



FEDERAL ELECTION COMMISSION **May 12 4 42 PM '94**
WASHINGTON, D.C. 20463

AGENDA ITEM
For Meeting of: MAY 19, 1994

May 12, 1994

MEMORANDUM

TO: The Commission

THROUGH: John C. Surina
Staff Director *[Signature]*

FROM: Lawrence M. Noble *[Signature]*
General Counsel

N. Bradley Litchfield *[Signature]*
Associate General Counsel

Jonathan M. Levin *[Signature]*
Senior Attorney

SUBJECT: Draft AO 1994-9

Attached is a proposed draft of the subject advisory opinion.

We request that this draft be placed on the agenda for May 19, 1994.

Attachment

ADVISORY OPINION 1994-9

Grant S. Cowan
Frost & Jacobs
201 East Fifth Street
P.O. Box 5715
Cincinnati, OH 45201-5715

DRAFT

Dear Mr. Cowan:

0 This responds to your letter dated March 18, 1994,
1 requesting an advisory opinion on behalf of Armco Steel
2 Company, L.P. ("ArMLP") concerning application of the Federal
3 Election Campaign Act of 1971, as amended ("the Act") and
4 Commission regulations to the effect of a business
5 reorganization on the affiliated status of various entities.

6 ArMLP is a Delaware limited partnership formed in May
7 1989 as a joint venture between Armco, Inc. ("Armco") and
8 Kawasaki Steel Corporation, a Japanese corporation
9 ("Kawasaki"). (Kawasaki operates through Kawasaki Steel
0 Investments, an indirect wholly owned U.S. subsidiary.)
1 Armco and Kawasaki each own a 49.5 percent limited
2 partnership interest in ArMLP. AK Management is the general
3 partner in ArMLP and owns a one percent interest in it. AK
4 Management is jointly owned (50/50) by AJV Investments, Inc.
5 and KSCA Inc., both Delaware corporations. AJV is a wholly
6 owned subsidiary of Armco, and KSCA is an indirect wholly
7 owned subsidiary of Kawasaki.

8 ArMLP intends to undergo a reorganization under which it
9 will become AK Steel Corporation ("AK Steel"), a Delaware
0 corporation and a wholly-owned subsidiary of another Delaware
corporation, AK Steel Holding Corporation ("AK Holding").

The reorganization will occur as follows: (1) Armco and Kawasaki will contribute their limited partnership interests in ArmLP to AK Holding. (2) AJV Investments and KSCA Inc. will each give their stock in AK Management to AK Holding. (3) AK Holding will transfer its limited partnership interest in ArmLP to AK Steel. (4) AK Holding will transfer its stock in AK Management to AK Steel.

As a result, AK Steel will be the sole partner of ArmLP, and as such, the partnership will dissolve by law. AK Steel will own all the assets of the former ArmLP and all of ArmLP's employees will become the employees of AK Steel. Thus, through a transfer of stock and partnership interests to AK Steel, ArmLP will become a corporation, AK Steel.

Immediately after the reorganization, AK Steel will engage in a recapitalization of the company. This entails the issuance of 19,504,310 shares of its common stock to the public through an initial public offering ("IPO"). It also entails the issuance of over one million shares to Armco and over five million shares to Kawasaki. Over 70,000 shares are being issued to Thomas Graham, the Chairman and CEO of AK Holding as part of his bonus. As a result, Kawasaki and Armco will hold approximately 20 percent and four percent of the common stock respectively.

Armco has maintained a non-Federal political action committee named the Armco Better Citizenship Committee ("ABC-PAC") to which ArmLP employees have contributed in the past through a payroll deduction plan. ArmLP has a Kentucky

non-Federal PAC named the Kentucky Armco Steel Company L.P. Better Citizenship Voluntary PAC ("ArmlP Kentucky PAC"). Prior to the reorganization, ArmlP intends to establish a Federal PAC with the name "Armco L.P. Federal PAC" ("ArmlP Federal PAC"). ABC-PAC and ArmlP Kentucky PAC will then act as collecting agents and will each transfer their funds to ArmlP Federal PAC after first obtaining the written authorization of the employee contributors. Immediately after the corporate reorganization, AK Steel will file an amended Statement of Organization reflecting the change in the name of the connected organization of the new Federal PAC.

