CENTER *for* COMPETITIVE POLITICS
Congress shall make no law...

October 1, 2014

Via Electronic Submission

Ronald W. Smith, Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

Re: Comment on Draft Amendments to MSRB Rule G-37 to Extend its Provisions to Municipal Advisors

Dear Mr. Smith,

I write on behalf of the Center for Competitive Politics ("CCP"), a § 501(c)(3) organization founded to educate the public concerning the benefits of increased freedom and competition in the electoral process. Toward that end, CCP engages in research, scholarship, and outreach to protect and promote the First Amendment rights of speech, assembly, and petition. CCP also operates a *pro bono* law center that brings legal challenges to state and federal laws and regulations that unconstitutionally burden the exercise of these freedoms.

MSRB Rule G-37 is of particular importance to CCP because it limits the ability of covered individuals to make contributions to candidates for public office. The right to support candidates in this way, regardless of occupation, is a central liberty secured by the First Amendment.

We have no doubt that Rule G-37 and the Draft Amendments are a well-intentioned effort to prevent pay-to-play practices at the state and local levels. However, both the current Rule and the Draft Amendments are vague on important particulars, or cover a wider range of activity than is necessary for the prevention of actual or perceived pay-to-play corruption. Pay-to-play practices could be prevented by alternative approaches that would lessen or eliminate any impact on First Amendment rights. Additionally, we believe the Board should more carefully consider recent Supreme Court decisions that impact the justification for campaign contribution limits and revise Rule G-37 and the Draft Amendments accordingly.

The vagueness and overbreadth of Rule G-37 and the Draft Amendments present serious constitutional concerns, in particular because the scope of covered persons and covered candidates will often be unclear, and consequently the Rule will chill activity that the MSRB likely does not intend to cover. The MSRB appears aware of this difficulty, and CCP applauds the Board's attempts to provide greater clarity in some portions of the Draft Amendment than what currently exists in the present Rule. Nevertheless, because the Draft Amendments largely preserve the existing vagueness and overbreadth problems of Rule G-37, while expanding the regulatory scope of the Rule, CCP writes to express concerns with the present Draft.

124 West Street South, Ste 201 Alexandria, VA 22314 www.campaignfreedom.org P: 703.894.6800 F: 703.894.6811

Below, I highlight CCP's most pressing and specific concerns. Before I address these issues, I begin by noting two areas where the Amendments do recognize constitutional issues or increase Rule G-37's clarity and precision, and urge the Board to build much more substantially on those elements if it proceeds to amend Rule G-37.

I. The Draft Amendments recognize that restrictions on First Amendment rights must be tailored to prevent *quid pro quo* corruption.

CCP commends the MSRB for recognizing that it must incorporate the United States Supreme Court's constitutional precedents into Rule G-37. In particular, the MSRB has taken the important step of recognizing that "corruption," in a legal sense, is limited to *quid pro quo* or "dollars for favors" transactions. Since its landmark campaign finance ruling in *Buckley v. Valeo*, the Supreme Court has recognized that, in order to be consistent with the First Amendment, restrictions on political contributions must be tailored to target actual or apparent corruption, meaning *quid pro quo* arrangements.[1] The Court's recent rulings in *Citizens United v. FEC*[2] and *McCutcheon v. FEC*[3] provide a strong signal that such restrictions will be carefully scrutinized.

The Regulatory Notice incorporates this understanding by reiterating from the outset that "'pay to play' practices typically involve a person making cash or in-kind political contributions (or soliciting or coordinating others to make such contributions) to help finance the election campaigns of state or local officials or bond ballot initiatives as a *quid pro quo* for the receipt of government contracts."[4] Constitutionally permissible regulations, as the Regulatory Notice recognizes, must be appropriately tailored to further this end, without unnecessarily stifling the exercise of First Amendment rights.[5] It is laudable that the Board has preserved this understanding of corruption in the Draft Amendments to Rule G-37, as misunderstanding the permissible scope of "corruption" is a common error. The Board's recognition[6] of *Buckley*'s requirements should guide any amendments it ultimately adopts.

