



FEDERAL ELECTION COMMISSION
Washington, DC 20463

November 9, 2004

MEMORANDUM

TO: ROBERT W. BIERSACK
PRESS OFFICER
PRESS OFFICE

FROM: JOSEPH F. STOLTZ *JFS*
ASSISTANT STAFF DIRECTOR
AUDIT DIVISION

SUBJECT: PUBLIC ISSUANCE OF THE AUDIT REPORT ON
TENNESSEE REPUBLICAN PARTY FEDERAL ELECTION ACCOUNT

Attached please find a copy of the audit report and related documents on Tennessee Republican Party Federal Election Account which was approved by the Commission on November 1, 2004.

The report may be released to the public on November 9, 2004.

Attachment as stated

cc: Office of General Counsel
Office of Public Disclosure
Reports Analysis Division
FEC Library
Web Manager



Report of the Audit Division on the Tennessee Republican Party Federal Election Account

January 1, 2001 – December 31, 2002

Why the Audit Was Done

Federal law permits the Commission to conduct audits and field investigations of any political committee that is required to file reports under the Federal Election Campaign Act (the Act). The Commission generally conducts such audits when a committee appears not to have met the threshold requirements for substantial compliance with the Act.¹ The audit determines whether the committee complied with the limitations, prohibitions and disclosure requirements of the Act.

Future Action

The Commission may initiate an enforcement action, at a later time, with respect to any of the matters discussed in this report.

About the Committee (p. 2)

The Tennessee Republican Party Federal Election Account (TRP) is a state party committee headquartered in Nashville, Tennessee. For more information, see the chart on the Committee Organization, p. 2.

Financial Activity (p. 2)

• Receipts	
○ Contributions from individuals	\$ 2,915,450
○ Transfers from affiliated/other party committees	1,014,314
○ Transfers from a nonfederal account for joint activity	824,619
○ All other receipts	450,400
○ Total Receipts	\$ 5,204,783
• Disbursements	
○ Operating disbursements	\$ 4,900,340
○ All other disbursements	255,446
○ Total Disbursements	\$ 5,155,786

Findings and Recommendations (p. 3)

- Misstatement of Financial Activity (Finding 1)
- Receipt of Contributions that Exceed Limits (Finding 2)
- Receipt of Prohibited Contribution (Finding 3)

¹ 2 U.S.C. §438(b).

Table of Contents

	Page
Part I. Background	
Authority for Audit	1
Scope of Audit	1
Changes to the Law	1
Part II. Overview of Committee	
Committee Organization	2
Overview of Financial Activity	2
Part III. Summaries	
Findings and Recommendations	3
Part IV. Findings and Recommendations	
Finding 1. Misstatement of Financial Activity	4
Finding 2. Receipt of Contributions that Exceed Limits	7
Finding 3. Receipt of Prohibited Contribution	9

Part I

Background

Authority for Audit

This report is based on an audit of the Tennessee Republican Party Federal Election Account (TRP), undertaken by the Audit Division of the Federal Election Commission (the Commission) in accordance with the Federal Election Campaign Act of 1971, as amended (the Act). The Audit Division conducted the audit pursuant to 2 U.S.C. §438(b), which permits the Commission to conduct audits and field investigations of any political committee that is required to file a report under 2 U.S.C. §434. Prior to conducting any audit under this subsection, the Commission must perform an internal review of reports filed by selected committees to determine if the reports filed by a particular committee meet the threshold requirements for substantial compliance with the Act. 2 U.S.C. §438(b).

Scope of Audit

Following Commission approved procedures, the Audit staff evaluated various factors and as a result, this audit examined:

1. The receipt of excessive contributions and loans.
2. The receipt of contributions from prohibited sources.
3. The disclosure of contributions and other receipts.
4. The disclosure of disbursements, debts and obligations.
5. The disclosure of expenses allocated between federal and nonfederal accounts.
6. The consistency between reported figures and bank records.
7. The completeness of records.
8. Other committee operations necessary to the review.

