UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

NEW YORK REPUBLICAN STATE COMMITTEE; and TENNESSEE REPUBLICAN PARTY, Plaintiffs, v. UNITED STATES SECURITIES AND EXCHANGE COMMISSION, Defendant.	)	Case No. 1:14-cv-01345-BAH

BRIEF OF CAMPAIGN LEGAL CENTER AND DEMOCRACY 21 AS *AMICI CURIAE* IN SUPPORT OF DEFENDANT AND IN OPPOSITION TO PLAINTIFFS' MOTION FOR PRELIMINARY INJUNCTION

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STATEMENT OF INTEREST

Amici curiae Campaign Legal Center and Democracy 21 are nonprofit organizations that work to strengthen the laws governing campaign finance, governmental ethics and political disclosure. *Amici* have participated in several of the Supreme Court cases cited by plaintiffs as forming the basis of their First Amendment challenge, including *Citizens United v. FEC,* 558 U.S. 310 (2010), *FEC v. Wis. Right to Life*, 551 U.S. 449 (2007) ("*WRTL*") and *McCutcheon v. FEC*, 134 S. Ct. 1434 (2014). *Amici* thus have substantial expertise in the legal issues raised in this case, and a demonstrated interest in the challenged Securities and Exchange Commission ("SEC") regulations.

All parties have consented to *amici*'s participation in this case.

INTRODUCTION & SUMMARY OF ARGUMENT

The SEC regulations challenged here are based on a simple proposition. *See Political Contributions by Certain Investment Advisers*; Final Rule, 75 Fed. Reg. 41,018 (July 14, 2010); 17 C.F.R. §§ 275.204-2, 275.206(4)-3, 275.206(4)-5 (the "Rule"). Large campaign contributions from an investment advisor to state entities from which the advisor seeks business are likely to give rise to quid pro quo exchanges, or at a minimum, the appearance of such exchanges. That is the premise not only of the challenged Rule, but also of the Municipal Securities Rulemaking Board ("MSRB") Rule G-37, which was upheld by the D.C. Circuit in *Blount v. SEC*, 61 F.3d 938 (D.C. Cir. 1995), as well as of numerous federal, state and municipal laws regulating political activities by governmental contractors.

Despite the broad acceptance of the proposition that governmental contracting should be insulated from pay-to-play activities, plaintiffs New York Republican State Committee and Tennessee Republican Party challenge the Rule as both beyond the SEC's statutory authority and contrary to the First Amendment. Plaintiffs are unlikely to succeed on either of these claims, and their motion for preliminary injunction should be denied. Furthermore, both plaintiffs lack standing to bring this action and their complaint accordingly should be dismissed.

Amici's primary experience lies in the area of campaign finance, so this memorandum will focus on plaintiffs' First Amendment claims, *see* Compl. ¶¶ 88-98 (Doc. 1), and on issues of standing. However, *amici* agree that the adoption of the challenged Rule falls well within the SEC's authority under Section 206(4) to promulgate regulations "that define, and prescribe means reasonably designed to prevent, such acts, practices, and courses of business as are fraudulent, deceptive, or manipulative." 15 U.S.C. § 80b-6(4). Further, *amici* believe that the challenged Rule should be analyzed as a measure regulating conflicts of interest and pay-to-play abuses in the market for state investment advisory services, not as a contribution limit, because the Rule regulates only registered investment advisors' eligibility for state business if they make contributions to government officials who have some role in deciding which advisors receive that business. That said, plaintiffs' First Amendment claims rely upon Supreme Court precedents that analyze campaign finance laws, and in that context, contribution limits—as opposed to expenditure restrictions—are the Rule's closest analogue for the purposes of constitutional review. For this limited purpose only, *amici* treat the Rule as a regulation of campaign contributions.

As a threshold matter, plaintiffs have no basis to assert standing to bring this case. They can make no credible claim that they have suffered a direct injury, because the Rule neither regulates their conduct, nor subjects them to any potential legal penalties or burdens. Plaintiffs also cannot claim associational standing to bring this action on behalf of the general class of covered investment advisors they claim as "members" because plaintiffs offer no actual evidence of any affiliation with these individuals and have not even identified any specific "member" covered by the Rule who wishes to make a prohibited contribution. In addition, the interests of investment advisors and plaintiffs differ and thus the participation of such investment advisors is necessary to litigate this challenge. Pay-to-play practices in the award of state investments implicate the fiduciary duties owed by the investment advisors to the pension plans they advise and potentially defraud their current and prospective clients. *See, e.g.*, 75 Fed. Reg. at 41,019. Plaintiffs cannot represent this perspective.

Plaintiffs' First Amendment case also suffers from at least three defects. First, plaintiffs all but disregard the Court of Appeals' decision in *Blount* to uphold a materially-identical regulation. They make an attempt to argue that the *Blount* Court relied on "outdated" jurisprudence, but can offer no case to support their claim that the Supreme Court's approach to the review of contribution limits has changed since *Blount*. Pls.' Mem. Supp. Prelim. Inj. (Doc. 7-1) ("PI Br.") at 25.

Second, plaintiffs argue that the Rule does not pass constitutional muster because it was not adopted to combat quid pro quo corruption, but turn a blind eye to broad swaths of the record that confirm that this is precisely the objective of the Rule: it simply takes aim at quid pro quo corruption in the market for state investments, not in the sphere of elections. But as the *Blount* Court noted, "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 944.