Unfortunately, while the Board recognizes that the regulation should be tailored so as to address *quid pro quo* transactions, the Draft Amendments fall short of the tailoring needed under the First Amendment.

II. The Draft Amendments add several new definitions that increase precision and clarity in Rule G-37.

The Draft Amendments bring some welcome, albeit limited, clarity to Rule G-37 by defining previously ambiguous terms. Substituting the term "municipal entity"—as defined in the

---

[1] 424 U.S. 1 (1976).
[2] 558 U.S. 310 (2010).
[3] 134 S. Ct. 1434 (2014).
[4] MUNICIPAL SECURITIES RULEMAKING BOARD, REGULATORY NOTICE 2014-15, REQUEST FOR COMMENT ON DRAFT AMENDMENTS TO MSRB RULE G-37 TO EXTEND ITS PROVISIONS TO MUNICIPAL ADVISORS (2014) ("Regulatory Notice") at 3
[5] *See, e.g., Id.*
[6] *See, e.g., Id.*

Exchange Act[7]—for the term "issuer" throughout the Rule is one such instance. This is commendable as it makes it easier for the regulated community to know who, exactly, is subject to the Rule without having to negotiate various definitions and standards.

Similarly, Draft Rule G-37(b)(ii)(B) contains a safe harbor for contributions made before the contributor becomes a dealer solicitor or municipal advisor. This would appropriately require that there be a real opportunity for actual or apparent *quid pro quo* corruption before First Amendment activity is stifled. The same is true for the similar exclusion under Draft Rule G-37(b)(ii)(C), applicable to contributions made more than six months before becoming a municipal finance professional or municipal advisor professional. Both provisions improve upon the existing Rule.

Finally, replacing "the term 'official of an issuer' with the new defined term 'official of a municipal entity' takes into account the possibility that an official may have the ability to influence the selection of a dealer but not a municipal advisor, or vice versa."[8] This tailoring is welcome, as is the MSRB's judicious notation that "these separate categories are created to ensure that there is a nexus between the contribution and the awarding of business that gives rise to a sufficient risk of corruption or the appearance of corruption to warrant a two-year ban."[9] This, indeed, is the fundamental idea behind the constitutional tailoring that the Supreme Court has required.

III. The Draft Amendments preserve, and in some cases exacerbate, existing vagueness and overbreadth.

Regrettably, the Draft Amendments, while providing some additional clarity in certain areas, are confusing in many others. One example is the proposed definition of the term "official of a municipal entity." This phrase denotes two types of officials, based upon the type of selection influence they exercise: an "official with dealer selection influence"[10] and an "official with

---

[7] *See* Exchange Act Rule 15Ba1-1(g),17 C.F.R. 240.15Ba1-1(g) (2014). which defines municipal entity to mean "any State, political subdivision of a State, or municipal corporate instrumentality of a State or of a political subdivision of a State, including: (1) Any agency, authority, or instrumentality of the State, political subdivision, or municipal corporate instrumentality; (2) Any plan, program, or pool of assets sponsored or established by the State, political subdivision, or municipal corporate instrumentality or any agency, authority, or instrumentality thereof; and (3) Any other issuer of municipal securities." The term includes both issuers of municipal securities as well as certain non-issuer entities. Examples of non-issuer municipal entities include public pension funds, local government investment pools ("LGIPs"), other state and local governmental entities or funds, and participant-directed investment programs or plans, such as 529 and 403(b) plans.

[8] Regulatory Notice at 11.

[9] *Id.* at 11-12.

