

# LOWENSTEIN SANDLER PC CLIENT ALERT

## PAY TO PLAY

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### READ THIS BEFORE MAKING YOUR NEXT POLITICAL CONTRIBUTION: PAY TO PLAY LEGISLATION EXPANDED

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**On September 24, 2008, Governor Jon Corzine issued Executive Orders 117 and 118, which expand the scope of circumstances in which a business that makes political contributions may be disqualified from doing work for State-level executive agencies in New Jersey.**

The executive orders go into effect on November 15, 2008, and therefore, businesses that engage in (or contemplate seeking) such government work must immediately become familiar with these new "pay to play" laws to prevent disqualification for contributions made on or after that effective date.

Among other changes, Executive Order 117 expands the scope of individuals whose contributions can disqualify a business from State work to include such individuals as partners, LLC members, and corporate officers, as well as their spouses/civil union partners and children residing at home under some circumstances. Executive Order 117 also widens the categories of disqualifying political contributions. Executive Order 118 extends pay to

play restrictions to State redevelopment projects. Governor Corzine has also announced a series of proposals that would require legislative action to eliminate a number of perceived "loopholes" in other pay to play laws.<sup>1</sup>

We are pleased to provide this summary of the new executive orders and the proposed legislation.

#### **A Brief Review of Pre-Existing Pay to Play Laws**

To understand the modifications brought about by the new executive orders, a brief review of the pre-existing pay to play laws applicable to State-level work is required. In September 2004, then-Governor James McGreevy issued Executive Order 134,<sup>2</sup> which was later codified as amended by legislation known as Chapter 51.<sup>3</sup> Executive Order 134 and Chapter 51 disqualify businesses from contracts with State-level executive agencies<sup>4</sup> if the business has made a contribution of more than \$300 to the current Governor, any candidate for Governor, or any State or county political party committee within eighteen months of the commencement of contract

negotiations.<sup>5</sup> If the contribution is made to the sitting Governor or to a State or county political party committee of the same party as the Governor within the last eighteen months of the Governor's term, the period of disqualification can be extended for the entire term of the next Governor elected (if from the same party).<sup>6</sup>

Under Executive Order 134 and Chapter 51, contributions made to political action committees ("PACs") formed under New Jersey law are not automatically disqualifying.<sup>7</sup> Rather, any such contribution made in the prior four years must be disclosed in advance of contract negotiations.<sup>8</sup> The New Jersey Department of the Treasury may disallow any contract award if it finds that a PAC contribution amounts to a "conflict of interest."<sup>9</sup>

#### **Executive Order 117 — Which Contributions Matter?**

Executive Order 117 expressly modifies the terms of Executive Order 134 and greatly expands the key personnel of the business whose contributions can result in disqualification.<sup>10</sup> For example,

under Executive Order 134, only contributions by partners and LLC members owning 10% or more of the business could be attributed to the business.<sup>11</sup> Now, in contrast, Executive Order 117 sweeps in a vast array of additional individuals whose contributions can disqualify a business.

Under Executive Order 117, the contributions of *any* partner, LLC member, or shareholder of a

professional corporation — regardless of level of ownership — are attributed to the business and will result in disqualification.<sup>12</sup> Additionally, for the first time, contributions made by corporate officers are disqualifying.<sup>13</sup> Finally, for each individual included in Executive Order 117 (e.g., partners, members, corporate officers), the contributions of that individual's spouse or civil union partner and children who reside with the individual

also may be attributed to the business.<sup>14</sup> Such spousal/child contributions are exempt if made to a candidate for whom the spouse/child is entitled to vote or to a political committee located in the jurisdiction where the spouse/child resides.<sup>15</sup>

A table comparing the attribution rules for contributions made by individuals under Executive Orders 134 and 117 is set forth below:

Type of Contributor	Executive Order 134 <i>Contributions are attributed to the business entity if made by the entity or:</i>	Executive Order 117 <i>Contributions are attributed to the business entity if made by the entity or:</i>
Corporation	10%+ Shareholder	10%+ Shareholder Any Officer
Professional Corporation	10%+ Shareholder	Any Shareholder Any Officer
General Partnership	Partner Owning 10%+	Any Partner
Limited Partnership	Partner Owning 10%+	Any Partner
Limited Liability Partnership	Partner Owning 10%+	Any Partner
Limited Liability Company	Member Owning 10%+	Any Member
Sole Proprietorship	Sole Proprietor	No Change
Other Form of Entity	10%+ Owner	Any Principal Any Officer Any Partner
PAC Controlled by Business Entity <sup>16</sup>	PAC	No Change
Subsidiary Controlled by Business Entity	Subsidiary	No Change
Spouse/Civil Union Partner of Individual	Sole Proprietor's Spouse/ Civil Union Partner	Any of the above individuals' Spouse/Civil Union Partner (with exemptions)
Resident Child of Individual	Sole Proprietor's Resident Child	Any of the above individuals' Resident Child (with exemptions)

Executive Order 117’s expanded attribution rules could have a dramatic effect on certain businesses, especially those with substantial portfolios of State work. Accordingly, such businesses are well-advised to

committees,<sup>18</sup> municipal political party committees, or the Lieutenant Governor or candidate for such office.<sup>19</sup>

A table comparing Executive Orders 134 and 117 is included below:

## Executive Order 118 — Pay to Play Restrictions Applied to Agreements with State Redevelopment Entities

Executive Order 118<sup>22</sup> applies to redevelopment agreements with any

Type of Political Recipient	Executive Order 134 <i>Contributions are disqualifying if made to:</i>	Executive Order 117 <i>Contributions are disqualifying if made to:</i>
Officeholders/Candidates	Governor Candidate for Governor	Governor Candidate for Governor <i>Lieutenant Governor</i> <i>Candidate for Lieutenant Governor</i>
Political Party Committees	State County	State County <i>Municipal</i>
Legislative Leadership Committees	Not Included	<i>Included</i>
Political Action Committees (PACs)	Disclosure Required, Conflict of Interest Review	No Change

implement a system to monitor and, if needed, control the political giving by their key personnel, their spouses or civil union partners, and resident children.

### Relevant Recipients Expanded

In addition to expanding the universe of relevant contributors, Executive Order 117 also expands the scope of recipients to whom disqualifying contributions may be made. Previously, under Executive Order 134, only those contributions to the Governor, candidate for Governor, or any State or county political party committee could result in disqualification.<sup>17</sup> Now, under Executive Order 117, disqualifying contributions include those to legislative leadership

### Seeking Refund of Inadvertent Contributions

In the event that a disqualifying contribution is inadvertently made, a business can take steps to obtain a refund of the contribution and avoid disqualification, but the timeframe is exceedingly short. The business must issue a written request to the recipient candidate or organization for a refund of the contribution *and* physically receive the refund within thirty days.<sup>20</sup> Recent case law illustrates that reliance on this clawback provision can be a risky proposition. The thirty-day time period has been strictly interpreted so that a business will face disqualification even if it sought a refund before thirty days had elapsed, but the refund was delayed due to the inaction of the recipient political organization.<sup>21</sup>

“State redevelopment entity,” which is defined broadly to include State-level executive agencies, as well as independent State authorities, boards, commissions, and other governmental entities.<sup>23</sup> Under Executive Order 118, a redeveloper will be disqualified from redevelopment agreements by contributions made by the redeveloper’s partners, members, and corporate officers, and their spouses/civil union partners or resident children.<sup>24</sup> The redeveloper can also be disqualified by the contributions of any “subsidiary business entity” and any “business entity” retained by the redeveloper to “perform professional, consulting, or lobbying services in connection with the redevelopment project.”<sup>25</sup> The reach of these latter two provisions is particularly wide; for example, under

Executive Order 118, a redeveloper that retains a law firm to provide counsel in connection with the redevelopment project can be disqualified by a contribution made by the resident child of a partner of that firm.