Third, plaintiffs argue that the Rule represents an impermissible "prophylaxis-upon-prophylaxis" approach that "relies in large part on wholly unsubstantiated speculation that some political contributions may in fact result in *quid pro quo* corruption." PI Br. at 23. This statement ignores both the extensive record of fraud in the award of state investments compiled by the SEC, and the ubiquity of scandals in contracting at all levels of government—all of which occurred despite the existence of the federal base contribution limits that plaintiffs contend entirely eliminate any possibility of corruption in the selection of state investment advisors. *See* PI Br. at 21-22. Further, even if the evidence of play-to-play activities was less plentiful, the Supreme Court has allowed the enactment of prophylactic measures when quid pro quo corruption is "neither easily detected nor practical to criminalize." *McConnell v. FEC*, 540 U.S. 93, 153 (2003).

For all these reasons, plaintiffs' motion for preliminary injunction should be denied and their complaint dismissed.

ARGUMENT

I. Plaintiffs Lack Standing to Bring This Action.

Because the Rule neither regulates the plaintiffs' conduct, nor subjects plaintiffs to any potential sanctions or burdens, plaintiffs lack Article III standing to bring this action. Likewise, plaintiffs do not satisfy the test for associational standing to allow them to represent the interests of those who are directly affected by the Rule.

Article III of the Constitution limits federal courts to the resolution of actual cases and controversies. *Arizonans for Official English v. Arizona*, 520 U.S. 43, 64 (1997). At a minimum, this requires the parties seeking to invoke federal jurisdiction to have standing. *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 560 (1992) ("[S]tanding is an essential and unchanging part of the case-or-controversy requirement of Article III."). To have standing, plaintiffs "must present an injury that is concrete, particularized, and actual or imminent; fairly traceable to the defendant's challenged behavior; and likely to be redressed by a favorable ruling." *Davis v. FEC*, 554 U.S. 724, 733 (2008) (citing *Lujan*, 504 U.S. at 560-61).

Article III standing requires the existence of "an actual factual setting in which the litigant asserts a claim of injury in fact," which ensures that the court "may decide the case with some confidence that its decision will not pave the way for lawsuits which have some, but not all, of the facts of the case actually decided by the court." *Valley Forge Christian College v. Americans United for Separation of Church and State*, 454 U.S. 464, 472 (1982). This means that a "plaintiff generally must assert his own legal rights and interests, and cannot rest his claim to relief on the legal rights or interests of third parties." *Warth v. Seldin*, 422 U.S. 490, 499 (1975).

In limited circumstances, the courts have recognized that an association that has not suffered a direct injury itself may have standing to represent the interests of its members who have been directly injured. *Id.* at 511. But to assert representational standing, an association must show that "(a) its members would otherwise have standing to sue in their own right; (b) the interests it seeks to protect are germane to the organization's purpose; and (c) neither the claim asserted nor the relief requested requires the participation of individual members in the lawsuit." *Hunt v. Washington State Apple Adver. Comm'n*, 432 U.S. 333, 343 (1977), *superseded in part by statute*, Worker Adjustment and Retraining Notification Act (WARN Act), 102 Stat. 890, 29 U.S.C. § 2101 *et seq.*, *as recognized in United Food & Commer. Workers Union Local 751 v. Brown Grp.*, 517 U.S. 544, 546 (1996).

Plaintiffs' claim to standing appears to be derived from three sources. First, plaintiffs allege that the Rule directly harms their interests by shrinking the pool of available contributors, based on their representation that "potential donors have informed each plaintiff that they will not make political contributions because of the SEC's rule." Compl. ¶ 41. Second, plaintiffs claim standing as representatives of the interests of "members" who are investment advisor subject to the Rule that "plaintiffs believe . . . would contribute to plaintiffs but for the political contribution rule." *Id.* ¶ 42. Finally, plaintiffs assert standing on behalf of their "members who are current or future candidates for federal elective office whose ability to raise funds is restricted." *Id.* ¶ 43.

Each of these claimed bases for standing suffers from fatal and overlapping defects.

Plaintiffs' attempt to assert standing on their own behalf and on behalf of candidates must fail because the Rule imposes no burden, obligation or potential liability on political parties or candidates. The SEC's rule does not prevent plaintiffs or candidates, or their agents, from soliciting or accepting contributions from anyone, including the covered investment advisors. Rather, the Rule "prohibits an investment adviser from providing advisory services for compensation to a government client for two years after the adviser or certain of its executives or employees make a contribution to certain elected officials or candidates." 75 Fed. Reg. at 41,018. In fact, while a covered investment advisor cannot receive compensation for services provided to the government in certain circumstances if it makes a covered contribution, the making of the contribution itself is not illegal. In contrast, under the Federal Election Campaign Act ("FECA"), either making or soliciting a prohibited contribution or a contribution in excess of the statutory limits, and the knowing acceptance of such a contribution by a candidate or political party, is illegal and carries possible civil and criminal penalties. *See, e.g.*, 2 U.S.C. § 437g(d).