Changes to the Law

On March 27, 2002, President Bush signed into law the Bipartisan Campaign Reform Act of 2002 (BCRA). The BCRA contains many substantial and technical changes to the federal campaign finance law. Most of the changes became effective November 6, 2002. Except for the period November 7, 2002, through December 31, 2002, the period covered by this audit pre-dates these changes. Therefore, the statutory and regulatory requirements cited in this report are primarily those that were in effect prior to November 7, 2002.

Part II

Overview of Committee

Committee Organization

Important Dates	Tennessee Republican Party Federal Election Account
• Date of Registration	July 14, 1976
• Audit Coverage	January 1, 2001 - December 31, 2002
Headquarters	Nashville, Tennessee
Bank Information	
• Bank Depositories	2
• Bank Accounts	8 Federal and 3 Nonfederal accounts
Treasurer	
• Treasurer When Audit Was Conducted	Joe R. Arnold
• Treasurer During Period Covered by Audit	Joe R. Arnold
Management Information	
• Attended Commission Campaign Finance Seminar	No
• Used Commonly Available Campaign Management Software Package	Yes
• Who Handled Accounting and Recordkeeping Tasks	A paid consultant and paid Committee staff.

Overview of Financial Activity (Audited Amounts)

Cash on hand @ January 1, 2001	\$ 102,294
Receipts	
○ Contributions from individuals	2,915,450
○ Transfers from affiliated/other party committees	1,014,314
○ Transfers from nonfederal account for joint activity	824,619
○ All other receipts	450,400
Total Receipts	\$ 5,204,783
Disbursements	
○ Operating disbursements	4,900,340
○ All other disbursements	255,446
Total Disbursements	\$ 5,155,786
Cash on hand @ December 31, 2002	\$ 151,291

Part III

Summaries

Findings and Recommendations

Finding 1. Misstatement of Financial Activity

TRP misstated receipts, disbursements and cash-on-hand balances for calendar years 2001 and 2002. In response to a recommendation in the interim audit report, TRP filed amended reports that corrected the misstatement of reported activity. (For more detail, see p. 4)

Finding 2. Receipt of Contributions that Exceed Limits

TRP received contributions from 20 individuals, three Political Action Committees (PACs) and one authorized committee that exceeded contribution limits by \$300,850, \$8,500, and \$1,000, respectively. The Audit staff recommended that TRP submit documentation to show that the contributions were not excessive or refund the excessive portion to the contributors. In response, TRP provided copies of refund checks (front only) and correspondence to support the refunds. (For more detail, see p. 7)

Finding 3. Receipt of Prohibited Contribution

TRP deposited a contribution of \$25,000 from an apparent prohibited source into its federal account. The Audit staff recommended that TRP document that the funds received were not from a prohibited source, document that the funds have been transferred to a nonfederal account, or transfer the funds from the federal account to the nonfederal account. In response, TRP documented a transfer of \$25,000 to a nonfederal account. (For more detail, see p. 10)

Part IV

Findings and Recommendations

Finding 1. Misstatement of Financial Activity

Summary

TRP misstated receipts, disbursements and cash-on-hand balances for calendar years 2001 and 2002. In response to a recommendation in the interim audit report, TRP filed amended reports that corrected the misstatement of reported activity. (For more detail, see p. 4)

Legal Standard

Contents of Reports. Each report must disclose:

- The amount of cash on hand at the beginning and end of the reporting period;
 - The total amount of receipts for the reporting period and for the calendar year;
 - The total amount of disbursements for the reporting period and for the calendar year; and
 - Certain transactions that require itemization on Schedule A (Itemized Receipts) or Schedule B (Itemized Disbursements).
- 2 U.S.C. §§434(b)(1), (2), and(4).

Facts and Analysis

The Audit staff reconciled reported activity to bank records for calendar years 2001 and 2002. The following charts outline the discrepancies for the beginning cash balances, receipts, disbursements, and the ending cash balances. The succeeding paragraphs explain why the differences occurred, if known.