ArmlP requests an advisory opinion as to whether the transfer of funds may be made from the two non-Federal PACs to ArmlP Federal PAC and whether the use of the non-Federal PACs as collecting agents will obligate them to register as political committees. You also request an opinion regarding the change in the name of the "connected organization" and the name of the PAC. You wish to ascertain that the ArmlP Federal PAC "will be treated as the PAC of AK Steel after the reorganization."

In addition, Armco LP requests an advisory opinion as to whether AK Steel PAC will be deemed as affiliated with the Federal committees of Armco, Inc.^{1/} You also ask whether AK

^{1/} Since April 13, 1978, Armco Employees' PAC has been registered with the Commission as the separate segregated fund of Armco, Inc.

Steel PAC would be affiliated with the separate segregated fund of any domestic subsidiary of Kawasaki, if such a fund were established.

In connection with this question, you note that none of the officers or employees of AK Holding or AK Steel will be employees or employees of Armco or the Kawasaki companies. You state that it is anticipated that neither the Articles of Incorporation nor the By-Laws of AK Steel and AK Holding will enable either Armco or Kawasaki to participate in the governance of AK Steel or AK Holding, and that the governance and management of AK Steel and AK Holding will be separate and independent from Armco and Kawasaki. Certain contracts and agreements with the two former parents will continue for AK Steel and Holding after recapitalization such as ArmLP's obligation to indemnify them for losses and liabilities relating to ArmLP's management, ownership and operation. Other arrangements, such as Armco's obligation to indemnify ArmLP for unemployment benefits up to \$20 million, and certain other costs, will terminate. The companies owning the partnership have signed a Joint Venture Termination Agreement, terminating obligations among the partners and stating what obligations still exist.

It is anticipated that the shares of AK Holding will be traded vigorously on the open market, leading to large numbers of different shareholders, and that no single group of shareholders will hold a controlling interest in AK Holding.

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The directors of Armlp include Thomas C. Graham, who is the President and CEO of Armlp, James F. Will, who is the Chairman of Armlp and President, CEO, and Director of Armco, and Kaiji Emoto, a Managing Director of Kawasaki. The other four directors of Armlp include an Assistant to the President of Armco, a Corporate Vice President and Chief Financial Officer of Armco, a Managing Director of Kawasaki, and a Senior Managing Director of Kawasaki. This also will be the first board of AK Steel. (Mr. Graham will become Chairman, as well as CEO.) Messrs. Graham, Will, and Emoto will constitute the board of AK Holding. Prior to the completion of the recapitalization, the other four directors named above will resign from AK Steel's board, and the three remaining directors will choose four "additional independent members" to be added to the boards of AK Holding and AK Steel by Messrs. Graham, Will, and Emoto. In addition, AK Holding and Kawasaki are negotiating an agreement under which, for so long as Kawasaki owns an agreed upon minimum percentage (15 percent) of the outstanding shares of Common Stock, AK Holding will take all action necessary to nominate and support the nomination of one person designated by Kawasaki for election as Director of AK Holding (presently Mr. Emoto) and to solicit proxies in favor of the election of that

person.^{2/} Finally, according to the prospectus, three of the seven executive officers of both AK Holding and AK Steel, all of whom are holdovers from Armlp, had been employees of Armco before working for the partnership.

Responses to Questions Posed

To a large extent, responses to your questions depend upon an analysis of the affiliated relationship or lack thereof among the business entities. The Act and Commission regulations provide that committees, including separate segregated funds, that are established, financed, maintained or controlled by the same corporation, person, or group of persons, including any parent, subsidiary, branch, division, department, or local unit thereof, are affiliated. Contributions made to or by such committees shall be considered to have been made to or by a single committee. 2 U.S.C. §441a(a)(5); 11 CFR 100.5(g)(2), 110.3(a)(1), and 110.3(a)(1)(ii). In addition, a corporation may make partisan communications to and solicit the restricted class (i.e., executive and administrative personnel and stockholders, and the families thereof) of its subsidiaries for contributions to the corporation's separate segregated fund. 2 U.S.C. §441b(b)(2)(A) and (4)(A)(i); 11 CFR

^{2/} According to the Prospectus for the IPO, Kawasaki (with respect to some of its shares), Armco, Inc., and Mr. Graham have agreed not to sell any of their shares for a period of 180 days after the offering without the prior written consent of a representative of the U.S. Underwriters and a representative of the Managers. With respect to most of its shares, Kawasaki has made a similar promise to those representatives covering a year-long period.