Thus, it is clear that the SEC's rule causes no direct injury to the plaintiffs or to candidates. Moreover, any indirect injury that they claim is speculative and depends on the assumption that these two particular political party committees and the candidates they claim to represent would receive political contributions but for the Rule. But no individuals or entities covered by the Rule, nor any individual candidates, have appeared in this case as parties. Plaintiffs offer only the bald assertion that they "believe that other contributors would contribute [to the parties and candidates] but for the Political Contribution Rule." Compl. ¶ 42. This assertion is backed by two virtually identical affidavits from the executive directors of the New York Republican State Committee and the Tennessee Republican Party, both of whom merely state that they "have encountered donors and potential donors . . . who have either limited their contributions or declined to contribute because of the political contribution rule." Weingartner Decl. ¶ 9; Leatherwood Decl. ¶ 9. A boilerplate allegation that unknown and unnamed individuals would contribute absent the Rule is hardly a sufficient basis upon which to litigate the constitutionality of the Rule and the interests of investment advisors subject to the Rule.

In reality, plaintiffs' theory of standing would recognize a constitutionally cognizable injury any time a regulation applicable to a third party might deter that person or entity from making a contribution to the plaintiffs or their candidates.[1] The breadth of plaintiffs' theory even allows them to assert standing to challenge the *record-keeping requirements* applicable to third parties because, allegedly, "the burden of these requirements effectively limits the willingness of investment advisors to make political contributions." Compl. ¶¶ 37-39. It is of apparently little import to plaintiffs that the targets of their fundraising efforts who are subject to the Rule may not in fact wish to make contributions to the plaintiffs, or may not believe themselves to be injured by the Rule.

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[1] This assumes, *arguendo*, that plaintiffs, as political party committees, have standing to assert the interests of their candidates. However, the Supreme Court, in holding that political parties have a constitutional right to make independent expenditures on behalf of candidates, rejected the assumption that the interests of a political party and its candidates are "identical, *i.e.*, the party, in a sense, is its candidates." *Colorado Republican Fed. Campaign Comm. v. FEC*, 518 U.S. 604, 622-23 (1996). Given the practical and political realities surrounding fundraising, the interests of the candidates and political parties may very well not align on this issue.

In addition to this theory, the two state political party plaintiffs also claim standing to represent the interests of their "members" from within their respective states, "many of whom are precluded from providing it with financial support due to the Political Contribution Rule." Compl. ¶¶ 11, 12; *see also* PI Br. at 7.

However, plaintiffs do not attempt to explain the basis upon which an individual can be imputed to be a "member" of the party in a manner analogous to a "member" of a trade association or other membership organization. Since plaintiffs wish to represent the interests of those who have *not* contributed to the party, it is incumbent upon them to do more than just reference the "potential donors" in their states who are among the "approximately 11,000 registered investment advisors nation-wide" who are covered by the Rule. Compl. ¶ 41. Presumably, each state party has its own rules and criteria governing who is considered a member, and presumably those rules define membership with more exactitude than simply 'anyone who might potentially contribute to the party.' If representational standing is to serve any of the interests protected by Article III, there must be some basis upon which the Court can be assured that a party claiming such standing will, in fact, represent the interests of those it purports to represent. It is for this reason that this court refused to find representational standing based on an organization's broad assertion of harm to "constituents" where the organization did not provide materials showing "any specific factual support that a particular member [of the organization] has suffered, or imminently will suffer, concrete harm." *Pharm. Research & Manufacturers of Am. v. Thompson*, 259 F. Supp. 2d 39, 52 (D.D.C. 2003), *aff'd sub nom. Pharm. Research & Mfrs. Am. v. Thompson*, 362 F.3d 817 (D.C. Cir. 2004).

Beyond failing to assert the basis upon which it is claiming a "membership" relationship with those it purports to represent, plaintiffs fail to meet the test for representational standing set forth in *Warth* and *Hunt*. Even assuming that covered investment advisors would have standing to challenge the Rule and that striking down the Rule is "germane" to the purposes of a political party, the nature of the Rule and the claims asserted here require the participation of those directly covered by the Rule.

Unlike the general contribution limits and prohibitions found in FECA, the SEC's Rule is aimed at the practices of individuals and firms involved in a business highly regulated by the SEC and involving complicated fiduciary relationships. As the SEC has explained:

> [I]nvestment advisers that seek to influence government officials' awards of advisory contracts by making or soliciting political contributions to those officials compromise their fiduciary duties to the pension plans they advise and defraud prospective clients. These practices, known as ''pay to play,'' distort the process by which advisers are selected. They can harm pension plans that may subsequently receive inferior advisory services and pay higher fees. Ultimately, these violations of trust can harm the millions of retirees that rely on the plan or the taxpayers of the State and municipal governments that must honor those obligations.

75 Fed. Reg. at 41,019 (Footnotes omitted)

Thus, it is very likely that the interests and perspective of the plaintiffs in obtaining political contributions from any source possible is not the same as the interests of individuals and firms regulated by the SEC's Rule. At the very least, the Court should not decide what interests are at stake without the participation of those directly affected by the Rule.

