



FEDERAL ELECTION COMMISSION
Washington, DC 20463

March 24, 1995

CERTIFIED MAIL,
RETURN RECEIPT REQUESTED

ADVISORY OPINION 1994-36

Susan M. Frank, Corporate Counsel
Science Applications International Corporation
10260 Campus Point Drive
San Diego, California 92121-1578

Dear Ms. Frank:

This refers to your letters of March 9, February 28, February 13, January 23, January 11, 1995, and November 17, 1994, on behalf of a separate segregated fund ("the Committee") to be established by Science Applications International Corporation ("SAIC"). Your request concerns the application of the Federal Election Campaign Act of 1971, as amended ("the Act"), to SAIC's proposed solicitation for political contributions on behalf of the Committee.

You state that SAIC is in the process of establishing the Committee and wishes to solicit contributions from employees who are direct or beneficial stockholders of SAIC. You note that Commission regulations permit a corporation to solicit its stockholders and their families on an unlimited basis, as well as its executive and administrative personnel, as further defined by Commission regulations. SAIC, which you describe as the largest U.S. employee-owned high technology company, has approximately 15,300 current employees (out of a total of 17,000) who are direct or beneficial owners of SAIC stock.^{1/} You indicate that many of these individuals would not qualify as executive or administrative personnel under Commission regulations. Therefore, SAIC seeks Commission guidance as to whether these employees could be solicited for contributions to the Committee in their capacity as stockholders.

THE PLANS

The materials included in your request detail various methods by which SAIC employees can obtain SAIC stock. As discussed more fully below, several plans allow for direct purchase of stock, while others allow for beneficial ownership through participation in SAIC retirement programs.

Direct purchase of SAIC stock

SAIC stock is not traded on any exchange, instead it is formally traded four times a year in an internal market.^{2/} Your materials indicate that the purchase price of SAIC stock is calculated according to a formula that takes into account various factors such as SAIC net income, objective market factors and shareholder equity.

During the time of the internal market, approved employees can purchase stock up to pre-approved limits from approved sellers or other stockholders. Employees can further acquire stock through performance awards of stock or stock options. Your materials indicate that the easiest way for an employee to purchase stock is through SAIC's Employee Stock Purchase Plan ("ESPP"). Under this plan, a portion of an employee's after tax salary is held in an account by a trustee and used to purchase stock during the four times a year that SAIC stock is traded.

The employees who purchase SAIC stock directly may vote the stock as they wish, have an immediate right of ownership, and would have the right to receive dividends, if dividends were declared. There are, however, certain restrictions on SAIC stock which stem from its status as an employee-owned corporation. The first is SAIC's right to repurchase its stock. A stockholder who is no longer affiliated with SAIC must give SAIC the opportunity to repurchase the stock at its current valuation. A second restriction is SAIC's right of first refusal. This applies if a stockholder wishes to sell stock outside the internal market, in which case, the stockholder must first give SAIC a chance to purchase the stock at the offered price. Even if SAIC chooses not to exercise the right of first refusal, SAIC must give written approval of any sale of stock outside the internal market and may put restrictions on the sale.^{3/}

Beneficial ownership of SAIC stock

Beneficial ownership of SAIC stock is gained through four basic retirement plans: the Cash or Deferred Account ("CODA"), the Employee Stock Ownership Plan ("ESOP"), and the Profit Sharing Retirement Plan I and II ("Profit Sharing I and II").^{4/}

CODA

SAIC's CODA is a voluntary 401(k) retirement plan. It is funded by an employee's contributions, the limit of which is determined by IRS regulations, and a maximum 10% match by SAIC. An employee's right to the employee's CODA contributions is fully vested at all times. An employee's right to the company match account vests at 25% per year starting with the third year of employment, with full vestment after six years of service. At the employee's option, employee contributions may be invested in several different investment funds which include U.S. Government bonds or non-SAIC corporate stock. The employee may also chose to have the employee contribution placed in SAIC stock. The company's matching contribution to CODA, however, is currently invested in SAIC stock. By directing the SAIC trustee of CODA accounts, an employee owning stock through CODA may vote the stock as that employee wishes.

An employee gains access to funds in a CODA account upon reaching the age of 59 1/2 or upon termination of employment with SAIC. Hardship withdrawals are also permitted for situations involving emergency circumstances, heavy financial need for medical reasons, purchase of a residence, tuition needs or to prevent eviction from the employee's residence. However, if hardship withdrawals are made, SAIC would suspend the employee's right to make contributions to the plan for one year. Payment from the CODA account is made in cash.