Under Executive Order 118, contributions are disqualifying if made to (i) the Governor or any candidate for Governor; (ii) the Lieutenant Governor or any candidate for Lieutenant Governor; (iii) any State, county, or municipal political party committee; (iv) any legislative leadership committees; or (v) any State, legislative, county, or municipal candidate or officeholder in the legislative district, county, or municipality where the redevelopment project is located.<sup>26</sup>

### **New Executive Orders Given Prospective Effect Only**

Executive Orders 117 and 118 go into effect on November 15, 2008, and have only "prospective effect."<sup>27</sup> In other words, contracts and redevelopment agreements entered and contributions made prior to November 15, 2008 are not subject to the expanded provisions of the new executive orders (but they are still subject to Executive Order 134, Chapter 51, and the other preexisting pay to play laws).

### **Additional Pay to Play Laws Proposed**

Governor Corzine has proposed additional legislation intended to tighten the other pay to play laws. Among the proposals is a plan to extend the broad disqualification scheme set forth in Executive Orders 117 and 118 to contracting and redevelopment activities at the county and municipal level. New pay to play restrictions would also apply to developers seeking government approvals and companies hired to conduct audits of governmental bodies. Additionally, the proposed legislation seeks to counteract "wheeling" — i.e., transfers of contributions between political organizations designed to allow contributors to circumvent campaign contribution limits and pay to play restrictions.

As these executive orders and legislative proposals demonstrate, New Jersey's ever-changing legal and political landscape makes up-to-date knowledge of the pay to play laws essential for any business contemplating work with State, county, or local government. Compliance with the complex statutory and regulatory scheme frequently involves significant information-gathering efforts coupled with highly fact-sensitive analysis. Careful consideration must be given to the development of appropriate policies, protocols, and internal controls to avoid disqualification as a result of an unwitting political contribution.

