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Pay-to-Play in New Jersey

An update on state and local requirements

Each year, companies and individuals in New Jersey receive thousands of solicitations for political campaign contributions to countless state, local and federal candidates, political party, political action and legislative leadership committees. Pay-to-play reforms at various levels of state and local government have given business entities pause prior to responding to such solicitations. Thus, business entities have been forced to become well-acquainted with the complicated facets of the state's pay-to-play laws in order not to jeopardize their public-business interests.

New Jersey's pay-to-play requirements just became more restrictive of the ability of business entities to make contributions without jeopardy to obtaining or maintaining public contracts. On Sept. 24, Gov. Jon S. Corzine signed two executive orders intended to further curb the campaign contributions of business entities. These will become effective Saturday.

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THE LAW & MORE

Executive Order 117 extends the state's prohibition on awarding contracts to business entities and their owners who have made contributions. Executive Order 118 represents the state's foray into redevelopment pay-to-play, which restricts a state redevelopment entity from awarding redevelopment agreements to business entities, their associated business entities and each of their owners who have made particular contributions.

In addition to his executive orders, Corzine announced a series of legislative goals that, if enacted, will further restrict the ability of business entities that are awarded public contracts at any level of government and their owners from making political contributions. Thus, the executive orders and legislative proposals have left the state and local pay-to-play laws in a state of flux, making things further confusing for business entities, their owners and employees. To clear up any potential confusion, as of this writing, the state of the law is as follows.

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State contracts

Any business entity that currently holds or intends to enter into a contract with "[t]he state or any of its purchasing agents or agencies or those of its independent authorities" for more than $17,500 must be particularly careful in responding to solicitations for contributions to gubernatorial/lieutenant gubernatorial candidates committees, state, county or municipal political party committees or legislative leadership committees.

Pursuant to N.J.S.A. 19:44A-20.14 and Executive Order 117, business entities that make reportable contributions to such committees would lose their state contracts. Reportable contributions are those in excess of $300 per election (the primary and general elections are treated separately) to a candidate committee or in the case of a political party or legislative leadership committee, those exceeding $300 per calendar year. Such reportable contributions shall not be made:

- Within the 18 months immediately preceding the commencement of negotiations for the public contract;
- During the term of the office of the governor and lieutenant governor, in the case of contributions to a candidate committee or election fund of the holder of that office, or to any state, county or

municipal political party or legislative leadership committee of a political party nominating such governor and lieutenant governor in the last gubernatorial election preceding the commencement of such term; or

- Within the 18 months immediately preceding the last day of the term of the office of governor and lieutenant governor, in which case such prohibition shall continue through the end of the next immediately following term of the office of governor and lieutenant governor, in the case of contributions to a candidate committee or election fund of the holder of that office, or to any state, county or municipal political party or legislative leadership committee of a political party nominating such governor and lieutenant governor in the last gubernatorial election preceding the commencement of the latter term.

Additionally, Executive Order 117 has extended the definition of business entity to include for-profit entities which:

- For corporations, includes the corporation, any officer of the corporation and any person or business entity that owns or controls 10 percent or more of the stock in the corporation;
- For general partnerships, includes the partnership and any partner;
- For professional corporations, includes the professional corporation and any shareholder or officer;
- For limited liability companies, includes the limited liability company and any member;
- For limited liability partnerships, includes the limited liability partnership and any partner;
- For sole proprietorships, includes the proprietor; and
- For any other business entities, includes the entity and any principal, officer, or partner.

The definition of business entity also includes any subsidiaries and political organizations organized under Section 527 of the Internal Revenue Code, that are directly or indirectly controlled by any of the above.

For individuals described in Executive Order 117's definition of business entity, contributions of their spouses or civil union partners, and any children residing with them, will be treated in the same manner as if the individuals themselves made contributions to the relevant entities. Executive Order 117 provides one exception, however, for the contributions of such spouses, civil union partners and children in the event that they contribute to a candidate for whom they are entitled to vote or to a political party committee within whose jurisdiction they reside.

