil suits are not misused in a partisan manner, and that the complex and sensitive rights and duties stated in the act are administered expertly and uniformly, the act provides that all civil complaints predicated on or *pertaining in any manner* to titles I and III of the act or sections 608 through 617 of title 18 United States Code shall be channeled to the Commission. Under section 315 persons challenging the constitutionality of the act, retain their right to do so in court without exhausting administrative remedies to the extent the courts have jurisdiction under established principles. The delicately balanced scheme of procedures and remedies set out in the act is intended to be the exclusive means for *vindicating the rights and declaring the duties stated therein.* [Emphasis added in both places.]

120 *Cong. Rec.* 35,134 (1974).

The question that the 1976, along with the 1974, language may leave open is whether it means that the Commission has exclusive jurisdiction over violations of the Act and chapters 95 and 96 themselves or whether, as with preemption, the Commission has exclusive jurisdiction over any activity that comes within the purview of the Act, i.e., the receipt or disbursements of funds (money or otherwise) for the purpose of influencing a Federal election. The discussion by courts of the Commission's exclusive jurisdiction has not usually implicated this ambiguity because the question has been centered around the jurisdiction of the Commission in cases of persons asserting a private right of action, such as a right to sue under 26 U.S.C. §9011(b) or 2 U.S.C. §437g(a)(8).[5] These cases use the above history to emphasize the exclusive nature of the Commission's jurisdiction.

One case may shed some light, however, on how these concepts may applied when the conflict entails the application of another Federal statute. In *Galliano v. United States Postal Service,* 836 F.2d 1362 (D.C.Cir. 1988), an unauthorized political committee, advocating the re-election of Senator Phil Gramm, brought an action seeking review of a Postal Service decision applying its statute to mailings by the PAC that it

[5] See, e.g., *Democratic Party v. National Conservative Political Action Committee,* 578 F.Supp. 797 (E.D. Pa. 1983) (3-judge panel), *aff'd in part, rev'd in part sub nom. Federal Election Commission v. National Conservative Political Action Committee,* 470 U.S. 480 (1985); *Carter-Mondale Reelection Committee, Inc. v. FEC,* 642 F.2d 539 (D.C.Cir. 1980); *Stockman v. FEC,* 138 F.3d (5th Cir. 1998); see also *McNamara v. Johnston,* 522 F.2d 1157 (7th Cir. 1975)

considered to be devices for obtaining money by means of false representations in its mailed solicitations. The controversy began with a complaint filed with the FEC by Senator Gramm's PCC against the unauthorized committee, alleging violations of 2 U.S.C. §441d, among other sections. The PCC also filed an action based on State law in U.S. District Court, and then notified the Postal Service's General Counsel of the solicitations, resulting in a Postal Service administrative complaint.

The key issue in the court case at the appellate level was whether the Postal Service could impose constraints on the names and disclaimers of the appellant unauthorized committee beyond those imposed by the Act (and hence, by the Commission). The Commission filed an *amicus* brief in this case with respect to the reach of the Act. The court discussed the tension between the general false representation claims of the postal statute and the specific disclaimer and name identification provisions of the Act, i.e., at 2 U.S.C. §§441d and 432(e)(4), and focused on two competing principles. The first, emphasized by the appellant and the Commission, is that "a precisely drawn, detailed statute pre-empts more general remedies," and that "[w]hen there is no clear intention otherwise, a specific statute will not be nullified by a general one, regardless of the priority of enactment." *Galliano*, at 1367, quoting other cases (citations omitted). The second, emphasized by the Postal Service, is that "when two statutes are capable of co-existence, it is the duty of the courts, absent a clearly expressed congressional intention to the contrary, to regard each as effective," and "that when two regulatory systems are applicable to a certain subject matter, they are to be reconciled and, to the extent possible, both given effect." *Id.*, quoting other cases (citations omitted).

The court noted the arguments of the appellant and the Commission that, unlike the general postal statutes on fraud, the specific Act provisions "were framed with the particular problems Congress identified in political solicitations in clear focus, and with the first amendment in plain view." *Galliano,* at 1368. The court discussed the above-cited legislative history and stated that it was consistent with the Commission's view that "responsibility for the civil enforcement of matters specifically covered by the Act" were placed "exclusivcly in the Commission's hands in the first instance." *Id.* The court resolved the case by also taking the second principle into account, however. It concluded that the Commission is the "exclusive arbiter" of questions concerning the name identifications and disclaimers of organizations soliciting political contributions but that false representations that are not covered by FECA within the mailings, e.g., statements as to what the committee raised and contributed, would be subject to the more general postal law, noting that nothing in the Act limits the Postal Service's enforcement authority with respect to this issue. *Galliano,* at 1370.