The nature of the Rule at issue and plaintiffs' claim of injury also distinguishes this case from *Wisconsin Right to Life State PAC (WRTL-PAC) v. Barland*, 664 F.3d 139 (7th Cir. 2011). *See* Compl. ¶ 42. In *Barland*, the Seventh Circuit found that WRTL-PAC had standing to represent the interests of its contributors and challenge the state aggregate limit on individual contributions to political candidates, parties and political committees on grounds that the law effectively limited the contributions that the PAC could receive. *Id*. at 147-48. However, at issue was a limitation that applied to *all* contributors, not just to a unique subset of contributors who may have legal and fiduciary interests not shared with the political party plaintiffs. Further, the court in *Barland* explicitly relied upon the declarations filed by two contributors stating that they would make contributions to the PAC in excess of the aggregate contribution limits if those contributions were legal. *Id*. Finally, *Barland* noted that the statute being challenged subjected contributors to potential civil and criminal liability for violating the contribution limits.[2] *Id*. at 148 n.8.

Here, by contrast, the challenged Rule targets a unique and highly regulated industry, plaintiffs have provided no statement from any covered investment advisor who wishes to make a prohibited contribution, and the Rule does not involve civil or criminal enforcement. To read *Barland* as authorizing standing for any political committee that wishes to challenge any law that theoretically could influence a potential donor's decision to contribute would eviscerate the concept of Article III standing.

Plaintiffs have provided no theory that would support their standing to bring this case, and their complaint accordingly should be dismissed.

[2] In its discussion of standing, *Barland* cites *EMILY's List v. FEC*, 581 F.3d 1 (D.C.Cir.2009), for the proposition that contribution limits can injure the recipient PAC. 664 F.3d at 147-48. However, as the court notes, the challenge in *EMILY's List* involved restrictions on the PAC receiving contributions. No such restrictions on the party plaintiffs exist in the instant case. Moreover, the other cases cited in *Barland* as supporting "standing to sue to vindicate the political-speech rights of its contributors" all involved plaintiffs who either had independently established standing based on the direct application of the law to their activities, or involved restrictions on third parties that directly and concretely threatened the ability of a business to survive. *Id*. at 148.

II. The Political Contribution Rule Is Consistent with the First Amendment.

A. The Court of Appeals Rejected a Constitutional Challenge to a Materially Similar Rule in *Blount v. FEC*.

In *Blount*, the D.C. Circuit Court of Appeals rejected a First Amendment challenge to MSRB Rule G-37, a rule that in almost all respects is identical to the Rule challenged here, concluding that it served multiple "compelling" governmental interests. 61 F.3d at 944-49.

Rule G-37 prohibits municipal securities professionals who have made more than *de minimus* contributions to the campaigns of officials of a municipal securities "issuer" from obtaining business from that "issuer" for two years after the contribution. Mun. Sec. Rulemaking Bd. Rule G-37(b). Municipal securities professionals are also barred soliciting or coordinating contributions for officials of any issuer with whom they are "engaging or . . . seeking to engage in municipal securities business" or for the political parties of the state of the issuer. Rule G-37(c).

In reviewing Rule G-37, the Court declined to decide the applicable level of scrutiny because it found that the Rule G-37 could survive strict scrutiny and thus "there [was] no need to decide the issue."[3] The agency asserted that Rule G-37 served at least two state interests: "prevent[ing] fraudulent and manipulative acts and practices, as well as the appearance of fraud and manipulation," and "perfect[ing] the mechanism of a free and open market for municipal securities in order to "promote just and equitable principles of trade." 61 F.3d at 942 (quoting SEC Release No. 34-33868 at 26, 29 (Apr. 7, 1994) (order approving proposed rule change)). Applying strict scrutiny, the Court found that both of these interests were compelling and that the

[3] The Supreme Court has since made clear that laws regulating political contributions—even complete bans on contributions—are subject only to "closely drawn" scrutiny. *McConnell*, 540 U.S. at 136; *FEC v. Beaumont*, 539 U.S. 146, 162 (2003).

Rule was narrowly tailored to serve these interests. In so holding, it noted the pay-to-play activities that Rule G-37 would prevent:

> [U]underwriters' campaign contributions self-evidently create a conflict of interest in state and local officials who have power over municipal securities contracts and a risk that they will award the contracts on the basis of benefit to their campaign chests rather than to the governmental entity. Petitioner himself remarked on national radio that "most likely [state and local officials] are gonna call somebody who has been a political contributor" and, at least in close cases, award contracts to "friends" who have contributed.

Id. at 944-45.

This analysis applies with equal force to the Rule challenged here. Its structure is identical to Rule G-37; the only material difference is that it regulates the grant of state investments, instead of the municipal securities business. And the SEC invoked the same governmental interests in its consideration and adoption of the challenged Rule as it did in connection to Rule G-37 in the *Blount* litigation.

In an attempt to blunt the precedential weight of *Blount*, plaintiffs argue that it "relied on First Amendment jurisprudence that is now significantly outdated," citing four Supreme Court cases for this claim—*WRTL*, *Citizens United*, *Davis* and *McCutcheon*. PI Br. at 25. But none of these cases addresses laws regulating contributions from government contractors, and indeed, the first two cases do not concern contributions at all. Thus, even insofar as the challenged Rule is understood to indirectly impact political contributions, the cited cases have no bearing on this Court's review of plaintiffs' First Amendment claims.

