



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

April 21, 2000

MEMORANDUM

TO: RON M. HARRIS
PRESS OFFICER
PRESS OFFICE

FROM: ROBERT J. COSTA *RJ Costa*
ASSISTANT STAFF DIRECTOR
AUDIT DIVISION

SUBJECT: PUBLIC ISSUANCE OF THE AUDIT REPORT ON
MICHIGAN STATE REPUBLICAN PARTY

Attached please find a copy of the audit report and related documents on the Michigan State Republican Party for which was approved by the Commission on April 13, 2000.

Informational copies of the report have been received by all parties involved and the report may be released to the public on April 21, 2000.

Attachment as stated

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

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REPORT OF THE AUDIT DIVISION
ON
Michigan Republican State Committee

Approved April 13, 2000



FEDERAL ELECTION COMMISSION

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TABLE OF CONTENTS

MICHIGAN STATE REPUBLICAN PARTY

	Page
Executive Summary	1
Final Audit Report	5
Background	5
Findings	7
Legal Analysis	29
Transmittal to Committee	35
Chronology	37

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FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

**REPORT OF THE AUDIT DIVISION
ON THE
MICHIGAN REPUBLICAN STATE COMMITTEE**

EXECUTIVE SUMMARY

The Michigan Republican State Committee (MRSC) registered with the Comptroller General of the United States on April 17, 1972.

The audit was conducted pursuant to Section 438(b) of Title 2 of the United States Code which states, in part, that the Commission may conduct audits of any political committee whose reports fail to meet the threshold level of compliance set by the Commission.

The findings of the audit were presented to the MRSC at an exit conference and later, in an Interim Audit Report. The MRSC's responses to those findings are included in the Final Audit Report.

The following is an overview of the findings contained in the Final Audit Report.

POSSIBLE IMPERMISSIBLE EXPENDITURES ON BEHALF OF FEDERAL CANDIDATES - PHONE BANKS - 2 U.S.C. §441a(d), 11 CFR §§110.7(a)(4), 100.8(b)(18)(i).

The MRSC operated a get-out-the-vote phone bank on behalf of the Presidential and Vice Presidential nominees, and three non-federal candidates. The project involved 124 salaried persons. The use of a salaried staff for the phone bank voids the contribution exemption at 11 CFR §100.8(b)(18)(v). The Audit concludes that MRSC made a \$5,794 contribution to or independent expenditure on behalf of Dole/Kemp '96. The Interim Audit Report recommended that MRSC demonstrate that the exemption was not voided. In response to the report the MRSC neither provided any additional documentation; nor did it accept or refute the finding.

SHARED EXPENSES PAID FROM NON-FEDERAL ACCOUNTS — 11 CFR §§100.8(a)(1), 104.10(b)(4), 106.5(a), (d), (e), (f) and (g), and 106.6(e)

The MRSC maintains an account entitled "Michigan Republican State Comm Administrative Account" (the Account). According to the MRSC, funds expended from the Account do not impact federal, state, or local elections, therefore, it considers such

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transactions to be non-campaign related. Receipt and disbursement transactions are not included in its federal or state disclosure reports. Approximately \$413,573 in expenses were identified that are subject to allocation between the federal and non-federal accounts. These expenses were administrative in nature and associated with a State Convention, State Committee Meetings, RNC Meetings/Conferences, as well as, the day to day operations of the MRSC.

A review of a second non-federal account, "Republican National Convention" (Convention Account) identified \$78,538 in apparent allocable expenses associated with activities during the Republican National Convention in San Diego, CA.

Finally, from the non-federal operating account (Operating Account) the MRSC disbursed \$10,951 for allocable GOTV activity.

The Interim Audit Report recommended that the MRSC reimburse the non-federal account for its share of allocable expenses (\$183,353) paid from these three accounts and file memo Schedules H4 disclosing the shared expenses.

In response, the MRSC made a reimbursement of \$21,402 for the federal share of expenses it acknowledged were allocable. The MRSC also demonstrated that \$7,173 represents solely non-federal expenses paid from the Account. The MRSC contends that the disbursements from the Convention Account were for social functions and did not impact on a federal election. The MRSC did not respond to the review of the Operating Account.

The Audit concluded that the MRSC should reimburse the non-federal account \$154,778 (\$183,353 - \$21,402 - \$7,173) for shared federal and non-federal activity.

REPORTING AND ITEMIZATION OF RECEIPTS AND DISBURSEMENTS -
2 USC §434(b), 11 CFR §§104.10(b)(4), 106.5(g)(1) and (3), & 102.17(iii)(8)(B).

Reports filed by the MRSC contained errors or omissions for which amending action was recommended in the Interim Audit Report.

The MRSC did not disclose on Schedule H3 \$284,919 in transfers from its non-federal checking account to its federal payroll account nor did it report the related payroll disbursements totaling \$284,919 on Schedule H4. In addition, the MRSC did not itemize on Schedule H3 transfers totaling \$634,239 from the non-federal operating account to the federal allocation account for the non-federal share of disbursements to vendors. Finally, the non-federal share (\$12,745) of in-kind transfers from the Republican National Committee were not reported on H3 Schedules.