The guiding principles that can be gleaned from this decision are the idea of the Act's specificity as to the conduct in question and the constitutional principles specifically considered in the enactment of the Act. The court stated that, in enacting the name identification and disclaimer principles, Congress specifically focused on First

Amendment concerns. Congress deliberately struck a fine balance of interests, and the Act's provisions were meant to provide a safe haven from further restraints for candidates and political committees with respect to names and disclaimers, such as the more general restraints imposed by the postal statute. *Galliano,* at 1370.

In applying these concepts to the newly proposed SEC rules, we could conclude that the problems attendant to the postal statute in *Galliano* do not apply. Instead of provisions generally covering communications of all sorts, the newly proposed rules focus on a specified group of persons with the intent of implementing a very specific regulatory mandate in mind - - the prevention of fraud in the investment adviser's field. Although the Act's provisions regulate receipts, disbursements, and recordkeeping with respect to Federal elections, they do not focus on the specific needs of deterring or preventing corruption in a specifically regulated area by the entity granted the mandate to regulate that area. Moreover, although the court in *Galliano* emphasizes the constitutional motivation for giving the Act a certain primacy in the situation presented, it should be noted that the U.S. Court of Appeals for the D.C. Circuit has already upheld the very similar MSRB rules on first amendment grounds. See *Blount v. Securities and Exchange Commission,* 61 F.3d 938 (D.C.Cir. 1995), *cert. denied,* 517 U.S. 1119 (1996).[6]

There also appears to be a tension in the wording of section 437c(b) and in the language of the legislative history. Section 437c(b) provides to the Commission "exclusive jurisdiction with respect to the civil enforcement of *such provisions*," meaning the Act and chapter 95 and 96 of title 26 (*emphasis added*). It does not provide exclusive jurisdiction with respect to provisions of other Federal laws that may regulate spending for the purpose of influencing a Federal election. (One can look at certain present and former provisions of the Hatch Act, the above-cited MSRB rules, which the Commission did not comment on, and perhaps, at the rules for qualifying for, and operating as, a tax exempt organization under 26 U.S.C. §501(c)(3), including the inability of qualified entities to sponsor a PAC.[7]) On the other hand, the legislative history of both 1974 and 1976, including the use of *Garmon* may be interpreted as emphasizing the Commission's exclusive competence as to the conduct involved, and centralizing coverage with respect to that conduct rather than to the particular provisions of the Act.[8] To counter that argument, it may be pointed out that the 1976 legislative history introduces the discussion of the *Garmon* analogy by stating that the new statutory language describes the intent to centralize the civil enforcement *of the Act*," not of all receipts and disbursements for the purpose of influencing a Federal election (emphasis added).[9]

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[6] The issue of the Commission's jurisdiction was not raised in *Blount*.

[7] However, 2 U.S.C. §438(f) explicitly recognizes the dual jurisdiction of the Commission and the IRS by requiring both agencies to work together to promulgate mutually consistent regulations.

[8] It is interesting to note that the *Garmon* case entailed the jurisdiction by the NLRB as opposed to the application of State law. It did not entail a conflict with the jurisdiction of another Federal agency, or the application of another Federal statute.

[9] The Bankruptcy Court's discussion in *In re Fund for a Conservative Majority ("FCM")*, 100 B.R. 307 (1989) may be somewhat illustrative of this point. In this case, which involved a political committee

It may also be argued, however, that the more specific statute is, in fact, the Act, and not the statutory provisions enforced by the SEC (e.g., the Investment Advisers Act). The Act applies specifically to receipts and disbursements for the purpose of influencing a Federal election, while the above-cited provisons of the Investment Advisers Act are anti-fraud and reporting provisions that do not specifically address elections or election-influencing activity. Only by regulation does the SEC put itself into a position to regulate election-influencing activity. Two questions arise. One is the question of where specificity is relevant, i.e., whether with respect to the activity regulated or with respect to the specific industry and persons regulated. The other question is whether, assuming the relevance of both categories, an agency without a specific statutory mandate to regulate campaign finance, may include such activity within its jurisdiction by virtue of regulations.

This office considers the validity of the proposed rules to be a close question with good arguments on both sides, and the Commission may wish to consider a decision to refrain from commenting on them. In making such a decision, however, the Commission should also consider the implications of an agency construing its authority to include campaign activity when the statute it administers does not specifically grant it that authority.

declaring bankruptcy under Chapter 11, the court determined that the existence of the Commission's debt settlement procedures would not override the court's exclusive jurisdiction to adjudicate bankruptcy petitions, despite the Act's exclusive jurisdiction provision and despite arguments as to the Act's specificity. *FCM,* at 310-311. In a footnote discussion, the court discusses the "exclusive jurisdiction " provision as referring to violations of the Act, and then states: "In the instant case, while the FEC anticipates a conflict between FECA and provisions of the Bankruptcy Code, it has not directed the Court's attention to a specific violation of the FECA by the debtor at this time." *FCM,* at 311, n.8.