2001 Committee Activity			
	Reported	Bank Records	Discrepancy
Opening Cash Balance @ January 1, 2001	\$94,098	\$102,294	\$8,196 Understated
Receipts	\$1,307,283	\$1,311,148	\$3,865 Understated
Disbursements	\$1,210,909	\$1,246,313	\$35,404 Understated
Ending Cash Balance @ December 31, 2001	\$190,472	\$167,129	\$23,343 Overstated

Opening Cash Balance – 2001

The beginning cash on hand was understated by \$8,196; due principally to prior period misstatements of financial activity and unreported bank depositories.

Receipts – 2001

The \$3,864 understatement of receipts was unexplained.

Disbursements – 2001

The understatement of disbursements was the net result of the following:

• Unreported bank fees	+ \$	2,375
• Unreported credit card charges	+	5,514
• Reported disbursements that were not reflected in the bank records - principally transfers to the nonfederal account	-	52,987
• Unreported disbursements - generally payroll related expenses and other federal operating expenditures	+	77,656
• Unexplained difference	+	<u>2,846</u>
Net understatement	+ \$	<u>35,404</u>

TRP staff stated that reported disbursements not reflected in the bank records (\$52,987) were intended to be transferred electronically. However, because a number of the transfer requests were not in writing, a failure to execute the transfers occurred. As for the \$77,656 in unreported disbursements, TRP used an electronic payroll vendor and much of the disbursement information was not captured by TRP's accounting system.

Ending Cash Balance – 2001

The \$23,343 overstatement of the closing cash on hand was the net result of the misstatements described above.

2002 Committee Activity			
	Reported	Bank Records	Discrepancy
Opening Cash Balance ² @ January 1, 2002	\$163,878	\$167,129	\$3,251 Understated
Receipts	\$3,623,477	\$3,893,635	\$270,158 Understated
Disbursements	\$3,696,037	\$3,909,473	\$213,436 Understated
Ending Cash Balance @ December 31, 2002	\$91,318	\$151,291	\$59,973 Understated

² The change in the "Reported" cash on hand balance between December 31, 2001, and January 1, 2002, (a reduction of \$26,594) was not supported by TRP records.

Opening Cash Balance – 2002

As a result of the prior year's misstatement and an unsupported change in the cash on hand balance for January 1, 2002, as compared to the ending cash on hand for December 31, 2001, the beginning cash balance was understated by \$3,251.

Receipts – 2002

The understatement of receipts was the net result of the following:

• Reported receipts from Schedule(s) A and H3 (Transfers From Nonfederal Accounts) that were never credited to a federal bank account - principally two reported transfers from a nonfederal account that never occurred	- \$ 220,220
• Unreported interest earned	+ 5,563
• Unreported receipts, from individuals (\$391,950 ³) and PACs (\$241,200) ⁴ deposited into a federal account	+ 633,150
• Over-stated unitemized receipts	- 148,059
• Unexplained difference	- 276
Net understatement	<u>+ \$ 270,158</u>

Disbursements – 2002

The overstatement of disbursements was the net result of the following:

• Unreported bank fees	+ \$ 6,352
• Disbursements reported on Schedule(s) B and H4 (Joint Federal/ Nonfederal Activity Schedule) that were never charged to a federal bank account because they were voided, duplicated or never charged	- 26,650
• Unreported disbursements – principally payroll, related payroll expenses and other federal operating expenditures	+ 228,192
• Unexplained difference	+ 5,542
Net overstatement	<u>+ \$ 213,436</u>

Ending Cash Balance – 2002

The \$59,973 overstatement of the closing cash on hand was the net result of the misstatements described above.

The Audit staff discussed this finding with TRP's representatives at an interim field conference and during the exit conference, and presented them with copies of relevant workpapers. TRP representatives stated that corrective amendments would be filed.

Interim Audit Report Recommendation And Committee Response

The Audit staff recommended that TRP file complete amended reports, including all supporting schedules, by reporting period, for calendar years 2001 and 2002. In response to the interim audit report, TRP filed amended reports that corrected the misstatement of reported activity.

³ As more fully discussed in Finding 2, \$300,850 of the unreported receipts are individual contributions that exceed annual limits. TRP reported only that portion of the contribution that could be retained in the federal account.