ESOP

The terms of SAIC's ESOP plan are similar to the CODA with the following differences. The company's ESOP contributions are invested principally in SAIC stock. Unlike CODA, participating employees do not make contributions into the plan. Finally, prior to reaching age 62, participants in ESOP are not permitted to make any withdrawals until they either retire or end their employment with the company. Employees reaching age 62 are permitted to make a one time in-service withdrawal from their vested plan accounts prior to actual retirement. ESOP does not otherwise permit a hardship withdrawal. At the employee's option, payment from an ESOP account can be either in cash or in SAIC stock.

Profit Sharing I and II

Again, the terms of Profit Sharing I and II are similar to CODA with regards to vesting and the choice of investments available. Profit Sharing II was developed in 1992; however, a sizable number of SAIC employees are still enrolled in the earlier plan. A major difference between the two plans is that Profit Sharing I, until 1987, allowed for employees to make voluntary contributions into voluntary profit sharing accounts. These funds could then be used to invest in the various options available under both plans, including the option to invest in SAIC stock. Funds invested in the voluntary accounts of Profit Sharing I could be withdrawn by employees at any time with no restrictions.⁵⁷ By contrast, Profit Sharing II, like ESOP, is funded entirely by SAIC contributions. As with ESOP, participants may not withdraw funds from their plan accounts until they either terminate their employment with SAIC or reach age 62. At age 62 they have the same in-service withdrawal rights held by participants in ESOP. Payments from Profit Sharing I and Profit Sharing II account, as with CODA account payments, are made in cash.

The Act and Commission Regulations

The Act permits a corporation or its separate segregated fund to solicit its individual stockholders and their families. 2 U.S.C. 441b(b)(4)(A)(i). Under the Commission regulations, a stockholder is defined as a person who (i) has a vested beneficial interest in stock; (ii) has the power to direct how that stock shall be voted (if it is voting stock); and (iii) has the right to receive dividends. 11 CFR 114.1(h); see also Advisory Opinions 1994-27, 1988-36, 1988-19, 1984-5, 1983-35 and 1983-17.

The solicitation of SAIC stockholders

Direct stockholders

From the materials provided in your request, it appears that direct stockholders of SAIC would meet the requirements of section 114.1(h). Again, employees purchasing stock directly from SAIC would have an immediate ownership of and, hence, a vested interest in the stock. They also have the right to vote the stock they own. SAIC stock also carries the right to receive dividends. Therefore, the requirements of section 114.1(h) are met.^{6/}

The Commission notes the various restrictions such as the right of repurchase and first refusal regarding the purchase and selling of SAIC stock. As your request states, these restrictions arise from the need of an employee-owned company to maintain a closed internal market. The Commission has not previously addressed the solicitation of employee stockholders in employee-owned companies.^{7/} However, the Commission notes that none of the restrictions described in your request amount to a forfeiture of the stock since, when stock is resold to or repurchased by SAIC, the price obtained would be the current price. Therefore, the Commission concludes that these restrictions do not interfere with the requirements of section 114.1(h) and direct SAIC stockholders are stockholders for purposes of the Act.

Beneficial Share Holders

The situation regarding employees holding SAIC stock as beneficial owners is more complex. Any employee enrolled for the third year in SAIC's CODA, ESOP or Profit Sharing I or II plan would meet the first requirement to the extent that the 25% vested value for that year would cover at least one share of stock beneficially held for that employee. The information contained in your request states that each employee who acquires SAIC stock through any of the four plans has the right to give voting instructions and that the trustee must comply with those instructions. Therefore, the second requirement of the regulations is met.

In past treatments of employee stock purchase plans, the third requirement--the right to receive dividends--is the element that has received the most intense scrutiny and analysis. Most of the plans discussed in the past have contained some limitations regarding the withdrawal of either the accumulated dividends or the underlying stock. See Advisory Opinion 1994-27 and the opinions cited therein. As stated in your request, SAIC policy is not to declare dividends. As noted in footnote 6, this policy does not, by itself, interfere with the requirements of section 114.1(h). A more important consideration are the limitations placed by the various plans on the right to withdraw funds from plan accounts, if dividends were declared. The test that the Commission has used is whether "participants are able to withdraw at least one share of stock...without incurring a suspension period..." to conclude that those participants had the right to receive dividends and were stockholders under 11 CFR 114.1(h). See Advisory Opinion 1994-27 and the opinions cited therein.

If an employee has already withdrawn stock which formed part of an investment in the various retirement plans, that employee would have the right to receive dividends in the same manner as any other SAIC stockholder and so would be considered as a stockholder for purposes of the Act and the Commission regulations. As in the past opinions, the remaining issue is whether, absent any actual withdrawal of stock, any vested plan participant may qualify as a stockholder under section 114.1(h).

