Prepared Written Testimony of

D. Mark Renaud

Partner

Wiley Rein LLP

"Politicizing Procurement: Will President Obama's Proposal Curb Free Speech and Hurt Small Business?"

Hearing Before the House Committee on Small Business and the House Committee on Oversight and Government Reform

Thursday, May 12, 2011 at 1:30 pm

Rayburn House Office Building, Room 2154

Chairmen and Ranking Members:

I appreciate the opportunity to submit comments in this hearing on the President's Draft Executive Order ("draft EO"), dated April 13, 2011 (and attached hereto at Appendix A), requiring government contractors and certain of their affiliates to disclose political and lobbying activity. My name is D. Mark Renaud, and I am a partner in the Election Law and Government Ethics group at Wiley Rein LLP. Our group is one of the oldest and largest such practices in the nation, and I personally have devoted over ten years to counseling private citizens, business entities, trade associations, and others on the nation's political laws, with a particular focus on federal, state, and local "pay-to-play" laws. At the outset, it is important to note that the views expressed herein are solely my own and do not reflect the views of my Firm or any of its clients.

As the President considers whether to issue the draft EO, I believe it is important for Congress, and especially these two committees, to understand the implications of the President's proposal and to appreciate the significant burdens that it would place on core First Amendment activity. As drafted, the President's proposal does little to further the draft EO's stated goals of transparency, efficiency, and integrity. If anything, the President's proposal actually creates several new problems where none existed before, and it does so without any empirical justification for the additional burdens it imposes. In many cases, these burdens will fall particularly hard on small businesses, who must use their limited resources to collect, sort, and then disclose information unrelated to the contracting process. In short, there simply is no nexus between the political information sought and the nation's contracts, no corruption to be remedied, and no need for the draft EO.

My testimony below explains these conclusions in greater detail.

A. Overview of the Draft EO and the Pay-to-Play and Campaign Finance Context in Which It Would Be Issued

1. How Does the President's Proposal Work?

In its current form, the draft EO essentially requires all persons, regardless of size, that submit offers in connection with federal contracts to disclose two types of information for the two years immediately preceding the submission of the bid:

- All contributions or expenditures to or on behalf of federal candidates, parties or party committees made by the bidding entity, its directors or officers, or any affiliates or subsidiaries within its control; and
- Any contributions made to third party entities with the intention or reasonable expectation that parties would use those contributions to make independent expenditures or electioneering communications.

The draft EO carves out an exception to this disclosure requirement when the aggregate "contributions and expenditures [do not exceed] $5,000 to a given recipient during a given year."

The plain language of the draft EO does not appear to require the disclosure of the political activities of directors and officers beyond those of the bidding entity. Nevertheless, since, the terms "affiliates," "officers," "control," and "third party entities" (among other terms) are vague and not defined, the scope of the draft EO is potentially very far-reaching. Similarly, the phrase "reasonable expectation that parties would use those contributions . . ." is a concept incorporated into the draft EO without any definition or interpretation. As a result, it is not clear whose political contributions the bidding entity must disclose or under what circumstances they must be disclosed.

To take but one example of the practical difficulties this vagueness creates, consider the parent-subsidiary relationship. Clearly, activity by certain subsidiaries would have to be disclosed, but it is unclear how far "within its control" reaches with respect to subsidiaries, joint ventures, etc.

Moreover, because of the undefined language in the draft EO, including the "reasonable expectation" phrase mentioned above, donations to 501(c)(4) and 501(c)(6) organizations could be subject to disclosure under the President's proposal if such entities are politically active with respect to federal elections or engage in radio and television grassroots advertisements near a federal election where the ads mention or feature federal candidates (known as "electioneering communications"). Donations to 501(c)(3) charities would be less likely to be disclosed since such charities may not, per federal tax law, make contributions or expenditures in connection with elections, although such entities might, given a rare confluence of facts and circumstances, permissibly engage in issue ads that fall within the definition of electioneering communications.

2. Current Federal Campaign Finance Law

The draft EO would be issued in the context of current campaign finance law, which already affects many of the contributions targeted by the draft EO.