114.3(a)(1) and 114.5(g)(1). See Advisory Opinion 1993-18.

Where an entity is not an acknowledged subsidiary of another entity, as in 11 CFR 110.3(a)(2)(i), Commission regulations provide for an examination of various factors in the context of an overall relationship to determine whether one company is an affiliate of another and, hence, whether their respective SSFs are affiliated with each other. 11 CFR 100.5(g)(4)(i) and (ii)(A)-(J), and 110.3(a)(3)(i) and (ii)(A)-(J). The relevant factors in the situation you have presented are as follows: (A) the ownership by one sponsoring organization of a controlling interest in the voting stock or securities of another sponsoring organization; (B) the authority or ability of one sponsoring organization to participate in the governance of another sponsoring organization through provisions of constitutions, by-laws, contracts or other rules, or through formal or informal practices or procedures; (C) the authority or ability to hire, demote or otherwise control the decisionmakers of another sponsoring organization; (E) common or overlapping officers or employees, indicating a formal or ongoing relationship between the sponsoring organizations; (F) members, officers, or employees of one sponsoring organization who were members, officers, or employees of another organization which indicates a formal or ongoing relationship or the creation of a successor entity; and (I) an active or significant role by one sponsoring organization in the formation of another. 11 CFR 110.3(a)(3)(ii)(A), (B),

(C), (E), (F), and (I).

A. Transfer of Funds from the Non-Federal PACs to ArMLP PAC

You have inquired as to ArMLP PAC's ability to receive funds transferred from two non-Federal PACs without the consequence of those PACs becoming political committees. In Advisory Opinion 1984-31, the Commission considered a request pertaining to the transfer of funds from a corporation's state committee to its Federal SSF. The Commission noted that, because the Federal PAC was already in existence, the state PAC could act as a collecting agent under 11 CFR 102.6(b) and (c) and make the transfer without having to register and report. In order to make such a transfer, however, the state PAC was required to obtain written authorization from the contributors whose contributions comprised the funds transferred stating their intent to make a contribution to the Federal SSF under the regulations at 11 CFR 102.6(b) and (c) and 114.5. The contributions of any contributors who did not state this were to be retained by the State PAC. Each contribution included in the transfer was to be reported by the Federal SSF as a contribution from the original contributor. 11 CFR 102.6(c)(7). In reaching this conclusion, the Commission assumed that the funds transferred were permissible under the Act.

The differences between the situation presented in Advisory Opinion 1984-31 and the situation presented by you is that one of the state PACs (ABC-PAC) is not the state PAC of the business entity itself and that the Federal PAC of

Armlp is not, strictly speaking, the SSF of a corporation. Commission regulations provide, however, that a collecting agent may be a committee, whether or not it is a political committee as defined in 11 CFR 100.5, that is affiliated with the separate segregated fund. 11 CFR 102.6(b)(1)(i). In analyzing the affiliated status of Armlp with Armco and Kawasaki, as well as the control of the joint venture partnership by two corporations, the Commission concludes that the situation in Advisory Opinion 1984-31 is analogous. See Advisory Opinion 1992-17.

From the information presented by you, it appears that Armlp is affiliated with each of its parents. Although neither Armco nor Kawasaki appear to have a controlling interest that overrides the other, they each own half of the limited partnership interest and half of the general partner, AK Management.^{3/} See 11 CFR 110.3(a)(3)(ii)(A). See Advisory Opinions 1992-17 and 1987-34. Compare Advisory Opinion 1984-36. As fifty percent owners of the general partner, they share equally the power to participate in the governance of Armlp. This is indicated by the presence on Armlp's Board of Directors of Armco's President and CEO and two other Armco officers and of three managing directors of Kawasaki (with the seventh director, Mr. Graham, presumably chosen by Armco and Kawasaki or their representatives on the Board). See 11

^{3/} In a limited partnership, the general partners are the managers of the business, as well as liable for partnership debts beyond their contribution. Black's Law Dictionary 928, 1121 (6th ed. 1990).