It is black-letter law that expenditure restrictions and contribution restrictions implicate different First Amendment interests, are subject to different standards of scrutiny and are supported by different governmental interests. *See, e.g.*, *FEC v. Beaumont*, 539 U.S. 146, 161 (2003); *McConnell*, 540 U.S. at 134-40. Expenditure restrictions are deemed the most onerous campaign finance regulations and are consequently subject to strict scrutiny and must be narrowly tailored to satisfy a "compelling" governmental interest. *WRTL*, 541 U.S. at 464; *see also Buckley*, 424 U.S. at 44-45. Contribution limits, by contrast, are deemed less burdensome of speech, and are constitutionally "valid" if they "satisf[y] the lesser demand of being closely drawn to match a sufficiently important interest." *McConnell*, 540 U.S. at 136 (quoting *Beaumont*, 539 U.S. at 162) (internal quotation marks omitted).

Both *WRTL* and *Citizens United* reviewed the federal ban on independent expenditures by corporations in federal elections. *See* 2 U.S.C. § 441b. Given the longstanding distinction the Supreme Court has drawn between expenditures and contributions for the purposes of constitutional review, the analysis of an *expenditure* restriction in *WRTL* and *Citizens United* has no bearing on a law regulating *contributions*. Indeed, the Supreme Court explicitly noted in *Citizens United* that it was not altering its approach to reviewing contribution restrictions. 558 U.S. at 359 ("Citizens United has not made direct contributions to candidates, and it is not suggested that the Court should reconsider whether contribution limits should be subjected to rigorous First Amendment scrutiny.").

Davis also is not relevant to the analysis of the Rule. There, the Supreme Court reviewed the "Millionaire's Amendment," a federal provision that tripled the contribution limit for any congressional candidate who faced an opponent who spent over $350,000 of his personal funds to support his campaign. *See* 554 U.S. at 739; Bipartisan Campaign Reform Act ("BCRA") § 319(a). However, the problem with the Millionaire's Amendment was not that it placed limits on contributions, but that it did so in an "asymmetric" manner that "impose[d] a substantial burden on the exercise of the First Amendment right to use personal funds for campaign speech." 554 U.S. at 740; *see also id.* at 737 (noting that "if § 319(a)'s elevated contribution limits applied *across the board*," then there would be no "basis for challenging those limits") (emphasis added). *Davis* is thus properly understood as a challenge to restrictions on personal expenditures, not an attack on contribution limits; accordingly, the law was subject to strict scrutiny, not the "closely drawn" scrutiny applied to contribution limits. *Id*. at 739. The Court's analysis therefore has no relevance to the review of the Rule. Furthermore, unlike the Rule here, the Millionaire's Amendment was not designed to prevent quid pro quo corruption or fraud, but rather to "level electoral opportunities for candidates of different personal wealth." *Id.* at 741 (internal quotation marks omitted). Indeed, as the Court reasoned, "reliance on personal funds reduces the threat of corruption, and therefore § 319(a), by discouraging use of personal funds, *disserves* the anticorruption interest." *Id*. at 740-41 (emphasis added).

Lastly, *McCutcheon* also does not cast doubt on the analysis in *Blount* because it neither altered the standard of review applied to contribution limits, nor questioned the governmental interests that such limits serve. 134 S. Ct. at 1445.

McCutcheon considered a very particular type of limit—the federal aggregate limits on total contributions that an individual can make to candidates, parties and PACs. 2 U.S.C. § 441a(a)(3) (2013). The aggregate limits had been justified as a means to prevent donors from circumventing the base limits on contributions to candidates by making "unearmarked contributions to political committees likely to contribute to [their preferred] candidate, or huge contributions to the candidate's political party." *Buckley*, 424 U.S. at 38. Thus, unlike the Rule at issue here, the aggregate limits had never been conceived as a method to directly prevent quid pro quo exchanges, but rather as an anti-circumvention measure to ensure that the base limits were not evaded. The plurality decision in *McCutcheon* invalidated the challenged aggregate limits because it believed numerous other provisions of federal law—such as limits on contributions to parties and PACs, as well as affiliation rules—made circumvention of the base limits even in the absence of the aggregate limits "highly implausible." *Id.* at 1453.

The *McCutcheon* plurality, however, specifically and repeatedly disavowed that it was altering the "closely drawn" standard of scrutiny traditionally applicable to contribution limits. *Id.* at 1451 & n.6; *see also id.* at 1445 ("[W]e see no need in this case to revisit *Buckley*'s distinction between contributions and expenditures and the corollary distinction in the applicable standards of review."). Further, the plurality's concern with the governmental interests offered for the aggregate limits analysis focused on the "improbability of circumvention" absent the aggregate limits. *Id.* at 1446, 1456. It did not question the fundamental importance of the interest in preventing corruption or fraud, as the plaintiffs do here. To be sure, the plurality emphasized that the government's anti-corruption interest was confined to the prevention of quid pro quo corruption and the appearance of such corruption, but it was the opinion of the plurality that this principle had governed the Supreme Court's campaign finance jurisprudence since the 1976 *Buckley* decision. *Id.* at 1450 (quoting *Citizens United*, 558 U.S. at 359) ("When *Buckley* identified a sufficiently important governmental interest in preventing corruption or the appearance of corruption, that interest was limited to quid pro quo corruption."). The *McCutcheon* plurality thus did not change the Supreme Court's approach to the review of contribution limits; it simply found that the circumvention schemes feared by the government in the absence of the aggregate limits—schemes requiring the cooperation of 50 or more party committees—were implausible. *Id*. at 1454 (finding it "hard to believe that a rational actor would engage in such machinations" just to evade the limits on individual contributions).

