



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

March 8, 2010

MEMORANDUM

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SUBJECT: Proposed Final Audit Report on the Georgia Federal Elections Committee
(LRA 793)

I. INTRODUCTION

The Office of General Counsel has reviewed the proposed Final Audit Report ("FAR") on the Georgia Federal Elections Committee ("the Committee"). Our comments address Findings 1 and 2. We concur with any findings not specifically discussed in this memorandum. If you have any questions, please contact Allison T. Steinle, the attorney assigned to this audit.

Both Findings 1 and 2 involve the Committee's payroll account. We believe the two findings are interrelated. Specifically, our ultimate analysis of Finding 1 depends on the documentation the Committee has provided in response to Finding 2. Therefore, we address Finding 2 first.

As background, we understand that the Committee established the payroll account in question to accommodate the restrictions imposed by its payroll vendor, Paychex, which would not draw the Committee's payroll from both its federal and non-federal operating accounts. Accordingly, the Committee elected to set up a separate account from which it makes its federal and non-federal payroll disbursements. The Committee states that this payroll account functions as an "escrow account" or "transmittal account" because it is used exclusively to pay salaries and payroll taxes. The Committee states that it calculates the appropriate amount of federal and non-federal funds for each payroll period and transfers these funds from the federal and non-federal operating accounts to the payroll account, from which it pays all its federal, non-federal, and allocable employees. The Committee states it reports the federal and allocable payroll disbursements from this account on Schedule B or Schedule H4 as appropriate. However, the Committee claims that this payroll account is neither a federal account nor an allocation account, and therefore it is not required to report entirely non-federal activity to the Commission.

II. FINDING 2 – PAYMENT OF FEDERAL ACTIVITY WITH NON-FEDERAL FUNDS

Finding 2 addresses the Committee's failure to maintain a monthly log detailing the time spent on federal activities for employees whose salaries and related expenses were paid from the payroll account. State party committees must keep a monthly log documenting the percentage of time each employee spends in connection with a federal election. 11 C.F.R. § 106.7(d)(1). If employees spend more than 25 percent of their time on federal election activity ("FEA") or in connection with a federal election, their salaries and related expenses must be paid only from a federal account. 11 C.F.R. § 106.7(d)(1)(ii). Prior to January 19, 2006, if employees spent less than 25 percent of their time on FEA or in connection with a federal election, their salaries and related expenses could be paid entirely with non-federal funds. However, under the new salary allocation rules that became effective January 19, 2006, if employees spend 25 percent or less of their time on FEA or activities in connection with a federal election, they may be paid either entirely with federal funds or at the same allocation rate as the committee's administrative expenses. 11 C.F.R. § 106.7(d)(1)(i). Only if employees spend all of their time on entirely non-federal activity may they may be paid entirely with non-federal funds. 11 C.F.R. § 106.7(d)(1)(iii).

In this case, the Committee claims that a portion of the payroll account—perhaps as much as two thirds of the funds that passed through the account—was used to pay salaries and payroll taxes for employees who were engaged in exclusively non-federal activity.¹ However, the Committee has not provided the monthly logs required by 11 C.F.R. § 106.7(d)(1). Instead, in response to the Interim Audit Report ("IAR"), the Committee has provided six affidavits from the employees in question stating that, prior to when the new salary rules became effective, they did not spend more than 25 percent of their time on FEA or activities in connection with a federal election, and that they did not spend any time on FEA or activities in connection with a

¹ The Audit Division has stated that 33 percent of the account's activity was reported on the Committee's disclosure reports to the Commission. It is our understanding that this means the Committee is claiming that only 33 percent of its salaries or related expenses were for employees who spent time on FEA or activities in connection with a federal election.

federal election after the new salary rules became effective. The proposed FAR concludes that the affidavits are sufficient to establish that the Committee properly allocated the salaries of the six employees.

In recent audits of state party committees, the Commission has permitted committees to use similar affidavits as supporting documentation, despite the fact that they had not maintained the monthly logs required under 11 C.F.R. § 106.7(d)(1). See FAR on the Missouri Democratic Party (Feb. 3, 2009). Therefore, consistent with the Commission's practices in these audits, we agree with the Audit Division that the Committee has provided sufficient alternate documentation to establish that the Committee did not improperly pay for federal activity using non-federal funds.

III. FINDING 1 – MISSTATEMENT OF FINANCIAL ACTIVITY

While Finding 2 concludes that a large proportion of funds in the payroll account were for non-federal salaries or related expenses, Finding 1 addresses the Committee's failure to report that activity. The Committee states that it should not be required to report the payroll account's non-federal activity to the Commission because the payroll account is neither a federal account nor an allocation account. The Committee argues that the disclosure of non-federal activity "would result in an artificial increase in the disclosure of its federal activity, which it believes would be burdensome for the Committee and confusing to readers of [the Committee's] reports." Committee Response at 2. However, the proposed FAR concludes that the payroll account functioned as an allocation account, from which all activity, including non-federal activity, was reportable to the Commission. To assist the Commission in resolving this issue, we address the Commission's options for how to treat a committee whose payroll vendor will not draw payroll from multiple federal and non-federal operating accounts.²

As an initial matter, we believe the Commission could determine that the Committee's establishment and use of the payroll account was reasonable under the circumstances. In the past, the Commission has been sympathetic to committees whose payroll vendors limit their ability to draw payroll from multiple federal and non-federal operating accounts. See *supra* n.2. Here, the Committee faced a Catch-22 created by the current salary allocation rules and the limitations of its payroll vendor. The Committee was prohibited from transferring funds from its non-federal account to reimburse its federal account for non-allocable non-federal activity, so if it used its federal account to make its payroll disbursements it could not have recouped the