For example, if a spouse of a partner in a general partnership that holds a state contract makes a contribution for more than $300 per calendar year to a municipal political party committee in a jurisdiction other than one where the spouse is entitled to vote, N.J.S.A. 19:44A-20.14, together with Executive Order 117, imputes the spouse's contribution to the general partnership business entity. As a result, the business entity's state contracts would have to be forfeited, unless repayment of the contribution is requested within 30 days pursuant to N.J.S.A. 19:44A-20.20.

Executive Order 118 provides that redevelopers for state redevelopment projects, subsidiaries directly or indirectly controlled by them and business entities (as defined above in this section of the article) hired by the redevelopers to perform professional, consulting or lobbying services with respect to a particular state redevelopment project, shall not make certain contributions after the public issuance of a particular state redevelopment project's request for proposal. Such prohibited contributions would include those to a gubernatorial/lieutenant gubernatorial candidates committee, state, county or municipal political party committees or legislative leadership committees, and contributions to the candidate committees of any state legislator, county or municipal officeholder, in a state legislative district, county or municipality in which the property subject to redevelopment is situated.

Other local unit contracts

The Local Unit Pay-to-Play Law, N.J.S.A. 19:44A-20.4, 20.5, combined with the opportunity for local units to enact their own pay-to-play ordinances creates confusion for business entities. The rules for business entities with local public contracts vary significantly from those with state contracts. Under the Local Unit Law, counties, municipalities and their agencies or instrumentalities may not award any contracts worth more than $17,500 that have not been awarded pursuant to a fair and open process, to a business entity if it or a person who owns more than 10 percent of the business entity makes a reportable contribution to a candidate that is ultimately responsible for the award of the contract or to the candidate's political party, in the one year prior to the award of the contract.

For the purposes of the Local Unit Law, a business entity is "any natural or legal person, business corporation, professional services corporation, limited liability company, partnership, limited partnership, business trust, association or any other legal commercial entity organized under the laws of this state or foreign jurisdiction."

For example, under the Local Unit Law a business entity can be precluded from receiving a municipal contract over $17,500 that is not considered "fair and open," if a person who owns more than 10 percent of the business entity made a general election contribution for more than $300 to the candidate committee of a successful candidate for mayor or that same contribution to the mayor's municipal political party. On the other hand, if the same contract were awarded to the business entity pursuant to a "fair and open" process, no amount in reportable contributions from either the individual owning 10 percent or more or his/her business entity could jeopardize the award of the contract. A contract is considered "fair and open" if it is:

- Publicly advertised in newspapers or on the website maintained by the public entity in sufficient time to give notice in advance of the contract;
- Awarded under a process that provides for public solicitation of proposals or qualifications and awarded and disclosed under criteria established in writing by the public entity prior to the solicitation of proposals or qualifications; and

- Is publicly opened and announced when awarded.

However, the Local Unit Law does not govern local public entities that have established their own rules. N.J.S.A. 40A:11-51 has provided counties, municipalities, independent authorities, boards of education and fire districts with the authority to establish their own pay-to-play ordinances, regulations, policies and resolutions (sometimes hereafter referred to as "ordinances"). Once the local public entity has adopted its own pay-to-play ordinance, it cannot be superseded or pre-empted by the Local Unit Law.

Previously, boards of education were not included among the local public entities required to follow the Local Unit Law. However, recent regulations promulgated by the Commissioner of Education now *require* school boards to have enacted their own pay-to-play policies by Oct. 1.

The terms of the ordinances vary significantly. In some instances, public entities have enacted ordinances that provide a higher contribution threshold than the state law. *See* Township of Franklin Ordinance No. 3405 (2003) (permits business entity contributions up to $400 to candidates for mayor or council and $500 to a Franklin Township political party committee). More frequently, pay-to-play ordinances provide stricter pay-to-play requirements than the Local Unit Law. *See* Township of Holmdel Ordinance 2-79 (2003) (permits only $250 contributions by business entities to candidates for township committee).