In short, *Blount* governs the consideration of plaintiffs' First Amendment claims here, and no case since its issuance has undercut its reasoning or altered the Supreme Court's longstanding approach to the review of laws impacting political contributions.

B. Pay-to-Play Laws, such as the Political Contribution Rule, Are Widely Recognized as Advancing Important Governmental Interests.

Plaintiffs maintain that the Supreme Court has made clear that a legislature or agency may justify the regulation of political contributions based on only one interest—the prevention of "quid pro quo corruption"—but suggests that this was not an objective of the SEC in adopting the challenged Rule. This position is willfully blind.

The SEC articulated the interests served by the Rule as the "prevent[ion of] direct quid pro quo arrangements, fraudulent and manipulative acts and practices"; and the "improve[ment] of the mechanism of a free and open market for investment advisory services for government entity clients." 75 Fed. Reg. at 41,024 n.79. The SEC further explained that "pay to play" arrangements in the grant of state investments "are inconsistent with an adviser's fiduciary obligations, distort the process by which investment advisers are selected, can harm advisers' public pension plan clients and the beneficiaries of those plans, and can have detrimental effects on the market for investment advisory services." *Id*. at 41,023.

Although the SEC thus perceives the Rule as preventing a broad range of harms, all of these harms arise from the pay-to-play quid pro quo exchanges the Rule was intended to bar. For instance, the SEC further states that the Rule is "a focused effort to combat quid pro quo payments by investment advisers seeking governmental business." *Id*. at 41,023 n.68; *see also id.* at 41,023 (noting that "payments to State officials as a quid pro quo for obtaining advisory business as well as other forms of 'pay to play'" are a form of fraud targeted by the Rule); *id*. at 41,024 ("The rule is targeted at those employees of an adviser whose contributions raise the greatest danger of quid pro quo exchanges.”). It is hard to imagine how the SEC could have expressed an interest in preventing quid pro quos any more clearly.

The rationales articulated by the SEC for the Rule were found to be sufficiently important by the *Blount* Court in its review of Rule G-37. There, the SEC asserted that G-37 both “protect[ed] investors in municipal bonds from fraud” and “protect[ed] underwriters of municipal bonds from unfair, corrupt market practices.” 61 F.3d at 944. The Court affirmed that both interests were “compelling.” *Id.*; *see also FEC v. Weinstein*, 462 F. Supp. 243, 248 (D.C.N.Y. 1978) (approving federal contractor contribution ban and noting that “the importance of the governmental interest” in preventing corruption “through the creation of political debts” had “never been doubted”).

Plaintiffs also suggest that “address[ing] practices that undermine the integrity of the *market for advisory services*” is not as compelling an interest as preventing quid pro quo corruption in politics. *See* PI Br. at 21 (alteration in original) (emphasis added) (quoting 75 Fed. Reg. at 41,053). But the D.C. Circuit confronted this precise argument in *Blount*, and rejected it. Petitioners in *Blount* had argued that in campaign finance cases, “the legislature was interested in clean elections,” whereas the SEC “is interested in clean bond markets,” and that “the latter interest is less compelling than the former.” 61 F.3d at 944. The Court rejected this attempt to differentiate between types of “corruption,” finding that “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.” *Id*. In short, preventing quid pro quos in the award of state investments is as compelling as preventing corruption in elections generally or in other decisions made by elected officials.

Tacitly acknowledging that the Rule was indeed intended to combat a form of quid pro quo corruption, plaintiffs argue that Congress has already enacted a restriction on political contributions from federal contractors and that many states have their own pay-to-play restrictions, making the SEC Rule redundant. But this position requires plaintiffs to turn a blind eye to the fact that the federal contractor contribution ban found in FECA, 2 U.S.C. § 441c, prohibits *federal* contractors from making any contributions to federal candidates, political parties and PACs, and does not purport to address contracts with *state* or *local* governments. Plaintiffs also ignore the fact that state laws aimed at preventing pay-to-play practices vary widely. There is no evidence that Congress believed FECA's contribution ban applicable to federal contractors precluded the SEC from enacting uniform pay-to-play rules aimed at preventing quid pro quo arrangements in state contracting involving investment advisors under its jurisdiction.

The federal contractor contribution restriction would not prevent the abuses feared by the SEC in the award of state investment contracts. Absent the SEC Rule, a state investment advisor—or PACs controlled by the advisor—would still be permitted to curry favor with potential state customers by making individual or PAC contributions. Likewise, the application of the base contribution limits in FECA would do little to avert this abuse because absent the Rule, an advisor still could make "limited" contributions to state officials running for federal office and steer a huge number of additional "limited" contributions to such officials through its associates or PACs. Finally, neither the base limits nor Section 441c—even if applicable—forbids investment advisors and their associates from soliciting or "bundling" contributions for a campaign, leaving open a clear channel for the exchange of quid pro quos. In short, even a cursory comparison of the Rule and existing federal law confirms they are not duplicative.