The MRSC failed to itemize and report contributions from political committees totaling \$4,440, the federal share of in-kind transfers from the Republican National Committee for \$7,647, and interest receipts totaling \$12,271.

The review of disbursements determined that the MRSC failed to report and itemize bank charges and disbursements to vendors totaling \$756,462, and transfers to the non-federal account totaling \$13,500. The MRSC reported but failed to itemize as an *Independent Expenditure* a disbursement for \$80,842 on behalf of a federal candidate.

In response to the Interim Audit Report the MRSC filed all schedules as recommended.

MISSTATEMENT OF FINANCIAL ACTIVITY - 2 U.S.C. §434(b)(1), (2) and (4).

A comparison of the Committee's reported activity to its bank account records revealed misstatements in beginning cash, ending cash, total receipts and total disbursements disclosed on the MRSC's 1995 and 1996 reports.

In response to the Interim Audit Report recommendations the MRSC filed amended reports which corrected the misstatements.

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FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

***REPORT OF THE AUDIT DIVISION
ON THE
MICHIGAN REPUBLICAN STATE COMMITTEE***

I. BACKGROUND

A. AUDIT AUTHORITY

This report is based on an audit of the Michigan Republican State Committee (MRSC), undertaken by the Audit Division of the Federal Election Commission (the Commission) in accordance with the provisions of the Federal Election Campaign Act of 1971, as amended (the Act). The audit was conducted pursuant to Section 438(b) of Title 2 of the United States Code which states, in part, that the Commission may conduct audits and field investigations of any political committee required to file a report under Section 434 of this title. Prior to conducting any audit under this subsection, the Commission shall 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.

B. AUDIT COVERAGE

The audit covered the period January 1, 1995 through December 31, 1996. During this period, the MRSC reported a beginning cash balance of \$175,858; total receipts for the period of \$8,750,815; total disbursements for the period of \$8,706,933; and an ending cash balance of \$219,740.¹

C. CAMPAIGN ORGANIZATION

The MRSC registered with the Comptroller General of the United States as the Michigan Republican State Committee on April 17, 1972. The Treasurer of the MRSC for the period covered by the audit is William H. Gnodtke. The MRSC maintains its headquarters in Lansing, Michigan.

To manage its financial activity, the MRSC maintained nine checking and savings accounts and held several certificates of deposits. The MRSC's receipts were composed of approximately 112,500 contributions totaling \$4,391,000 from individuals,

¹ All figures in report are rounded to the nearest dollar.

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contributions from political committees (\$74,300) and other party committees (\$909,001), refunds/rebates, interest and transfers from its non-federal account.

D. AUDIT SCOPE AND PROCEDURES

The Audit staff was unable to verify the allocation between the federal and non-federal accounts of \$535,503 in media expenditures. The MRSC made two payments to Strategic Media Services on October 15, 1996 and October 30, 1996 totaling \$535,503 which it reported as "Production & Development," and categorized the purpose as Administrative/Voter Drive. The MRSC allocated these disbursements at the ballot composition (Administrative) ratio of 62.5% non-federal; 37.5% federal. The invoices supporting this activity describe the incurred costs as "TV Buys 10/16-10/23 - Detroit" and "TV Buys 10/28-11/4 - Michigan (Detroit, MI)." The Audit staff repeatedly requested the tapes of these broadcasts so that the generic voter drive aspect (as reported) could be verified. When these requests did not result in the production of the requested information, the Commission issued subpoenas to both the vendor and MRSC to obtain all documentation relating to these media products but neither entity was able to provide the documentation (video tapes, storyboards or scripts) necessary to verify the reported allocation.

The audit included testing of the following general categories:

1. The receipt of contributions or loans in excess of the statutory limitations;
2. The receipt of contributions from prohibited sources;
3. Proper disclosure of contributions from individuals, political committees and other entities, to include the itemization of contributions when required, as well as, the completeness and accuracy of the information disclosed (see Finding II.C.);
4. Proper disclosure of disbursements including the itemization of disbursements when required, as well as, the completeness and accuracy of the information disclosed (see Finding II.C.);
5. Proper disclosure of campaign debts and obligations;
6. The accuracy of total reported receipts, disbursements and cash balances as compared to bank records (see Finding II.D.);
7. Adequate recordkeeping of campaign transactions;
8. Proper reporting and funding of allocable expenses (see Findings II.B. and C.); and,

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9. Other audit procedures that were deemed necessary in the situation.

In the Audit report on Dole For President, Inc. (DFP), a media program sponsored by the Republican National Committee (RNC) was discussed. The program was used to air a number of television commercials between April and August of 1996 that featured Senator Dole in a positive light, President Clinton in a negative light, or both. The DFP Audit report placed the cost of this program at \$18,453,619. It was also explained that much of the media placement was done through the state party committees. As was explained in an internal RNC memorandum, the reason for using the state party committees for the placement was to take advantage of their more favorable federal/non-federal allocation ratios. The RNC would have been required to use 65% federal funds and 35% non-federal funds to pay for the program. Conversely, the average ratio for the state party committees that were intended to be used to place the ads was, according to the RNC memorandum, 37% federal and 63% non-federal. MRSC was one of eighteen states through which media was placed in connection with the RNC program. The amount placed through MRSC was \$1,101,936.