Model ordinance

The Citizens Campaign, a self-proclaimed "non-partisan community of citizens devoted to developing and gaining adoption of constructive, common-interest solutions to the problems facing our communities and our state," established a model pay-to-play ordinance in 2001, which has had a significant impact on the pay-to-play landscape. *See* Citizens Campaign, Membership Benefits and Information at www.jointhecampaign.com/membership-benefits-and-application/. The Citizens Campaign claims to have taken part in the drafting of at least 63 ordinances, mostly in Mercer and Monmouth counties.

The Citizens Campaign's model ordinance defines a business entity as: "[A]n individual including the individual's spouse, if any, and any child living at home; person; firm; corporation; professional corporation; partnership; organization; or association. The definition of business entity includes all principals who own 10% or more of the equity in the corporation or business trust, partners, and officers in the aggregate employed by the entity as well as any subsidiaries directly controlled by the business entity."

The model ordinance proposes to eliminate the exception for a fair and open process. As a result, whether or not a business entity is awarded a local public contract pursuant to a fair and open process, a business entity: "[M]ay annually contribute a maximum of $300 each for any purpose to any candidate, for mayor or governing body, or $300 to the (Municipality) party, or $500 to the (County) party committee, or to a PAC referenced in this ordinance, without violating [the ordinance]. However, any group of individuals meeting the definition of 'professional business entity' under [the ordinance], including such principals, partners, and officers of the entity in the aggregate, may not annually contribute for any purpose in excess of $2,500 to all (Municipality) candidates and officeholders with ultimate responsibility for the award of the contract, and all (Municipality) or (County) political parties and PACs referenced in this ordinance combined, without violating [the ordinance]."

It is not entirely clear what the Citizens Campaign, or the local entities that have adopted its ordinance, intended by the term "principals, partners, and officers of the entity in the aggregate." An argument could be made that based upon the Citizens Campaign's definition of business entity, the term "in the aggregate" is designed to combine a business entity's principal, partner and officer ownership interests, which may ultimately aggregate up to more than 10 percent. However, it appears more likely that such language is intended to ensure that the contributions of a business entity and its principals, partners and officers do not, in total, exceed the $2,500 threshold. Whatever the interpretation, business entities seeking local public contracts in these jurisdictions face extraordinary record-keeping burdens for the purposes of tracking both their owners' ownership interests and the political contributions of such owners and officers.

Cross jurisdictions

As a result of the adoption of ordinances at various levels of local government, a business entity's political contribution to a committee in one jurisdiction could unknowingly raise pay-to-play concerns in another. For example, in the Borough of Highland Park, any business entity contributing more than $500 to a Middlesex County political party committee and any political action committees are precluded from eligibility for a public contract.

A number of public entities recently enacted redevelopment pay-to-play ordinances. These are designed to stop redevelopers (which by definition generally include their professionals, consultants and lobbyists) contracted for a particular project from receiving local redevelopment contracts if they have made local political contributions. The Citizens Campaign also has drafted a model ordinance in this respect, which has been adopted by 18 public entities.

N.J.S.A. 40A:11-51.1.c requires that upon adoption, all local pay-to-play ordinances be filed with the secretary of state's office. Problem is, only 112 have been filed. *See* www.state.nj.us/state/secretary/ordinance.html. Our experience suggests there are far more because we have encountered a significant number of ordinances that have not been filed with the secretary of state. So how are contributors expected to know whether a particular pay-to-play restriction exists before they write a check? They're not.

An issue exists as to whether the language of N.J.S.A. 40A:11-51 means no ordinance can become effective unless it has been filed with the secretary of state's office. The state Department of Community Affairs, Division of Local Government Services rejects that notion.