Federal campaign finance law currently prohibits all federal contractors from making contributions to candidates for federal office, federal political party committees, and federal PACs. *See* 2 U.S.C. § 441c(a)(1). This ban does not, however, extend to a separate segregated fund or political action committee ("PAC") connected to a federal contractor, *id.* § 441c(b), or to a contractor's directors, officers, or employees, assuming such individuals are not foreign nationals. The PACs, directors, officers, and employees are, like all PACs and individuals, limited in how much they may contribute to federal political committees and candidates, *id.* § 441a(1), and such contributions in excess of $200 per election or calendar year, as appropriate, are publicly disclosed on the recipients' campaign finance reports filed with the Federal Election Commission ("FEC") (and available at www.fec.gov), *id.* § 434(b)(3)(A). Moreover, all federal PACs must disclose all of their disbursements to the FEC, *id.* § 434(b)(4), and the contributions

of the PACs of employers of federal lobbyists are also reported publicly on semiannual Lobbying Disclosure Act reports (Form LD-203), *id.* § 1604(d).

Under federal campaign finance laws, corporations may not require their directors and officers to make contributions, for political contributions are a voluntary and personal decision. *See id.* § 441b(b)(3). Moreover, there is no requirement that a company track the individual contributions of its officers or directors. In fact, such tracking could be problematic under the Federal Election Campaign Act ("FECA") and employment law (with respect to the officers). Although the personal federal political contributions and expenditures of officers and directors are publicly available on the FEC's website, for the same FECA and employment-law reasons, attorneys often caution corporations against researching such information with respect to their directors, officers, and employees.

3. Pay-to-Play Laws Around the Nation

In the past several years, one of the major trends in campaign finance law throughout the country has been the adoption of so-called "pay-to-play laws." By pay-to-play laws, I mean laws, ordinances, and rules designed to prevent "paying" (*i.e.*, providing political contributions) in order to "play" (*i.e.*, receiving a grant, contract, etc. from the government). Scandals triggered most of these laws, although, in an ironic twist, it was the imminent application of Illinois' pay-to-play laws that led to the downfall of Illinois Governor Blagojevich.

By my count, 21 states and 13 major local jurisdictions now have pay-to-play laws of some sort. In addition, many smaller localities in California and New Jersey, among other states, also have such rules. Some of these rules, such as the rules of the State Investment Council of New Jersey and the Teacher Retirement System of Texas, are targeted specifically to persons involved in the financial services industry, although most are of general application to persons who hold or seek contracts with the given government entity.

There is an almost infinite variety among the pay-to-play laws around the country. Some are at the state level, others at the municipal level, and still others at the agency level. Some state laws apply at both the state and local levels. Several of the pay-to-play laws employ contribution bans, while several others limit contributions, and still others employ only a disclosure mechanism. Moreover, some of the pay-to-play laws are limited to the contracting entity whereas others encompass related business entities, PACs, owners, directors, officers, and other employees. The application of the laws range from the duration of the procurement process itself to a look-back period of four plus years. Finally, some of the laws focus exclusively on no-bid contracts, whereas others also cover competitively bid contracts.

Importantly, the real difference among the many pay-to-play laws is their ability to address the issues of corruption and the appearance of corruption. The most targeted pay-to-play laws are those adopted in the context of a procurement process where elected officials or their political appointees make the ultimate contracting decisions. Examples include the Municipal Securities Rulemaking Board's ("MSRB") Rule G-37, New Mexico's general state pay-to-play law, and San Francisco's pay-to-play ordinance. In these jurisdictions, the ban, limit, or disclosure requirement has a direct connection to the contracting process.

By contrast, in jurisdictions where the contracting officers are more insulated from the influence of elected officials and their political appointees, any "pay-to-play" laws merely employ pay-to-play terminology in order to ease passage under the banner of "reform." The rules in these jurisdictions impose burdens on core First Amendment activities that have real effects, but, given the context of the applicable procurement laws, can provide no positive benefit to the contracting process or the political process.