⁴ Neither TRP nor the Audit staff could explain this omission.

Finding 2. Receipt of Contributions that Exceed Limits

Summary

TRP received contributions from 20 individuals, three Political Action Committees (PACs) and one authorized committee that exceeded contribution limits by \$300,850, \$8,500, and \$1,000, respectively. The Audit staff recommended that TRP submit documentation to show that the contributions were not excessive or refund the excessive portion to the contributors. In response, TRP provided copies of refund checks (front only) and correspondence to support the refunds.

Legal Standard

A. Party Committee Limits. A party committee may not receive more than a total of \$5,000 per year from any one contributor. 2 U.S.C. §441a(a)(1)(C) and 11 CFR §§110.1(a) and (d) and 110.9(a).

B. Handling Contributions That Appear Excessive. If a committee receives a contribution that appears to be excessive, the committee must either:

1. Return the questionable check to the donor; or
 2. Deposit the check into its federal account and:
 - ♦ Keep enough money in the account to cover all potential refunds;
 - ♦ Keep a written record explaining why the contribution may be illegal;
 - ♦ Include this explanation on Schedule A if the contribution has to be itemized before its legality is established;
 - ♦ Seek a *retribution* of the excessive portion, following the instructions provided in Commission regulations (see below for explanation of *retribution*); and
 - ♦ If the committee does not receive a proper retribution within 60 days after receiving the excessive contribution, refund the excessive portion to the donor.
- 11 CFR §§103.3(b)(3), (4) and (5) and 110.1(k)(3)(ii)(B).

C. Joint Contributions. Any contribution made by more than one person (except for a contribution made by a partnership) must include the signature of each contributor on the check or in a separate writing. A joint contribution is attributed equally to each donor unless a statement indicates that the funds should be divided differently. 11 CFR §110.1(k)(1) and (2).

D. Retribution of Excessive Contributions. Commission regulations permit committees to ask donors of excessive contributions whether they had intended their contribution to be a joint contribution from more than one person and whether they would like to *retribute* the excess amount to the other contributor. The committee must inform the contributor that:

1. The retribution must be signed by both contributors;
2. The retribution must be received by the committee within 60 days after the committee received the original contribution; and
3. The contributor may instead request a refund of the excessive amount. 11 CFR §110.1(k)(3).

Within 60 days after receiving the excessive contribution, the committee must either receive the proper retribution or refund the excessive portion to the donor. 11 CFR §§103.3(b)(3)

and 110.1(k)(3)(ii)(B). Further, a political committee must retain written records concerning the reattribution in order for it to be effective. 11 CFR §110.1(l)(5).

E. Revised Regulations Applied. The Commission recently adopted new regulations that allow committees greater latitude to reattribute contributions to joint account holders and has decided to apply these regulations to current matters. The Audit staff has evaluated the excessive contributions discussed below using the new regulations.

F. Federal v. Nonfederal Account. The federal account may contain only those funds that are permissible under the federal election law; the nonfederal account may contain funds that are not permitted under the federal law (but are legal under state law), such as contributions that exceed the limits of the federal law and contributions from prohibited sources, such as corporations and labor organizations. 11 CFR §102.5(a)(1)(i) and (a)(3).

Facts and Analysis

TRP deposited individual contributor checks that exceeded the \$5,000 contribution limitation into the federal account but only reported the federal portion on the Commission's disclosure reports. The apparent intent of the committee and contributor was to "split" the contribution between the federal and nonfederal bank accounts and then transfer the nonfederal portion to a nonfederal bank account. Only three such transfers, totaling \$126,000, were made. Even then, TRP failed to make these transfers in a timely fashion, resulting in the apparent excessive contributions. After considering the transfers noted above, the review of contributions identified 20 individuals, three PACs, and one authorized committee that exceeded the limitations by \$300,850, \$8,500, and \$1,000, respectively. TRP did not deposit the questionable contributions into a separate account nor did it consistently maintain sufficient funds to refund these contributions.⁵ (See Finding 1, 2002 Committee Activity.)