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4 CFR 110.3(a)(3)(ii)(B), (C), and (E). See Advisory Opinions
5 1992-17 and 1987-34. In addition, the prospectus material
6 sent by you indicates that the partnership is the successor
7 to the Eastern Steel Division of Armco. 11 CFR
8 110.3(a)(3)(ii)(I). Thus, ABC-PAC, Armco's state PAC, would
9 be affiliated with Armco L.P. PAC.^{4/}

10 The Commission notes that the standard for collecting
11 agent at 11 CFR 102.6(b)(1)(i) refers to affiliation with the
12 separate segregated fund. The Act does not extend to a
13 partnership the ability granted to a corporation at 2 U.S.C.
14 §441b(b)(2)(C) to conduct itself as a connected organization
15 and benefit from the exemption for establishment,
16 administration, and solicitation costs. Advisory Opinions
17 1990-20 and 1982-63, See California Medical Association v.
18 Federal Election Commission, 453 U.S. 182 (1981).

19 Nevertheless, the Commission has treated a joint venture
20 partnership of corporations differently as a result of its
21 relationship with corporations that could pay the exempt
22 costs for the partnership PAC. The Commission has permitted
23 a partnership consisting of two corporate partners with which
24 it was affiliated to pay the establishment, administration,
25 and solicitation costs of the partnership PAC without a
26 partnership contribution resulting. (The general rule, as
27 stated in that opinion, applies to a partnership owned

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29 ^{4/} The Commission has long held that affiliates may include
30 entities other than corporations. Advisory Opinions 1992-17,
1989-8, 1987-34, and 1983-48.

entirely by corporations and affiliated with at least one of those corporations.) Thus, the partnership PAC could function as a separate segregated fund. Advisory Opinion 1992-17. See also Advisory Opinion 1987-34. Similarly, ArmlP PAC may function, in effect, as a separate segregated fund.^{5/}

Based on the foregoing, ABC-PAC, as well as Armco L.P. Kentucky PAC, may act as collecting agents and transfer funds from each PAC to ArmlP PAC. This must be done in accordance with the requirements set in Advisory Opinion 1984-31. In addition to the notice requirements, particular attention must be paid to the requirements of 11 CFR 104.12, i.e., the assumption that the cash-on-hand balance is composed of the contributions most recently received by the transferring state PACs and the exclusion of funds not permissible under the limitations and prohibitions of the Act. See Advisory

^{5/} In the event that ArmlP PAC functions as a separate segregated fund, it will have to identify a connected organization on its statement of organization. 2 U.S.C. §433(b)(2). Commission regulations provide that a connected organization may be a corporation which directly or indirectly establishes, administers, or financially supports a political committee but makes no provision for a partnership in that role. 11 CFR 100.6(a). Therefore, if support is provided directly by the affiliated corporations, Armco and Kawasaki Steel Investments along with KSCA (Kawasaki's domestic subsidiaries), or indirectly by the corporations by virtue of support from ArmlP, ArmlP PAC must amend its statement of organization by identifying the two corporations as its connected organizations. Advisory Opinion 1992-17.

Opinion 1990-16.^{6/}

B. Affiliation After Recapitalization

The presence or absence of affiliation between AK Holding and Armco and between AK Holding and Kawasaki after the IPO depends upon application of the factors described above.

After the IPO, neither Armco nor Kawasaki will come close to owning a controlling interest in the outstanding common shares. In addition, you anticipate that AK Holding shares will be vigorously traded on the open market and no single group of shareholders will hold a controlling interest. See 11 CFR 110.3(a)(3)(ii)(A).

In assessing the next five factors cited above as relevant, the disaffiliation of Kawasaki and Armco becomes problematic. You state that you anticipate that the governing documents will enable neither Armco, Inc. nor Kawasaki to engage in the governance of AK Steel and AK Holding and that the governance and management of AK Steel

^{6/} You should note that in Advisory Opinion 1984-31, the Commission requires compliance with the solicitation provisions of 11 CFR 114.5 and the opinion addresses contributions from members of the restricted class of solicitees. See 11 CFR 114.5(g)(1) and 114.1(c) and (h). Furthermore, to solicit outside the restricted class requires additional safeguards not presented in your request. See 11 CFR 114.6(c) and (d). Your requests for authorization from (i.e., solicitation of) each contributor, therefore, should not extend to those contributors not in the restricted class, e.g., non-executive and non-administrative employees, and employees of a company not affiliated with Armco L.P. You should note that the determination of which contributions are represented in the cash on hand must include all of the recent contributions, not just those from contributors in the restricted class.

and AK Holding will be independent and separate from the former joint venturers. There is also a Joint Venture Termination Agreement terminating obligations and continuing others. See 11 CFR 110.3(a)(3)(ii)(B), (C), and (E).