B. The Draft EO Is Not A Targeted Pay-to-Play Law

In its opening paragraphs, the draft EO styles itself as a pay-to-play provision, modeled after efforts in the states. Although it may resemble one or more of the non-targeted pay-to-play rules, the draft EO differs greatly from what is the focus of the targeted pay-to-play rules in the states and localities. The result is that any disclosures are marginally related to the integrity of the procurement process.

1. The Draft EO Would Not Prevent Corruption

If adopted, the draft EO would operate in the context of the federal contracting rules under which source selection decisions are most often made by contracting officers and other civil servants insulated from the pressures of the electoral marketplace. These personnel are neither elected officials nor appointees of elected officials and heretofore have not been privy to the political activities of those seeking federal contracts.

The draft EO would puncture these safeguards, then, by introducing the political into an area where politics and political contributions are not currently part of the calculus. This contrasts sharply with the state and local experiences where elected officials often make or approve the contracting decisions or appoint the commissioners or others who make or approve such decisions. In such states and localities, politics already is a part of the contracting process. Thus, rather than introduce politics into the system, the state and local pay-to-play laws seek to remove or limit the influence of politics.

The federal contracting process is different. Since elected officials and their political appointees are typically not directly involved in federal contracting decisions, even an absolute ban of political activities by the bidders, their affiliates, and their officers and directors would not have any meaningful effect on the contracting process. With respect to the draft EO, the disclosure of the bidders' political activities would do even less. In fact, although one can

readily read an inference of corruption in the language of the draft EO, neither the draft EO, the manufactured findings that were part of the DISCLOSE Act when it was introduced in the House, the findings of the House committee on the DISCLOSE Act, nor any recent commentary on the draft EO provides empirical evidence that political contributions have led to a corruption of the federal contracting process.

If acquisition professionals are fully insulated from the reportable political activity, then the draft EO is woefully misplaced. If, on the other hand, the insulation is insufficient or incomplete under some circumstances, then the draft EO is a distraction from the real and immediate task at hand – fixing the problematic areas of the federal procurement process.

2. The Draft EO Would Not Prevent the Appearance of Corruption, But Would Instead Inject Partisanship into the Process

Combating the appearance of corruption can serve as a legitimate basis for a pay-to-play law. Nonetheless, the draft EO cannot provide such a basis when it does not, as stated above, combat actual corruption.

As supporters of the draft EO have indicated, one of the aims of the draft EO is to show taxpayers where contractors spend their profits.[1] These supporters themselves, however, have exacerbated the cynicism of the public (the "appearance of corruption"), for with every reform pronouncement on the draft EO, they have tied contributions with federal contracts even though they have not and cannot produce any evidence of actual corruption.

Moreover, the process of making this political activity public through the draft EO will likely make the public more cynical unless, as discussed in detail below, the bidders and their affiliates and officers and directors cease all political activity to protect themselves. Despite the

---

[1] It must be profits since political activity and lobbying activity are both unallowable under FAR cost principles.

lack of a connection between political activity and the federal contracting process, the mandatory reports of the bidders will explicitly tie political activity to particular procurements, and periodic news reports will remind the public regularly of the nexus created solely by the draft EO. The bootstrapping of a "reform" mechanism on the government contract process thus will breed public cynicism rather than foster additional confidence in government decisionmakers.

Finally, contrary to common assumptions, the disclosures mandated by the draft EO would not support any informational interest if, in fact, one exists in this context at all. Disclosure would be required without any "sufficiently important" government interest that bears a "substantial relation" to the disclosure requirement, *Citizens United v. FEC*, 130 S.Ct. 876, 914 (2010), since the premise of the requirement for disclosure, *i.e.*, that the disclosed contributions entail corruption in the contracting process, is a faulty one. Moreover, in the marketplace of ideas, the federal government would effectively be putting its thumb on the scale through the operation of the draft EO. In the draft EO and the databases that would be created as a result, the government would be proclaiming to the public the idea that these contractor contributions were different in that they do or may corrupt the government contracting process. Since this is false, the context of this forced disclosure would "officially" skew the public's perception of these contributions and may subtly and unjustifiably alter the electoral decisions the public may make as a result. This contrasts with the requirement of general disclosure currently found on the FEC's website, where all contributions and expenditures are disclosed without distinction.