[10] Draft Rule G-37(g)(xvi)(A) ("'Official with dealer selection influence' means any person (including any election committee for such person) who was, at the time of the contribution, an incumbent, candidate or successful candidate: (1) for elective office of the municipal entity which office is directly or indirectly responsible for, or can influence the outcome of, the hiring by the municipal entity of a dealer for municipal securities business or (2) for any elective office of a state or of any political subdivision, which office has authority to appoint any person who is directly or indirectly responsible for, or can influence

municipal advisor selection influence."[11] The decision to replace the term "official of an issuer" with the term 'official of a municipal entity' is, as noted previously, itself a positive development. These definitions, however, worsen existing overbreadth and vagueness problems in several important ways.

First, the definitions encompass all incumbents or candidates for an office which is "directly *or indirectly responsible for, or can influence* the outcome of" the decision to hire a dealer for municipal securities business or an advisor for municipal advisory business.[12] It also includes incumbents and candidates "for any elective office of a state or of any political subdivision, which office *has authority to appoint* any person who is *directly or indirectly responsible for, or can influence the outcome* of" such hiring.[13]

The breadth of this definition is staggering. The inherent vagueness of "indirect influence" and "indirect responsibility" is self-evident. Moreover, there are no articulated standards sufficient to guide the regulated community in determining who is and is not a qualified officeholder (and consequently, which contributions do and do not trigger the ban on business). This in and of itself stifles activity protected by the First Amendment. What is more, the definitions extend to *candidates* for office, prohibiting contributions simply because someone is running for an office that may not, in fact, have any connection to any municipal dealer or advisor selection. Even a contribution to a losing candidate would appear to trigger sanctions under the Draft Amendments.

This lack of clarity will inevitably mean that some contributions that would otherwise be made, and which pose little to no danger of pay-to-play corruption, will not be made. That is itself a substantial First Amendment harm.

The definition of "solicit" under Draft Rule G-37(g)(xix) suffers from similar problems, arising from an effort to achieve comprehensive regulation through overbroad language. This definition includes "a direct or indirect communication with a municipal entity for the purposes of obtaining or retaining an engagement" for dealer or adviser regulated under the Rule.[14] The spirit of this rule is easily understood—to avoid a *quid pro quo* of dollars for municipal business. But the phrase "indirect communications" is undefined, and worse, uncabined. In fact, as the hallmark of a communication is the conveyance of information from one person to another, it is not clear what an "indirect communication" entails; either information is conveyed or it is not.

---

the outcome of, the hiring by a municipal entity of a dealer for municipal securities business by an issuer.")

[11] Draft Rule G-37(g)(xvi)(B) ("'Official with municipal advisor selection influence' means any person (including any election committee for such person) who was, at the time of the contribution, an incumbent, candidate or successful candidate: (1) for elective office of the municipal entity which office is directly or indirectly responsible for, or can influence the outcome of, the hiring by the municipal entity of a municipal advisor for municipal advisory business; or (2) for any elective office of a state or of any political subdivision, which office has authority to appoint any person who is directly or indirectly responsible for, or can influence the outcome of, the hiring by a municipal entity of a municipal advisor for municipal advisory business.")

[12] Draft Rule G-37(g)(xvi)(A)-(B).

[13] *Id.*

[14] Draft Rule G-37(g)(xix).

Draft Rule G-37(c)(i) and (ii) prohibit solicitation (though under a different definition of "solicit" than applies elsewhere in the Rule) and coordination of contributions. This portion of the Draft Rule is overbroad because it applies to dealers or municipal advisors that are "engaging or seeking to engage in municipal securities business or municipal advisory business."[15] How can a regulated person determine whether such actors are "seeking" to engage in this type of business? Even if this provision were decipherable, it would surely present significant difficulties of proof. Perhaps more importantly, it will deprive regulators of a clear and consistent definition of covered persons, a circumstance that may ultimately lead to the perception or reality of selective enforcement.