Participants in Profit Sharing II and ESOP may not access their funds prior to leaving employment with SAIC or reaching retirement age. Participants in CODA are similarly restricted except that prior to retirement or reaching retirement age they may withdraw funds from their accounts for hardship purposes.^{8/} Because of these restrictive withdrawal rights, participants in CODA, Profit Sharing II and ESOP, prior to retirement or reaching retirement age, would not qualify as stockholders under the Commission regulations. Since upon reaching retirement age, participants in CODA, Profit Sharing II and ESOP may access their funds, but without some of the more onerous restrictions discussed in Advisory Opinion 1994-27, this class of participants would also qualify as shareholders.^{9/}

As with Profit Sharing II, most employee participants in Profit Sharing I would also not qualify as stockholders. However, a number of participants (besides those reaching retirement age) in the earlier profit sharing plan would qualify. Those participants who, with their remaining voluntary accounts, choose the option of investing those funds in SAIC stock would qualify as stockholders since they could access their funds without restrictions.

Accordingly, with respect to stockholder solicitations for contributions to SAIC's separate segregated fund, the Commission concludes that the Committee (or SAIC) may solicit political contributions from employees who are direct stockholders. With regard to beneficial stockholders, SAIC may solicit as stockholders only those plan participants who have retired, have reached retirement age (as defined in each plan), or those who have purchased SAIC stock through the employee's voluntary contributions in SAIC's Profit Sharing I plan. Of course, the solicitation by the Committee or SAIC must otherwise meet the requirements for a proper solicitation under the Act and regulations. 2 U.S.C. 441b(b)(3)(A), (B) and (C); see 11 CFR 114.5(a).^{10/}

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.

Sincerely,

(signed)

Danny L. McDonald
Chairman

Enclosures (AOs 1994-27, 1988-36, 1988-19, 1985-35, 1984-5, 1983-35 and 1983-17.)

1/ You state that as of October 1, 1994, 91% of SAIC's stock was held directly or indirectly by the company's employees, directors, officers and consultants, with the remainder held by former affiliates of SAIC.

2/ According to your February 13 submission, 10,626 employees are direct SAIC stockholders.

3/ Your request materials state that SAIC's right of repurchase does not apply to stock purchased during or before 1981 and to stock held beneficially through participation in SAIC's Employee Stock Ownership Plan discussed below.

4/ These plans together hold approximately 46% of SAIC's Class A common stock. Your materials indicate that employees can belong to more than one plan. As of November 30, 1994, CODA had 16,522 participants; ESOP had 13,454; Profit Sharing I had 11,618; and Profit Sharing II had 2,032.

5/ Profit Sharing I technically no longer holds any SAIC stock. For tax purposes, the various accounts administered by Profit Sharing I were combined with accounts held under CODA. However, the funds originated from the prior voluntary accounts of Profit Sharing I are subject to the liberal withdrawal rules of Profit Sharing I rather than the more restrictive rules of CODA. A significant fact is that the transferred voluntary accounts held in CODA still currently hold a small number of SAIC shares. In a phone conversation with Commission staff, you have stated that the number of employees participating in Profit Sharing I who have invested in SAIC stock with their voluntary accounts is quite small.

6/ SAIC's past and current policy not to declare dividends is not relevant to the analysis of the cited regulation. It is not necessary that a corporation actually declare and pay out dividends to stockholders or makes it its policy to do so. Rather, what is required under section 114.1(h) is that the stock carry the right to receive dividends, if they were declared.

7/ In Advisory Opinion 1985-35, the Commission dealt with the solicitation of the non-shareholding directors of an employee-owned corporation. The Commission concluded that the employee-owned status of the company did not affect the solicitability of these directors. See Advisory Opinion 1985-35.

8/ In Advisory Opinion 1994-27, the Commission examined a stock ownership plan that contained a provision for hardship withdrawals identical to that permitted in SAIC's CODA plan. The Commission concluded that this purpose based limitation was at least as restrictive as limitations based on frequency of permitted withdrawals, or those providing for suspension as a penalty for withdrawals.

9/ There are no restrictions on the withdrawal rights of CODA participants upon reaching retirement age. Again, for participants in ESOP and Profit Sharing II, prior to actual retirement they are permitted one in-service withdrawal. Since, following the Commission's conclusion in Advisory Opinion 1994-27, there is no purpose-based limitation, no forfeiture of rights and no suspension of participation in the plan, the above withdrawal rights are sufficient to constitute a right to receive dividends. See Advisory Opinion 1994-27.

10/ For example, a corporation or separate segregated fund that solicited contributions of a particular amount must inform the person solicited that such amount is only a suggestion and that the person is free to contribute more or less than the suggested amount. 11 CFR 114.5(a)(2). Moreover, any solicitation for a separate segregated fund must describe the political purpose of

the fund and specify that persons have the right to refuse to contribute to the fund without reprisal. 11 CFR 114.5(a)(3), (a)(4), and (a)(5).