C. A Prophylactic Rule Is Not Only Permissible, But Is Often Deemed Necessary to Prevent Pay-to-Play Activities.

1. There Is Ample Evidence of Quid Pro Quo Corruption in the Selection of Investment Advisors and Government Contracting in General.

In addition to questioning the importance of the SEC's anti-fraud objectives, plaintiffs also suggest that the SEC has offered no evidence of quid pro quos in the selection of investment advisors or public pension fund managers. PI Br. at 12 (citing 75 Fed. Reg. at 41,090) ("The SEC admits it cannot say that quid pro quo arrangements between elected officials and investment advisers are widespread."). Again plaintiffs' position requires willful blindness.

Even a quick perusal of the record establishes that the SEC amassed extensive evidence of fraud in the award of state investment contracts. It detailed its concerns about the prevalence of schemes in which investment advisors funneled contributions through third-party "placement agents" in order to secure business with public pension plans. 75 Fed. Reg. at 41,019. It listed multiple actions brought by the SEC and State authorities to prosecute quid pro quo deals to influence the award of contracts in connection to the New York State Common Retirement Fund. Indeed, one of the officials ensnared in these investigations, former New York State Comptroller Alan Hevesi, admitted he steered *$250 million* of state business to an investment firm in exchange for gifts and more than $500,000 in contributions.[4] The SEC also referenced its enforcement action against the former treasurer of the State of Connecticut for awarding State investments to private equity fund managers in exchange for payments, including political contributions, and discussed similar cases that had been prosecuted by state authorities in New

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[4] *See* Office of New York Attorney General Eric T. Schneiderman, *Former Comptroller Alan Hevesi Sentenced To Up To Four Years In Prison For Role In Pay-To-Play Pension Fund Kickback Scheme* (Apr. 15, 2011), http://www.ag.ny.gov/press-release/former-comptroller-alan-hevesi-sentenced-four-years-prison-role-pay-play-pension-fund.

York, New Mexico, Illinois, Ohio, Connecticut and Florida. 75 Fed. Reg. at 41,020; *see also id* at 41,020 nn.19-25.

Furthermore, corrupt practices are hardly limited to the grant of government investments. Pay-to-play activities are endemic in many areas of government contracting, as evidenced by numerous pay-to-play laws at the federal, state and municipal levels. At least seventeen states have enacted limits or prohibitions on campaign contributions from prospective and/or current government contractors or licensees.[5] A number of municipalities, including New York City and Los Angeles, have followed suit.[6]

The pervasiveness of pay-to-play practices in contracting has also been frequently recognized by the courts, which have generally approved of state regulation of contributions and other political activities by prospective and current state contractors. *See, e.g.*, *Green Party of Connecticut v. Garfield*, 616 F.3d 189 (2d Cir. 2010) (upholding Connecticut law banning contributions from state contractors, "principals" of contractor and their immediate family members); *Ognibene v. Parkes*, 671 F.3d 174 (2d Cir. 2011) (upholding New York City provision imposing additional limitations on campaign contributions by entities "doing business" with the City); *Yamada v. Weaver*, 872 F. Supp. 2d 1023 (D. Haw. 2012), *appeal docketed*, No.

[5] Cal. Gov't Code § 84308(d); Conn. Gen. Stat. § 9-612(f)(1)-(2); Haw. Rev. Stat. § 11-355; 30 Ill. Comp. Stat. 500/50-37; Ind. Code §§ 4-30-3-19.5 to -19.7; Ky. Rev. Stat. Ann. § 121.330; La. Rev. Stat. Ann. §§ 18:1505.2(L), 27:261(D); Mich. Comp. Laws § 432.207b; Neb. Rev. Stat. §§ 9-803, 49-1476.01; N.J. Stat. Ann. § 19:44A-20.13 to -20.14; N.M. Stat. Ann. § 13-1-191.1(E)-(F); Ohio Rev. Code § 3517.13(I) to (Z); 53 Pa. Cons. Stat. § 895.704-A(a); S.C. Code Ann. § 8-13-1342; Vt. Stat. Ann. tit. 32, § 109(B); Va. Code Ann. § 2.2-3104.01 (amended by Va. Acts 2013, Ch. 583 (eff. July 1, 2014)); W. Va. Code § 3-8-12(d).

[6] N.Y.C. Admin. Code §§ 3-702(18), 3-703(1-a) to (1-b); L.A., Cal., City Charter § 470(c)(12).

12-15913 (9th Cir. Apr. 20, 2012) (upholding Hawaii law prohibiting all contractors from making contributions to candidate and non-candidate committees).[7]

The courts have also highlighted that many state and municipal laws were passed in direct response to scandals involving quid pro quo exchanges of campaign contributions for state contracts. For instance, in upholding Connecticut's sweeping governmental contractor contribution ban, the Second Circuit noted that the law was passed after numerous pay-to-play corruption scandals in Connecticut, one involving the former governor, John Rowland, who accepted over $100,000 worth of gifts and services from state contractors in exchange for the grant of lucrative state contracts. *Green Party*, 616 F.3d at 193 (citing *Green Party of Conn. v. Garfield*, 648 F.Supp.2d 298, 306-08 (D. Conn. 2009)); *see also Ognibene*, 671 F.3d at 179 (noting the series of pay-to-play scandals in New York City preceding enactment of the contractor contribution restriction); *Yamada*, 872 F. Supp. 2d at 1049 n.27 (recounting corruption scandals that preceded law).