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- <sup>1</sup> On the same day, Governor Corzine issued two additional executive orders addressing ethics in government. Executive Order 119 created the "Governor's Local Government Ethics Task Force," effective immediately, to be composed of eleven members who will examine the need to amend local government ethics laws. Exec. Order 119 (Sept. 24, 2008), available at <http://liberty.state.nj.us/infobank/circular/eom119.htm>. Executive Order 120 amends a previously-enacted financial disclosure law to include certain additional public officials, including the state comptroller. Exec. Order 120 (Sept. 24, 2008), available at <http://liberty.state.nj.us/infobank/circular/eom120.htm>.
- <sup>2</sup> Exec. Order 134 (Sept. 22, 2004), available at <http://www.state.nj.us/infobank/circular/eom134.htm>. Other pay to play laws include Chapter 19, which restricts the ability of businesses that made certain political contributions from entering contracts with the Legislature, counties, or municipalities. N.J.S.A. 19:44A-20.2 to -20.5. Chapter 271 requires a business to disclose its political contributions made within the twelve months prior to the award of certain contracts and, if the business received \$50,000 or more in government contracts in a given year, to file an annual disclosure statement providing detailed contract and contribution information. N.J.S.A. 19:44A-20.26 to -20.27. Later amendments to Chapters 19, 51, and 271 excluded non-profit organizations. L. 2007, ch. 304. Additional pay to play rules have been enacted at the agency and local level. For example, the State Investment Council issued regulations setting forth disclosure and disqualification provisions applicable to investment management firms entering service contracts with the Division of Investment of the New Jersey Department of the Treasury. N.J.A.C. 17:15-4. Many counties, municipalities, and other local governmental units have also enacted their own pay to play laws applicable to contracts with those governmental entities. See <http://www.state.nj.us/state/secretary/ordinance.html> (listing local pay to play laws).
- <sup>3</sup> L. 2005, ch. 51 (codified at N.J.S.A. 19:44A-20.13 to -20.25).
- <sup>4</sup> Executive Order 134 and Chapter 51 apply to contracts with the "State or any of its purchasing agents or agencies or those of its independent authorities." Exec. Order 134 ¶ 1; L. 2005, ch. 51 ¶ 2. Regulations issued by the Election Law Enforcement Commission ("ELEC") broadly define the governmental entities involved to include "the principal departments in the Executive Branch, and any division, board, bureau, office, commission or other instrumentality within or created by such department and any independent State authority, board, commission, instrumentality or agency." N.J.A.C. 9:25-24.4.
- <sup>5</sup> N.J.S.A. 19:44A-20.14.
- <sup>6</sup> *Id.*
- <sup>7</sup> N.J.S.A. 19:44A-20.18. PACs formed under New Jersey law are technically referred to as "continuing political committees." *Id.*
- <sup>8</sup> *Id.*
- <sup>9</sup> *Id.* According to guidance published on Treasury's website, the  
Conflict of interest review involves an analysis of the committee to which the contribution was made, and a determination as to whether the contribution appears to have been an attempt to circumvent the prohibitions of the Executive Order. Further, we review information regarding the transaction and the committee to which the contribution was made to determine whether there is a nexus between the contribution and the contract award that would result in a conflict of interest.  
N.J. Dept. Treasury, Chapter 51 Q & A, Question No. 54, at <http://www.state.nj.us/treasury/purchase/execorder134Q&A.htm> (last visited October 3, 2008).
- <sup>10</sup> Exec. Order 117 ¶ 1 (Sept. 24, 2008), available at <http://liberty.state.nj.us/infobank/circular/eom117.htm>. As noted, Executive Order 134 was codified by the Legislature by Chapter 51, and it is an open question whether duly-enacted legislation (such as Chapter 51) can be modified by a subsequent executive order (such as Executive Order 117). However, it should be noted that the Legislature is currently considering legislation to adopt and codify Executive Order 117. Moreover, absent indications to the contrary, a reasonably prudent business is well-advised to treat Executive Order 117 as fully enforceable and to comply with all of its provisions and restrictions.
- <sup>11</sup> Exec. Order 134 ¶ 4.
- <sup>12</sup> Exec. Order 117 ¶ 1.a.i.B-F.
- <sup>13</sup> *Id.* ¶ 1.a.i.
- <sup>14</sup> *Id.* ¶ 1.a.iv.
- <sup>15</sup> *Id.*
- <sup>16</sup> According to guidance issued by ELEC, contributions by PACs are attributed to the business entity only if the business's management participates in the PAC's organization, decision-making, or policy formulation. See 38 N.J. Reg. 4661(a); ELEC, Adv. Op. No. 02-2007 (June 19, 2007), available at <http://www.elec.state.nj.us/pdf/AO/ao022007.pdf>. ELEC has indicated that additional regulations on this issue are forthcoming. See 38 N.J. Reg. 4661(a).
- <sup>17</sup> N.J.S.A. 19:44A-20.14.
- <sup>18</sup> Legislative leadership committees are special political organizations "established, authorized to be established, or designated by the President of the Senate, the Minority Leader of the Senate, the Speaker of the General Assembly or the Minority Leader of the General Assembly . . . for the purpose of receiving contributions and making expenditures." N.J.S.A. 19:44A-3.s.
- <sup>19</sup> Exec. Order 117 ¶ 3, 4.
- <sup>20</sup> N.J.S.A. 19:44A-20.20.
- <sup>21</sup> *In re Earle*, 401 N.J. Super. 310, 325-27 (2008). On September 23, 2008, the New Jersey Supreme Court granted certification in *Earle*, which also presents a First Amendment challenge to Executive Order 134 and Chapter 51. Oral argument has yet to be scheduled.
- <sup>22</sup> Exec. Order 118 (Sept. 24, 2008), available at <http://liberty.state.nj.us/infobank/circular/eom118.htm>. As per Executive Order 118 ¶ 10, definitions for terms such as "redevelopment" and "redevelopment project" can be found in the Local Redevelopment and Housing Law, N.J.S.A. 40A:12A-3.
- <sup>23</sup> Exec. Order 118 ¶ 1.e. Although, as a technical matter, Executive Order 118 does not apply to agreements entered with county or local redevelopment entities, legislation has been proposed to extend Executive Order 118's broad disqualification scheme to redevelopment agreements at the local and county level. Moreover, as any given redevelopment project can involve government participants from various levels, businesses currently engaged (or contemplating engagement) in redevelopment work are urged to exercise extreme caution when assessing whether a contribution will result in disqualification.
- <sup>24</sup> *Id.* ¶ 1.a.
- <sup>25</sup> *Id.* ¶ 1.c.
- <sup>26</sup> *Id.* ¶ 3.
- <sup>27</sup> Exec. Order 117 ¶ 5; Exec. Order 118 ¶ 11.

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