Exacerbating these problems is current Rule G-37(d)'s prohibition on persons "directly or indirectly, through or by any other person or means, do[ing] any act which would result in a violation" of the two-year ban on business or prohibition on solicitation or coordination. While it is appropriate to prohibit circumvention of otherwise-constitutional rules that target *quid pro quo* corruption or its appearance, this catchall provision—and the now familiar use of the word "indirectly"—could be read broadly. In practice, it will often be interpreted to reach nearly any behavior that could conceivably be covered by the Rule's already-overbroad provisions, a particularly troubling prospect given the penalties involved. Again: how does one "indirectly" perform an act?[16] This is insufficient tailoring under the First Amendment.

In short, the Draft Amendments attempt to obtain universal coverage by employing terms that are both vague and overbroad. This is an approach to regulation the United States Supreme Court has long decried,[17] and a practice that leaves the present Draft Amendments open to eventual constitutional challenge.

IV. By creating new categories of regulated entities—collectively, the MAP categories—the Draft Amendments make the rule less clear.

The draft rule proposes to add five categories of Municipal Advisor Professionals ("MAP"), which are analogous to the existing categories of Municipal Finance Professionals. While likely a commendable attempt to clarify the scope of the Rule, these new definitions exacerbate rather than reduce constitutional problems. Under the current Rule, it can be difficult to determine what constitutes a sufficient "control" relationship for purposes of establishing vicarious liability when working as or with a Municipal Finance Professional, under one of the five categories. The

---

[15] Draft Rule G-37(c)(i)-(ii).

[16] Similarly, Draft Amended Rule G-37(g)(x) includes those performing these services for "indirect compensation" within the definition of a "municipal advisor third-party solicitor." The lack of a limit to what could constitute such "indirect compensation" is further troubling. Absent guidance on this matter, roughly anything of any subjective value to an individual could be construed as "indirect compensation" by officials seeking to zealously enforce the Rule.

[17] *See, e.g, NAACP v. Button*, 371 U.S. 415, 438 (1963) ("[b]road prophylactic rules in the area of free expression are suspect. Precision of regulation must be the touchstone in an area so closely touching our most precious freedoms") (citing *Near v. Minnesota*, 283 U.S. 697 (1931); *Shelton v. Tucker*, 364 U.S. 479 (1960); *Louisiana ex rel. Gremillion v. NAACP*, 366 U.S. 293 (1961); *Schneider v. Irvington*, 308 U.S. 147, 162 (1939)).

Amendments preserve this imprecision. For example, a triggering contribution may be made, in the case of the Draft Amendments, by any associated person of a municipal advisor who "is a supervisor of any municipal advisor principal up through and including the Chief Executive Officer or similarly situated official"[18] or "is a member of the executive or management committee (or similarly situated official)."[19]

This stands in stark contrast to the organizational and accountability structure of PACs, which both the current and Draft Rule G-37 reference multiple times. An entire regulatory regime has developed solely for the purpose of determining who is legally responsible for a PAC's activity, including its organization,[20] registration,[21] reporting[22], and other obligations. This system exists within a decades-old and comprehensive regime that is continually fine-tuned administratively,[23] legislatively[24] and judicially[25] to ensure that it does, in fact, limit its regulatory scope to activity that is properly tailored to preventing *quid pro quo* corruption. The complexity, specificity, and careful drafting of PAC rules are consistent with the importance of the First Amendment rights that PAC status implicates. Imprecise or overbroad regulation in this context violates the Constitution. Nevertheless, the MAP categories attempt to impose arguably greater burdens, but lack such a structure. What's more, such structure would be insulated from all of the avenues of judicial and administrative review that PACs enjoy.

Finally, the Regulatory Notice asserts that "[t]he regime established by Rule G-37 is widely recognized as having significantly curbed 'pay to play' practices and the appearance of such practices in the municipal securities market."[26] CCP would caution the Board, however, in relying too heavily on this assertion. The evidence on this point is far from conclusive, as the citations in the Regulatory Notice are primarily internal. They do not provide adequate grounds to enact and retain rules that are already constitutionally problematic.