The Audit staff discussed this finding with TRP's representatives at an interim field conference and during the exit conference, and presented them with copies of relevant workpapers. TRP representatives stated that they would contact the donors and make refunds in accordance with our recommendations.

Interim Audit Report Recommendation And Committee Response

The Audit staff recommended that TRP:

- Provide evidence demonstrating that the contributions in question are not excessive; or
- Refund \$300,850 to individuals, \$8,500 to PACs, and \$1,000 to the authorized committee, providing evidence of such refunds (copies of the front and back of the negotiated refund checks); and
- If funds are not available to make the necessary refunds, disclose the refunds due on Schedule D (Debts and Obligations) until funds become available to make the refunds.

In response to the interim audit report, TRP provided check copies (front only) and correspondence to support the recommended refunds.

⁵ The Audit staff also considered the apparent prohibited contribution received by the TRP in determining if a sufficient balance was maintained to refund the questionable contributions. (See Finding 3)

Finding 3. Receipt of Prohibited Contribution

Summary

TRP deposited a contribution of \$25,000 from an apparent prohibited source into its federal account. The Audit staff recommended that TRP document that the funds received were not from a prohibited source, document that the funds have been transferred to a nonfederal account, or transfer the funds from the federal account to the nonfederal account. In response, TRP documented a transfer of \$25,000 to a nonfederal account.

Legal Standard

- A. Federal v. Nonfederal Account.** The federal account may contain only those funds that are permissible under the federal election law; the nonfederal account may contain funds that are not permitted under the federal law (but are legal under state law), such as contributions that exceed the limits of the federal law and contributions from prohibited sources, such as corporations and labor organizations. 11 CFR §102.5(a)(1)(i) and (a)(3).
- B. Questionable Contributions.** If a committee receives a contribution that appears to be prohibited (a questionable contribution), it must follow the procedures below:
1. Within 10 days after the treasurer receives the questionable contribution, the committee must either:
 - Return the contribution to the contributor without depositing it; or
 - Deposit the contribution (and follow the steps below). 11 CFR §103.3(b)(1).
 2. If the committee deposits the questionable contribution, it may not spend the funds and must be prepared to refund them. It must therefore maintain sufficient funds to make the refunds or establish a separate account in a campaign depository for possibly illegal contributions. 11 CFR §103.3(b)(4).
 3. The committee must keep a written record explaining why the contribution may be prohibited and must include this information when reporting the receipt of the contribution. 11 CFR §103.3(b)(5).
 4. Within 30 days of the treasurer's receipt of the questionable contribution, the committee must make at least one written or oral request for evidence that the contribution is legal. Evidence of legality includes, for example, a written statement from the contributor explaining why the contribution is legal or an oral explanation that is recorded by the committee in a memorandum. 11 CFR §103.3(b)(1).
 5. Within these 30 days, the committee must either:
 - Confirm the legality of the contribution; or
 - Refund the contribution to the contributor and note the refund on the report covering the period in which the refund was made. 11 CFR §103.3(b)(1).

Facts and Analysis

In reviewing the transfers from other political committees, the Audit staff noted a \$25,000 contribution, deposited in May 2002, from the Republican National Committee's "nonfederal accounts of party committees" which was earmarked to a TRP nonfederal bank account. TRP erroneously deposited the funds to a federal bank account. The Audit staff was unable to determine if these funds were ultimately transferred to a nonfederal account. The TRP did not deposit these questionable funds into a separate account nor did it consistently maintain sufficient funds to refund the contribution.

The Audit staff discussed this finding with TRP's representatives at an interim field conference and during the exit conference, and presented them with copies of relevant workpapers. TRP representatives stated they would take corrective action.

Interim Audit Report Recommendation And Committee Response

The Audit staff recommended that TRP:

- Provide evidence that these funds are not from a prohibited source; or
- In the alternative, transfer \$25,000 to a nonfederal account and provide evidence of such a transfer in a timely manner; and,
- If funds are not available to make the necessary transfer, disclose the amount due on Schedule D (Debts and Obligations) until funds become available to make the transfer.

In response to the interim audit report, TRP documented a transfer of \$25,000 to a nonfederal account.