Significantly, however, the boards of both AK Holding and AK Steel each contain a high-ranking director or executive from Armco and from Kawasaki. Sitting on both boards will be the President and CEO of Armco (Mr. Will) and a Managing Director of Kawasaki (Mr. Emoto). In addition, Kawasaki's position on the board is, in effect, an obligation of AK Holding for the near future. It is also significant that the directors from Armco and Kawasaki are two of the three persons choosing the new members of both boards.

Relevant to factor (F), which pertains to former officer and employees of one sponsoring organization who were officers or employees with another, is the presence of three former Armco employees among the seven executive officers, all of whom are also holdovers from ArmLP. See 11 CFR 110.3(a)(3)(ii)(F). The Commission also notes that Armco and Kawasaki were instrumental in the formation of the Armco LP joint venture partnership, the predecessor organization. See 11 CFR 110.3(a)(3)(ii)(I).

The Commission has addressed possible disaffiliation situations in prior opinions. Most recently, in Advisory Opinion 1993-23, the Commission addressed a situation where the parent spun off its remaining shares in its subsidiary to the parent's shareholders, after offering one-eighth of its

4 shares in the subsidiary to the public. The Commission
5 concluded that the former parent and former subsidiary would
6 be disaffiliated. The Commission relied partially on the
7 Separation Agreement between the parent and subsidiary and
8 considered it to prevail over the presence of some of the
9 factors set out at 11 CFR 110.3(a)(3)(ii). The Commission,
10 in distinguishing the situation in Advisory Opinion 1993-23
11 from similar previous corporate spin-offs where the
12 Commission declined to disaffiliate, noted, however, that, in
13 Advisory Opinion 1993-23, there would be a complete
14 separation of the former subsidiary's group of directors,
15 officers, and employees from that of the former parent. See
16 Advisory Opinions 1987-21 and 1986-42.

17 In view of the background presented as to the
18 relationships of the companies, the continued presence on the
19 boards of AK Holding and AK Steel of the high-ranking
20 officials of Armco and Kawasaki leads the Commission to
21 conclude that the disaffiliation of AK Steel and AK Holding
22 from those two companies would be premature at this time.
23 This does not preclude a different conclusion at a later
24 point in the operations of AK Steel and AK Holding.^{7/}

25 C. Change in the Name of the Connected Organization and the

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27 ^{7/} The Commission notes that Kawasaki's interest in AK
28 Holding raises the question of foreign national involvement
29 in the solicitation and making of contributions with respect
30 to Federal and non-Federal elections. See 2 U.S.C. §441e; 11
CFR 110.4(a). Because you did not raise this issue, the
Commission will not analyze it. The Commission, however,
refers you to Advisory Opinion 1992-16 and opinions cited
therein.

PAC

The Act and regulations require that the name of any separate segregated fund established by a corporation includes the full name of the connected organization. 2 U.S.C. §432(e)(5); 11 CFR 102.14(c). The facts presented by you indicate that AK Steel is the successor organization to ArmlP. In addition, ArmlP PAC was not only acting as a PAC "sponsored" by a partnership, but could act as a separate segregated fund. (See analysis above.) After the reorganization, what will then be the former Armco L.P. PAC may be treated as the PAC of AK Steel. If this is done, the PAC name must include the name of AK Steel in its PAC name, assuming that AK Steel is acting as its connected organization. See Advisory Opinions 1993-7, 1986-42, and 1980-98.^{8/}

This response constitutes an advisory opinion concerning application of the Act, or regulations prescribed by the Commission, to the specific transaction or activity set forth in your request. See 2 U.S.C. §437f.

For the Commission,

Trevor Potter
Chairman

Enclosures (AOs 1993-23, 1993-7, 1992-17, 1992-16, 1990-20, 1990-16, 1989-8, 1987-34, 1987-21, 1986-42, 1984-36, 1984-31, 1983-48, 1982-63, and 1980-98)

^{8/} The Commission notes that AK Holding is the parent of AK Steel. There is nothing in the Act precluding a connected organization from including the parent's name in the name of the SSF. Advisory Opinion 1989-8.