It is also worth noting that, once the MSRB finalizes any rule amendments and submits them to the SEC, the Commission must publish them in the Federal Register for public comment before

---

[18] Draft Rule 37-G(g)(iii)(D).
[19] Draft Rule 37-G(g)(iii)(E).
[20] 52 U.S.C. § 30102 (2014).
[21] 52 U.S.C. § 30103.
[22] 52 U.S.C. § 30104.
[23] *See, e.g.*, Pub. L. 93-443 (codified as amended at 52 U.S.C. § 30106) (Federal Election Commission's enabling statute, noting that "The Commission shall administer, seek to obtain compliance with, and formulate policy with respect to, this Act and chapter 95 and chapter 96 of the Internal Revenue Code…[and] shall have exclusive jurisdiction with respect to the civil enforcement of such provisions.")
[24] *See, e.g.,* Federal Election Campaign Act of 1971 (Pub. L. 92-225) ("FECA"); Bipartisan Campaign Reform Act of 2002 (Pub. L. 107-155).
[25] *See, e.g, Buckley v. Valeo*, 424 U.S. 1 (1976) (invalidating certain FECA provisions, including the scope of its definition of a political committee, under the First Amendment).
[26] Regulatory Notice at 4 (citing "*See* Release No. IA-3043 (Jul. 1, 2010), 75 FR 41018, at 41020, 41026-41027 (Jul. 14, 2010) ('IA Pay to Play Approval Order') (discussing the rationale for adopting the SEC's "pay to play" rule for investment advisers and modeling major components of SEC Rule 206(4)-5 on Rule G-37); *see also id.* at n. 101 and accompanying text.")

they become law.[27] If incorporated into the final rule, the constitutional and practical problems identified in this letter will continue to draw criticism for the reasons just described.

V. The contribution limits are unreasonably low and have no justification.

Virtually all highway fatalities could be eliminated if the speed limit were reduced to 20 mph. Yet few, if any, people would favor such a change. The draft amendments likewise take a radical approach to limiting contributions to certain candidates by barring them altogether. While eliminating political contributions completely in such cases will prevent "pay-to-play" arrangements, they also stifle protected First Amendment activity. Under the Draft Rule, if a covered advisor cannot vote for the covered candidate, no contribution is permitted, not even a dollar.[28]

The proposed rule's $250 contribution limit for officials for whom one can vote, and its ban on contributions for candidates for whom one cannot, is not narrowly tailored.[29] This is clear where the SEC, in 2010, found that a $150 contribution limit for investment advisers who could not vote for the candidate was sufficient to achieve its pay-to-play objectives.[30] The MSRB has provided no explanation as to why the higher SEC limits are insufficient, and CCP remains skeptical that even those limits are constitutional absent a strong evidentiary record on that point.

Moreover, the ban on contributions to candidates for whom one cannot vote is likely unconstitutional: the Supreme Court's 2014 decision in *McCutcheon v. FEC* reiterated the importance of associational rights, which are not limited to associating with candidates in one's own district.[31] The *McCutcheon* ruling would make little sense if bans on out-of-district contributions were constitutional. Similarly, the Supreme Court has never "allowed the exclusion of a class of speakers from the general public dialogue,"[32] which is exactly what the Draft Rule would do.

Even where the covered advisor may vote for the covered candidate, the contribution limit is $250. The same contribution limit would apply whether the candidate is running for office in a city with millions of residents or a town with just a few thousand citizens. A uniform $250 contribution limit covering a wide variety of municipalities evinces no effort to tailor the rule to concerns about corruption. The words of U.S. District Court Judge Beryl Howell, speaking of

---

[27] *See, e.g.*, MUNICIPAL SECURITIES RULEMAKING BOARD, MARKET REGULATION—RULEMAKING PROCESS, http://www.msrb.org/About-MSRB/Programs/Market-Regulation.aspx (last accessed October 1, 2014).

[28] Draft Rule G-37(b)(ii).

[29] *Id.*

[30] 17 C.F.R. 275.206(4)-5(b) (2014).