Whatever the legal impact of a local public entity's failure to file its pay-to-play ordinance, when a local public entity has not filed with the secretary of state's office, the ordinances can be difficult to locate. Many local pay-to-play ordinances are not available online. However, our

experience is that many of these ordinances are even difficult to attain upon a telephone call to the responsible employee's office for the local public entity (i.e., clerk's office). On certain occasions, we have found that local employees were not aware of a local pay-to-play ordinance, even when one was in effect. At other times, we have been told that access to a local pay-to-play ordinance would be granted only if we were to submit a request pursuant to the Open Public Records Act.

Disclosure obligations

Business entities seeking public contracts also face a series of disclosure obligations. State contracts require that business entities certify they have not made a contribution that would bar the award of a state contract. This is required to be submitted by a business entity prior to the award of the contract.

Pursuant to Executive Order 118, a state redeveloper must provide a certification that it has not made a contribution that would bar the award of the redevelopment agreement, prior to entry into a state redevelopment contract.

At least 10 days prior to the award of a non-fair and open contract having an anticipated value in excess of $17,500 by a local public entity, a business entity is required to submit what is known as a Chapter 271 Political Contribution Disclosure Form (PCD form). This form requires the disclosure of designated reportable contributions by the business entity and its principals, partners, officers or directors and their spouses, and any subsidiaries or political organizations organized under Section 527 of the Internal Revenue Code directly or indirectly controlled by the business entity.

Recent regulations promulgated by the commissioner of education require that all business entities contracting with school boards submit a PCD form whether or not the contract was awarded under a fair and open process. Additionally, some local ordinances require the submission of additional disclosure forms of its contracting business entities.

Finally, all business entities that have received more than $50,000 in public contracts in the aggregate in a calendar year are required to electronically submit the business entity annual statement to the Election Law Enforcement Commission by March 30 of the following calendar year. This form requires a summary of each qualifying business entities' public contracts and similarly requires a listing of the reportable political contributions made by the business entity and its principals, partners, officers, or directors and their spouses, and any subsidiaries or political organizations organized under Section 527 of the Internal Revenue Code directly or indirectly controlled by the business entity.

A most confusing component of the pay-to-play laws in New Jersey can be found in their inconsistency. Prior to making a political contribution here, business entities must be sure they have complied with a wide range of laws, regulations, ordinances and resolutions at various levels of government. According to Corzine's remarks upon signing of Executive Orders 117 and 118, additional pay-to-play reforms will be initiated by the legislature. Such reform undoubtedly will enable the play-to-play laws to apply more uniformly statewide.

The act of making a political contribution is a form of constitutionally protected speech. *Buckley v. Valeo*, 424 U.S. 1. However, should business entities with public contracts choose to exercise this right, their business interests depend on how closely they monitor their compliance with the wide range of pay-to-play requirements. Business entities should take steps to ensure compliance with the law through the establishment of internal controls that are specifically designed to account for the public business interests of each business entity. Failure by business entities to do so will jeopardize their public contracts.

Suggestions for compliance

- Keep tabs on numbers of shares owned by shareholders and make sure the contributions of all those who owned more than 10 percent are closely monitored.
- Establish procedures for reporting and monitoring the political contributions of the business entity and its principals, partners, officers or directors, their spouses and children living at home, and any subsidiaries or political organizations organized under Section 527 of the Internal Revenue Code directly or indirectly controlled by the business entity.
- Maintain records ensuring that all such contributions comply with state and local law, and are identified when filing the Chapter 271 Political Contribution Disclosure Forms with all appropriate public entities and the business entity annual statement with the Election Law Enforcement Commission.
- Maintain an ongoing list of business entity contributions, the name and type of entity (candidate committee, political party committee, continuing political committee) to which the contribution has been made.
- Do not make *any* contributions at the county, municipal or school board level unless you have first received a copy of the local pay-to-play ordinance, regulation, policy or resolution, if any.
- Establish standard language that should be submitted with each contribution specifically stating the entity receiving the political contribution does not have permission "wheel" the contribution to another entity.