² The question of whether a committee could set up a single payroll account to pay both federal and non-federal salaries and related expenses was raised by a commenter during the 2005 salary allocation rulemaking. See Explanation and Justification for State, District, and Local Party Committee Payment of Certain Salaries and Wages, 70 Fed. Reg. 75,379, 75,383 (Dec. 20, 2005). However, the Commission concluded that it was beyond the scope of the rulemaking and has not to our knowledge directly revisited the question. *Id.* In a subsequent Reports Analysis Division referral to the Office of General Counsel, which was not made public because the Commission declined to open a MUR, the Commission determined not to seek enforcement action against a committee faced with the same problem caused by the same payroll vendor. The committee in question there, however, had elected to pay its non-federal payroll from its federal operating account and transfer in non-federal funds to reimburse those payments rather than set up a separate payroll account.

portion of that "hard money" it used for non-federal salaries and related expenses. 11 C.F.R. § 106.7(f)(1). However, the Committee could not use the non-federal account to make all of its payroll disbursements, because the Committee was prohibited from making disbursements from its non-federal account for allocable or federal purposes. 11 C.F.R. §§ 102.5(a). The Committee attempted to comply with the law by creating a separate payroll account from which it could make 100 percent non-federal disbursements, as well as federal and allocable disbursements.

However, the Committee did not report any of the payroll account's non-federal activity to the Commission. Therefore, the question becomes whether, as the Committee claims, the Committee could treat its payroll account as a kind of "escrow account" or "transmittal account" that is neither federal nor non-federal, and from which the Committee would only be required to report its federal and allocable activity, but not its non-federal activity. This appears to be a question of first impression because neither the statute nor the regulations contemplate the existence of such an account, and therefore do not provide any guidance on the treatment of the account for disclosure purposes.

On the one hand, the Committee is correct that the payroll account at issue here was unlike an ordinary allocation account in that it contained non-federal funds to be used for the payment of non-allocable, 100 percent non-federal expenses. See 11 C.F.R. § 104.17(b). Commission regulations specify that allocation accounts may be used "solely for the purpose of paying the allocable expenses of joint federal and non-federal activities." 11 C.F.R. § 106.7(f)(1) (emphasis added). Here, requiring the Committee to disclose all activity in the payroll account would result in the Committee disclosing payroll information for some exclusively non-federal employees paid with exclusively non-federal funds for a particular pay period.

On the other hand, however, we agree with the Audit Division that the payroll account served as the functional equivalent of an allocation account, in that it allowed the Committee to make both federal and non-federal disbursements with funds originating from both its federal and non-federal operating accounts. See 11 C.F.R. §§ 102.5(a), 106.7(f)(1). The transfer and reimbursement rules ordinarily prohibit state party committees from transferring non-federal funds to an account containing federal funds to reimburse that account for 100 percent non-federal activity. 11 C.F.R. § 106.7(f). Allocation accounts permit state party committees to mix funds from a committee's federal and non-federal operating accounts to pay allocable expenses, but are considered federal accounts from which that committee must report all activity, including the non-federal portion of activity. See 11 C.F.R. §§ 104.17, 106.7(f); Explanation and Justification for Methods of Allocation between Federal and Non-Federal Accounts, 55 Fed. Reg. 26,058, 26,065-66 (June 26, 1990). Just as this reporting requirement allows the Commission to verify that committees are transferring and using the proper amount of non-federal funds to pay for allocable activities, requiring the Committee to report 100 percent non-federal disbursements here allows the Commission to verify that the Committee used and transferred the proper amount of non-federal funds to pay for non-allocable non-federal activities, and did not use non-federal funds to subsidize federal activities. See 55 Fed. Reg. at 26,066 (noting that a reporting requirement "allow[s] the Commission to track the flow of non-

federal funds into federal accounts, and [] ensure[s] that the use of such funds is strictly limited to payment for the non-federal share of allocable activities”). While the Committee claims that the disclosure of its non-allocable non-federal activity would be burdensome, it has already stated that it calculates the appropriate amount of federal and non-federal funds for each payroll period in order to transfer the proper amounts from the federal and non-federal operating accounts to the payroll account. The Audit Division’s proposed treatment of the payroll account would only require the Committee to disclose the financial information it has already calculated. Moreover, the Committee’s concern that such a reporting requirement would result in an artificial increase in federal activity and confusion by readers is addressed by the Audit Division’s recommendation that the Committee only report the non-federal activity as “Other Disbursements” on Schedule B, Line 29.³ Accordingly, because we are of the view that committees should be required to report non-federal funds if they mix those funds with federal funds in a single account, *see* 55 Fed. Reg. at 26,066, and the payroll account at issue here functions as a federal allocation account in that it mixes non-federal and federal funds, we conclude that the Committee should be required to report all of the payroll account’s activity, including the transfer in and disbursement of non-federal funds to pay salaries and related expenses that are 100 percent non-federal.

We reiterate that the transfer and reimbursement rules ordinarily prohibit state party committees from transferring funds from a non-federal account to reimburse a federal account for non-allocable non-federal activity. 11 C.F.R. § 106.7(f)(1). We note that in order to ensure complete compliance with the law in the future, the Committee will have to choose a payroll vendor that will draw its payroll from its federal and non-federal operating accounts in compliance with the regulations.

³ Currently, the proposed FAR instructs the Committee to report the non-federal activity on Schedule B, Line 29, with a memo entry indicating that the transactions are being disclosed as a result of the FEC audit. However, to avoid confusion by readers, we recommend that the FAR instruct the Committee to also include memo entries for these transactions that specifically indicate that they are for non-allocable non-federal activity.