[31] 134 S. Ct. at 1449 ("To require one person to contribute at lower levels than others … is to impose a special burden on broader participation in the democratic process. And as we have recently admonished, the Government may not penalize an individual for 'robustly exercis[ing]' his First Amendment rights.") (quoting *Davis v. FEC*, 554 U.S. 724, 739 (2008)).

[32] *Citizens United v FEC*, 558 U.S. at 341.

SEC Rule 206(4)-5, are relevant here: "the $350 seems like it came out of thin air."[33] In the absence of a reasoned and empirically sound rationale for the Board's $250 figure, it appears to have been pulled from thin air.

Despite the lack of a record justifying its new contribution limits, the MSRB appears to have substituted its judgment for the more considered deliberations of state legislatures. Most of the states have crafted contribution limits in an attempt to limit corruption or the appearance of corruption. Some states do not limit contributions to candidates. There is no evidence that states without contribution limits are more corrupt than states with such limits. The Board has failed to explain why the campaign finance regulations crafted by state governments for the specific circumstances of each state are nevertheless inadequate to address "pay-to-play" concerns.

VI. The MSRB should consider alternatives to the proposed Draft Amendments.

In the case of *McCutcheon v. FEC*, the Supreme Court ruled that aggregate limits on contributions to candidates are unconstitutional.[34] In the opinion, the Court specifically noted that Congress had failed in its duty to consider any of the available "alternatives" that would also serve the government's interest "while avoiding unnecessary abridgment of First Amendment rights."[35]

There are many possible, and effective, alternatives to the draconian contribution restrictions proposed by the Draft Amendments. There is no evidence that the Board considered these other, less restrictive alternatives.

One possible approach would provide for tougher penalties for those who use pay-to-play arrangements to obtain contracts. Stronger investigative tools to audit suspected pay-to-play activities could focus resources on the bad actors in the system. Whistleblower protections could be written to protect those who report wrongdoing and whistleblowers could also be given rewards based on the size of the ill-gotten contracts or the penalties imposed for violations.

The Board also appears not to have considered alternatives that would provide exemptions from the rule if contracts are put up for bid in a transparent way that forecloses pay-to-play manipulation. Similarly, certain contracting procedures might be imposed, or certain officials may be required to recuse themselves from decisions regarding certain contractors. A contribution limit rule, if retained, should be limited to those circumstances where it is indeed needed, and only after alternative means of preventing pay-to-play practices have been considered.

VII. The MSRB should clearly exempt contributions in support of independent expenditures from the proposed Draft Amendments and current rule.

---

[33] Josh Gerstein, *Judge Mulls SEC Limits on Political Donations*, POLITICO (Sept. 12, 2014), http://www.politico.com/blogs/under-the-radar/2014/09/judge-mulls-sec-limits-on-political-donations-195402.html

[34] 134 S. Ct. at 1462.

[35] *Id.* at 1458 (citation and internal quotation marks omitted).

In adopting Rule 206(4)-5, the SEC explained that "the 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, volunteering, making speeches, and other conduct."[36] This reasoning tracks that of *Citizens United*, where the Court ruled that "independent expenditures do not lead to, or create the appearance of, quid pro quo corruption. In fact, there is only scant evidence that independent expenditures even ingratiate. Ingratiation and access, in any event, are not corruption."[37]

Clearly, the proposed Draft Amendments and current rule must explicitly permit contributions in support of independent expenditures.

* * *

CCP respectfully requests that the Board reconsider these elements of the Draft Amendments, and thanks for Board for the opportunity to comment. Should you have any questions or desire CCP's assistance in modifying the Draft Amendments further, please contact me at 703-894-6800 or adickerson@campaignfreedom.org.

Very truly yours,

Allen Dickerson
Legal Director

[36] Political Contributions by Certain Investment Advisers, 75 Fed. Reg. 41018, 41024 (July 14, 2010).
[37] 558 U.S. at 360 (internal citation omitted).