COMPLIANCE WEEK

'Political Risk' Can PAC A Compliance Punch

By Paul J. Martinek — May 31, 2006

Politics can be an expensive game. And anyone who wants to know the cost of sloppy politics might want to check with the Federal Home Mortgage Loan Corp.

Freddie Mac, as the company is commonly known, agreed in April to pay a $3.8 million fine to the Federal Election Commission—the largest penalty in FEC history. The fine settled allegations that Freddie Mac used corporate staff and resources to solicit contributions from employees which were passed on to federal candidates, in violation of the Federal Elections Campaign Act and FEC regulations. It also served as a costly reminder to Corporate America about the perils of not complying with the myriad of federal, state and local elections laws.

Freddie Mac isn't the only company to be accused of running afoul of election laws. In 2002 the FEC fined toy-making titan Mattel $477,000 for improper contributions made by one of Mattel's executives and by a former consultant. In 2003 the Commission reached settlements with Audiovox Corp. and several of its executives and distributors for penalties totaling $849,000, for reimbursing individual contributions to federal candidates.

And last summer Westar Energy Inc., two of its former executives and a lobbyist agreed to pay fines totaling $40,500 to settle accusations that it used corporate resources to support members of Congress, including then-House Majority Leader Tom DeLay. Westar was so stung by the experience that after agreeing to the fine it vowed to get out of politicking altogether (see FEC Enforcement Actions in box at right).

According to James Jonas, a partner with the law firm Holland & Knight, relatively few companies do a good job monitoring political activities. "There are only a handful of the most politically active companies that have robust compliance programs—generally those companies that have continued to be major corporate sponsors of political activity," he says.

RELATED RESOURCES

Text Of U.S. Campaign Finance Law (October 2005)

Summary Of FEC Regulations On Campaign Finance

FEC Enforcement Actions

FEC Statement On Freddie Mac Case (April 18, 2006)

FEC Statement On Audiovox Case (October 2003)

FEC Statement On Mattel Case (Dec. 5, 2002)

FEC Statement On Westar Energy Case (May 12, 2005)

Related Coverage

Activists Want Contributions To Be A Disclosure Item (Sept. 14, 2004)


Laufer

While corporate political activities may garner more attention during a federal election year, "every year is an election year when you're looking at it from the state and local perspective," says Laurence Laufer, a partner with Genova, Burns & Vernoia. "Every state and some localities have their own enforcement agencies. A lot of problems arise at the state and local level, though there may be less awareness of the range of requirements out there. And, occasionally, somebody gets nipped by it."

Jonas says that companies that aren't major sponsors of political activity are kidding themselves if they think they don't need to be concerned. "Any entity with humans is going to have political activity," he says. "Many companies think they aren't engaged in political activities when they are … The biggest problems arise when companies pretend they are not being politically active. As long as an organization is not ignoring the fact that it is political in some sense of the word, all that activity can be purposeful and there can be compliance."

FREDDIE MAC SETTLEMENT

Below is an excerpt from the Federal Election Commission's settlement with Freddie Mac, detailing specific violations:

Between 2000 and 2003, Freddie Mac used corporate resources to facilitate 85 fundraising events that raised approximately $1.7 million for federal candidates. Freddie Mac documents, prepared by former Senior Vice President of Government Relations R. Mitchell Delk and others and directed to Freddie Mac's Board of Directors and CEO, described the fundraisers as "Political Risk Management" undertaken because Freddie Mac differed from most major corporations which have "a well-funded PAC to buttress their lobbying activities." The fundraisers were organized by Mr. Delk and former Vice-President Clark Camper, and benefited members of the House Financial Services Committee and other members of Congress. Consulting firms were hired to plan and organize the fundraising dinners, many of which were held at the Galileo Restaurant in Washington. Freddie Mac paid monthly retainers to those firms that grew to more than $25,000 per month by the end of 2002.

In addition to conducting fundraising events, Freddie Mac executives used corporate staff and resources to solicit and forward contributions from company employees to federal candidates. The FEC also found that Freddie Mac contributed $150,000 in 2002 to the Republican Governors Association ("RGA"), a contribution the RGA later returned.

As a federally chartered corporation, Freddie Mac is prohibited from making contributions in connection with any election to political office and Commission regulations prohibit a corporation (including its officers, directors or agents) from facilitating or acting as a conduit for contributions. 2 U.S.C. 441b(a) and 11 CFR 114.2(f). A corporation illegally facilitates the making of contributions when it uses corporate resources or personnel to plan and carry out fundraisers for federal candidates.