3. The Draft EO Attacks Independent Expenditure Activity That Does Not Cause Corruption or the Appearance of Corruption

The inadequacies of the draft EO discussed above are reflected in two particular elements of the mandated disclosure regime. This is the targeting of activities that go beyond

contributions – independent expenditures and electioneering communications. By contrast, state and local pay-to-play laws, even the non-targeted ones, remain focused on contributions.

Although the U.S. Supreme Court has repeatedly stated that independent expenditures do not corrupt or cause the appearance of corruption, *see, e.g., Citizens United*, 130 S.Ct. at 908-11; *Buckley v. Valeo*, 424 U.S. 19, 47 (1976), the draft EO tramples further into the realm of core speech by requiring disclosure of such expenditures by bidders and their affiliates, officers, and directors. In this respect, it is telling that I have found only one state or local jurisdiction that extends its pay-to-play reach directly to independent expenditures – Nebraska – and then only with respect to its lottery division. No other jurisdiction appears to include contractor independent expenditures as part of its pay-to-play laws –even as part of a disclosure mechanism.

A good example of why the pay-to-play laws focus on contributions and not independent expenditures can be found in recent activity at the U.S. Securities and Exchange Commission ("SEC"). In implementing its recent and very stringent pay-to-play contribution ban and limits for investment advisers, the SEC was very concerned about preventing actual corruption and the appearance of corruption. After reviewing the relevant case law, the SEC concluded that its anti-corruption goal was achieved by restricting only direct contributions. *See Political Contributions by Certain Advisors*, 75 Fed. Reg. 41,018, 41,023-24 (July 14, 2010). In fact, the SEC specifically disclaimed any interest in regulating independent expenditures. *See id.* at 41,024 ("[T]he rule does not in any way impinge on a wide range of expressive conduct in connection with elections. For example, the rule imposes no restrictions on activities such as making independent expenditures to express support for candidates . . . ."); *see also id.* at 41,030

("We also note that 'contributions' are not intended to include independent 'expenditures,' as that term is defined in 2 U.S.C. 431 & 441b.") (internal citations omitted).

4. The Draft EO Attacks Electioneering Communications That Do Not Cause Corruption or the Appearance of Corruption

Even further afield from contributions and the possible sources of corruption and the appearance of corruption is the draft EO's targeting of contributions to third parties for electioneering communications. As a reminder, electioneering communications are, at least under federal campaign finance law, television and radio ads aired in a relevant congressional district or state 30 days before a primary or 60 days before a general election that mention or feature a federal candidate in that jurisdiction. Electioneering communications do not involve express advocacy, as such communications are defined as independent expenditures or, if coordinated, in-kind contributions. The inclusion of electioneering communications in the draft EO thus implicates grassroots lobbying advertisements, which are even further removed from the pay-to-play sphere than independent expenditures.

No state or locality, not even Nebraska's lottery division, purports to apply its pay-to-play ban, limit, or disclosure requirements to payments made for such grassroots lobbying activities. Like independent expenditures, electioneering communications are independent and unable to cause the corruption or appearance of corruption that pay-to-play laws attempt to address. The draft EO, on the other hand, improperly targets such lobbying activities without any anti-corruption rationale for doing so.

C. Bidders and Their Affiliates and Officers and Directors Will Rationally Curtail Political Activities as a Result of the Draft EO

Compliance by corporations with any pay-to-play law has two dimensions: corporate and personal. In both cases, compliance with the draft EO is likely to have negative ramifications on

core First Amendment activity by introducing uncertainty as to the use of political information in the contracting process. Uncertainty means risk.