Plaintiffs ignore the record compiled by the SEC and are apparently unaware of the extensive evidence of pay-to-play activity at both the federal and state level. But even if the evidence were less overwhelming, the D.C. Circuit has already found that given the clear conflict of interest inherent in the political activities of financial professionals seeking state business, an

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[7] State courts have likewise sustained strict contractor contribution limits. *See In Re Earle Asphalt Co.*, 950 A.2d 918, 325 (N.J. Super. App. Div. 2008) ("In sum, the State's interest in insulating the negotiation and award of State contracts from political contributions that pose the risk of improper influence, . . . or the appearance thereof, is a sufficiently important interest to justify a [$300] limitation upon political contributions.") (internal citations and quotation marks omitted), *aff'd*, 966 A.2d 460 (N.J. 2009) (per curiam). Relatedly, state courts have also upheld a range of contribution restrictions applicable to certain highly regulated industries deemed to pose a heightened threat of political corruption. *See, e.g.*, *Casino Ass'n of La. v. State ex rel. Foster*, 820 So.2d 494 (La. 2002) (upholding state law prohibiting any political contributions from officers, directors, and certain employees in the casino industry, and their spouses); *Soto v. New Jersey*, 565 A.2d 1088 (N.J. 1989) (upholding prohibition on casino-industry contributions); *Schiller Park Colonial Inn, Inc. v. Berz*, 349 N.E.2d 61 (Ill. 1976) (upholding law prohibiting political contributions from any officer, associate, agent, representative, or employee of a liquor licensee).

extensive record is not necessary to support a pay-to-play restriction. In *Blount*, the plaintiff claimed that the SEC had failed to provide any evidence of specific instances of quid pro quos in the negotiated municipal bond business. The D.C. Circuit rejected this attack, noting that "[a]lthough the record contains only allegations, no smoking gun is needed where, as here, the conflict of interest is apparent, the likelihood of stealth great, and the legislative purpose prophylactic." 61 F.3d at 945.

2. The First Amendment Does Not Bar Prophylactic Rules.

As demonstrated by the record for the Rule and recent experience in states and municipalities, evidence of play-to-play corruption in contracting is still plentiful and concerns about pay-to-play corruption are widespread. But even if quid pro quos were to occur only occasionally in contracting, the Supreme Court has allowed legislatures to take a prophylactic approach when such exchanges are "neither easily detected nor practical to criminalize." *McConnell*, 540 U.S. at 153 (noting that "[t]he best means of prevention is to identify and to remove the temptation"). As the Supreme Court stated in *Shrink Missouri*, "[t]he quantum of empirical evidence needed to satisfy heightened judicial scrutiny of legislative judgments will vary up or down with the novelty and plausibility of the justification raised." 528 U.S. at 391. In light of the record compiled by the SEC here, and the enactment of pay-to-play statutes in at least 20 states and municipalities, the suggestion that those seeking state contracts might "pay to play" is hardly novel or implausible. Therefore, even if the evidence of quid pro quo exchanges were less abundant than it is here, a prophylactic approach would still be permissible.

Lastly, at least as important as the need to prevent instances of actual fraud in contracting is the need to avoid the appearance of fraud. *See Buckley*, 424 U.S. at 27 ("Congress could legitimately conclude that the avoidance of the appearance of improper influence 'is also critical . . . if confidence in the system of representative Government is not to be eroded to a disastrous extent.'") (citation omitted). Recognizing the importance of this interest, the Second Circuit observed in upholding New York City's "doing business" law that recurrent pay-to-play scandals had "created a climate of distrust that feeds the already-established public perception of corruption." *Ognibene*, 671 F.3d at 191 n.15. It was therefore "not necessary to produce evidence of actual corruption to demonstrate the sufficiently important interest in preventing the *appearance of corruption*." *Id.* at 183 (emphasis added). Similarly, as the Second Circuit emphasized in *Green Party*, "widespread media coverage of Connecticut's recent corruption scandals" created a "manifest need to curtail the *appearance of corruption* created by contractor contributions." 616 F.3d at 200 (emphasis added). Thus, as multiple courts have found, limiting contractor contributions is a key measure to combat the public perception that public business is for sale to private interests.

Although plaintiffs insinuate that *McCutcheon* cast doubt on the constitutionality of prophylactic laws, they fail to mention that the plurality there explicitly acknowledged that Congress could pass laws not only to directly combat actual quid pro quo corruption, but also to limit "the appearance of quid pro quo corruption." 134 S. Ct. at 1451. As the Court of Appeals found in *Blount*, "campaign contributions self-evidently create a conflict of interest in state and local officials." 61 F.3d at 944. The SEC is statutorily authorized to adopt prophylactic measures that combat not only actual quid pro quos in the grant of state investments, but also the appearance of quid pro quo corruption created by unchecked contributions by state investment advisors.

CONCLUSION

For the foregoing reasons, this Court should deny plaintiffs' motion for preliminary injunction and dismiss their complaint.

RESPECTFULLY SUBMITTED this 29th day of August 2014.

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