Source

Federal Home Loan Mortgage Corporation Pays Largest Fine In FEC History (Federal Elections Commission, April 18, 2006)

Jan Baran, a partner with the law firm of Wiley, Rein & Fielding, notes that negative publicity associated with campaign activities—even ones never proven unlawful—can hurt the corporation.


Baran

"Any time there is an allegation of illegal activity, whether proven or not, it's always harmful to both the politician and the business in the court of public opinion," Baran says. "Reputations suffer and, when it comes to the company, allegations of improper or illegal activity will make them—at least temporarily—a pariah among government officials. It's hard to interface with the government if you've been accused of illegal activities."

And as the scandal surrounding disgraced lobbyist Jack Abramoff indicates, criminal prosecution is also a possibility. "The lesson of Abramoff is that companies have to do due diligence on who they are hiring," says William Minor, a partner with the DLA Piper Rudnick Gray Cary law firm.

PACs As Compliance Tools

Successful compliance with election laws and regulations, says Laufer at Genova, Burns & Vernoia, hinges on companies having internal controls in place to track donations, interactions with elected officials, and other related activity. "Is there a political action committee? Is there a policy that deals with political activities of employees? Are there procedures in place? Who's responsible? Do they have an understanding of the laws?" he says.


Minor

To provide protection, companies can turn to creating political action committees that do all their political giving, Minor says. He also encourages a comprehensive, company-wide policy about political activities. Companies "need to think about why they're active in political activity in the first place," he says. "Any contribution should be made for the good of the company and for the shareholder."

At Morgan Stanley, for example, the board of directors adopted a policy explaining when and how the financial services company makes political contributions (see box below, right). "Individuals engaging in political campaign activities are expected to do so as private citizens and not as representatives of Morgan Stanley," the policy states. Employees cannot represent themselves as acting or speaking on behalf of the company without permission from its government relations department. Morgan Stanley also operates its own PAC, funded through voluntary employee contributions.

Other companies such Brinker International—the parent of restaurant chains like Chili's Grill & Bar and Romano's Macaroni Grill—do not have a separate policy on political activity, but fold a statement about political giving and lobbying into their more general code of conduct. Brinker's code states that directors, officers and employees "are prohibited from using corporate facilities or other assets of the company for the benefit of political candidates or parties. Any personal political contributions will not be reimbursed." Brinker also makes political contributions through a PAC.

Jonas says that "being politically active is probably the best protection to assure compliance" with election laws, since politically active companies often have robust education and compliance programs to prevent trouble.

Jonas

The traits of a robust compliance program, he says, include "having somebody within the organization who has a primary responsibility for political activity or compliance, and an engaged legal department. The next thing you need is to have external counsel that makes it part of their business to be an expert in the compliance arena."

One pitfall is when a company thinks that "one of these three will do it for them," Jonas says. "They say, 'I've hired great external counsel. They're going to handle this. I need not worry.' That's a mistake. You need all three: in-house expertise, an engaged legal department and good outside counsel."

Some companies specify oversight of political contributions in their governance and committee charters. Wyeth's board of directors, for example, has a Corporate Issues Committee that is responsible for reviewing certain policies and monitoring compliance "in significant areas of legal, social, and public responsibility" including—among other things—political contributions and political action.

EXCERPT

Below is Morgan Stanley's policy on political contributions and activities employees may engage in.

The Firm believes that the integrity of the United States municipal securities marketplace is dependent on all market participants maintaining the highest standards of ethical business conduct. Accordingly, the Firm's Political Contributions Policy prohibits political contributions to state or local officials or candidates in the United States that are intended to influence the awarding of municipal finance business to the Firm or the retention of that business. The applicable restrictions depend on your title, position, and responsibilities. It is important that employees and officers review the Political Contributions Policy and the procedures that apply to their business unit or consult with Compliance prior to engaging in any political activity in the United States. Among other things, violations of the Policy can have serious consequences for the Firm's ability to do business in certain jurisdictions in the United States.

Source

Morgan Stanley Code Of Ethics And Business Conduct

The Governance Committee at Xerox has numerous similar responsibilities, including "review significant shareholder relations issues, corporate political contributions and the Company's charitable contributions." The Nominating and Governance Committee at The Williams Companies has similar responsibilities, including annual review of charitable and political contributions.

Baran at Wiley, Rein & Fielding, sees three challenges of compliance against political risk. First, employees need training on what regulations exist around political activity and donations. Second, an ongoing internal enforcement and compliance process must exist, and be effective enough to monitor individual compliance. And third, he says, "There has to be a culture of compliance: an attitude in the company that not only are the laws there, but we are going to make sure we comply with them above and beyond the call of duty. Companies that take that approach will not have problems."

Related resources, cases and coverage can be found in the box above, right.