1. The Draft EO Will Reduce Corporate Political Involvement

In my experience, there is no doubt that many contractors will refrain from any activity, including political activity, that gives even the appearance of making them less competitive vis-à-vis one or more contracts. With the draft EO, the risk for the contractor is that its political activity could reduce its competitive profile with respect to the contracts on which it will be bidding – whether the risk comes from the fact that the contractor engaged in any reportable political contributions at all, the magnitude of such contributions, or the identity of the recipients of the reportable contributions. Thus, the contractor will likely follow rational risk mitigation strategies and reduce or eliminate the reportable activity. (In the worst case scenario, the contractor may increase reportable activity that benefits the incumbent administration on the theory that it may decrease its risk of reporting little or no support – the opposite, I think all would agree, of the stated goal of the draft EO.)

As stated above, federal contractors are prohibited from making contributions, so the corporate activity that will be reduced will be the contributions to third parties that might possibly make independent expenditures or electioneering communications. In fact, this appears to be the goal of the draft EO even though there is no reported link between independent expenditures or electioneering communications and the contractor activity at the federal level. Since we do not know how the FAR Council is going to implement the draft EO, it is difficult to measure the activities that the contractor will curtail. If, in the worst case scenario, reportable contributions extend to dues payments to trade associations and similar groups, then the draft EO will not only undermine permissible political activities, which is problematic enough, but also

will work to defund trade associations and other groups so that they cannot engage in their representational activities in all spheres of modern life – legislative, social, media, political, etc.

2. The Draft EO Will Reduce Personal Political Activity

The draft EO also will negatively affect the personal political activities of covered officers and directors. First, officers and directors, even in large contractors, may internalize the corporate reaction discussed above, although, in the context of officers and directors, this reaction would affect candidate and party contributions as well. Second, although large corporations can offer parallel compliance processes and management structures that provide some comfort to the provision by employees of personal political information to the corporation, small businesses may not have the luxury of these duplicative processes. In such cases, the employee-employer relationship is particularly politicized given that officers, for example, may need to report contributions to persons with whom they may have a direct report relationship. If the subordinate officer feels his or her personal contributions may either cause problems for upcoming contract bids or be adverse to the political leanings of a superior, then the officer will rationally choose to curtail such contributions.

Although contributions of more than $200 are already itemized and reported to the FEC, the draft EO would be the particular source of this chilling effect given that (1) the reported contributions would be officially tied to the contractor participating in a bid; (2) the contributions would be reported as part of the bidding process; and (3) the company would have to collect the information in order to report it. Currently, corporations are not required to report the political activities of their employees, and, in fact, attorneys advise companies not to investigate the publicly-available campaign finance information about their employees – for employment law as well as campaign finance reasons. The draft EO would, then, change the employee/corporate balance under the campaign finance laws for contractors.

3. The Vague Language Found in the Draft EO Exacerbates the Risks

The risks presented by the draft EO are exacerbated by the vague language used in the draft EO and the lack of clear guidance. Although the FAR Council will have a chance to weigh in on the final rules, campaign finance is not one of the Council's core competencies, and it will be tasked with providing guidance on an expedited basis (by the end of the year) amid a Presidential election cycle. In any event, such vagueness often is not clarified in the rulemakings or guidance that subsequently emanates from the responsible agencies (just look at the MSRB's guidance on Rule G-37 for examples of a lack of clarity). Vagueness causes an even broader swath of political activity to be chilled.

Vagueness is present because the draft EO is filled with undefined terms. One of the most dangerous vague ideas in the draft EO is the phrase "with the intention or reasonable expectation" used with respect to contributions made to third parties. It is not clear what this might mean, and I fear that the FAR Council may not provide any additional clarity. To the extent that reportable contributions turn on the intent of the contributor, then this phrase just serves as the precursor to an unending number of disputes over any unreported third-party contributions. If the bidder made a payment to a third party, there must be some objective criteria by which it can determine whether the payment is reportable. The "reasonable expectation" language does not help much, given that reasonableness will be based on the time and place of the decision to contribute and/or the actual contribution, often a fact-specific determination. With hindsight, however, others, including competing bidders, losing bidders, political opponents, and the government acquisition officials themselves, may see some other, after-the-contribution development with respect to the third party and challenge the bidder's certification, protest the contract award, and generally embark on a fishing expedition with respect to any contributions not reported. Besides these needless and intrusive investigations,

such risks may lead to pre-clearance by the company of all covered directors' and officers' activities in order that the company may analyze all the risks before any reportable contributions are made.

APPENDIX A

Draft 4/13/11; 4:00 pm

EXECUTIVE ORDER

- - - - - - -

DISCLOSURE OF POLITICAL SPENDING BY GOVERNMENT CONTRACTORS

By the authority vested in me as President by the Constitution and the laws of the United States of America, including the Federal Property and Administrative Services Act, 40 U.S.C. 101 et seq., and to ensure the integrity of the federal contracting system in order to produce the most economical and efficient results for the American people, it is hereby ordered that:

Section 1. The Federal Government must ensure that its contracting decisions are merit-based in order to deliver the best value for the taxpayer. It is incumbent that every stage of the contracting process - from appropriation to contract award to performance to post-performance review - be free from the undue influence of factors extraneous to the underlying merits of contracting decision making, such as political activity or political favoritism. It is important that the contracting process not only adhere to these principles, but also that the public have the utmost confidence that the principles are followed. When the public lacks confidence that the contracting system works fairly, it may deter participation and deprive the government of the most robust competition and the best providers. And without the full complement of tools to hold the system accountable, the possibility of actual misconduct or the appearance thereof is increased.

In order to begin to address these problems, the Federal Government prohibits federal contractors from making certain contributions during the course of negotiation and performance of a contract. Notwithstanding these measures and the diligent work of the government's contracting officers and other acquisition professionals, additional measures are appropriate and effective in addressing the perception that political campaign spending provides enhanced access to or favoritism in the contracting process. Several states have adopted "pay-to-play" laws that go further by limiting not only contributions by the contracting entity itself, but also by certain officers and affiliates to prevent circumvention and in other cases by requiring disclosure. This state innovation towards better government should be encouraged and the Federal government should draw from the best practices developed by the states.

Sec. 2. Therefore, in order to increase transparency and accountability to ensure an efficient and economical procurement process, every contracting department and agency shall require all entities submitting offers for federal contracts to disclose certain political contributions and expenditures that they have made within the two years prior to submission of their offer. Certification that disclosure of this information has been made in the manner established by the Federal Acquisition Regulatory Council (FAR Council) pursuant to Sec. 4 shall be required as a condition of award.

This disclosure shall include:

(a) All contributions or expenditures to or on behalf of federal candidates, parties or party committees made by the bidding entity, its directors or officers, or any affiliates or subsidiaries within its control; and

(b) Any contributions made to third party entities with the intention or reasonable expectation that parties would use those contributions to make independent expenditures or electioneering communications.

This disclosure shall be required whenever the aggregate amount of such contributions and expenditures made by the bidding entity, its officers and directors, and its affiliates and subsidiaries exceeds $5,000 to a given recipient during a given year.

Sec. 3. All disclosed data shall be made publicly available in a centralized, searchable, sortable, downloadable and machine readable format on data.gov as soon as practicable upon submission.

Sec. 4. On or before the end of this calendar year, the FAR Council shall adopt such rules and regulations and issue such orders as are deemed necessary and appropriate to carry out this order. Such rules, regulations, and orders shall minimize the costs of compliance for contractors and shall not interfere with the ability of contractors or their officers or employees to engage in political activities to the extent otherwise permitted by law.

Sec. 5. Each contracting department or agency shall cooperate with the FAR Council and provide such information and assistance as the FAR Council may require in the performance of its functions under this order.

Sec. 6. (a) This order shall be implemented consistent with applicable law and subject to the availability of appropriations.

(b) This order is not intended to, and does not, create any right or benefit, substantive or procedural, enforceable at law or in equity by any party against the United States, its departments, agencies, or entities, its officers, employees, or agents, or any other person.

Sec. 7. This order shall become effective immediately, and shall apply to contracts resulting from solicitations issued on or after the effective date of the action taken by the FAR Council under section 4 of this order.

THE WHITE HOUSE,