Unless specifically discussed below, no material non-compliance was detected. It should be noted that the Commission may pursue any of the matters discussed in this report in an enforcement action.

II. AUDIT FINDINGS AND RECOMMENDATIONS

A. POSSIBLE IMPERMISSIBLE EXPENDITURES ON BEHALF OF FEDERAL CANDIDATES - PHONE BANKS

In the case of the general election campaign of any candidate for President of the United States who is affiliated with such party, the national committee of a political party may make expenditures on behalf of the candidate subject to certain limitations pursuant to 2 U.S.C. §441a(d)(2). Section 110.7(a)(4) Title 11 of the Code of Federal Regulations allows the national committee of a political party to make expenditures under 2 U.S.C §441a(d) and 11 CFR §110.7(a)(4) through a designated agent, such as a state party committee. The Regulations at 11 CFR §110.7(a)(4) do not provide a state party committee any other mechanism for making an expenditure on behalf of a presidential candidate in excess of the contribution limitations that apply to political committees.

Section 100.8(b)(18)(i) of Title 11 of the Code of Federal Regulations explains the restrictions placed on get-out-the-vote or voter registration activities by state party committees on behalf of party nominees. If such an activity is conducted on behalf of the Presidential and Vice Presidential nominee(s), the costs incurred are not an expenditure for the purpose of influencing the election of these candidates provided that such costs are not incurred in connection with any broadcasting or specified other forms of public political advertising. Subsection (iv) within this regulation explains that if the activities include references to any candidate(s) for the House or Senate, the costs of such activities which are allocable to that candidate(s) shall be an expenditure on behalf of

such candidate(s) unless the mention of such candidate(s) is merely incidental to the overall get-out-the-vote and voter registration activity. Subsection (v) makes it clear that payment of the costs incurred in the use of phone banks in connection with voter registration and get-out-the-vote activities is not an expenditure on behalf of a federal candidate provided such phone banks are operated by volunteers. The use of paid professionals to design the phone bank system, develop calling instructions and train supervisors is permissible.

Disbursements for a Salaried Get-Out-the-Vote Program

The MRSC reported disbursements for a shared exempt activity totaling \$23,174 in November and December, 1996. The expenditures, allocated 25% federal and 75% non-federal, were for telephone service (\$3,706) and for salaries and payroll taxes (\$19,468). The MRSC provided a script ("MIGOP Turnout Script #2") which urged the persons called to vote for Bob Dole, Jack Kemp and for three non-federal candidates. The MRSC annotated the script as "Part of GOTV Program." Although a MRSC official stated that the phone bank was operated by volunteers, the MRSC has failed to provide any documentation to explain the role of the 124 salaried persons involved with the project. The use of a salaried phone bank for get-out-the-vote activity on behalf of the Presidential and Vice Presidential nominees voids the exemption at 11 CFR §100.8(b)(18)(v). Absent documentation the Audit staff is of the opinion that this project reflects a \$5,794 (\$23,174 x 25%) contribution to, or independent expenditure on behalf of, Dole/Kemp '96.

In the Interim Audit Report, the Audit staff recommended that the MRSC provide documentation to demonstrate that the exemption at 11 CFR §100.8(b)(v) was not voided by the use of paid staff with respect to the MIGOP phone program and as a result the costs associated with the program are not contributions to Dole/Kemp '96.

In response to the report MRSC did not provide any additional documentation, but stated they were investigating the matter and were unable to accept or refute the findings.

B. SHARED EXPENSES PAID FROM NON-FEDERAL ACCOUNTS

Section 106.5(a)(2) of Title 11 of the Code of Federal Regulations requires committees that make disbursements in connection with both federal and non-federal elections to allocate expenses in the following categories:

Administrative expenses;

The direct costs of fundraising programs and events;

Activities exempt from the definition of contribution and expenditure at 11 CFR §§ 100.7(b) and 100.8(b); and,

Generic voter drives.

Section 106.5(g)(1) of Title 11 of the Code of Federal Regulations states, in part, committees that have established separate federal and non-federal accounts under 11 CFR 102.5(a)(1)(i) shall pay the expenses of joint federal and non-federal activities as follows: (i) pay the entire amount of an allocable expense from its federal account and transfer funds from its non-federal account to its federal account solely to cover the non-federal share of that allocable expense; or (ii) establish a separate allocation account into which funds from its federal and non-federal accounts shall be deposited solely for the purpose of paying allocable expenses. Once a Committee has established a separate allocation account for this purpose, all allocable expenses shall be paid from that account for as long as the account is maintained.

Section 104.10(b)(4) of Title 11 of the Code of Federal Regulations states, in part, a political committee that pays allocable expenses in accordance with 11 CFR 106.5(g) or 106.6(e) shall also report each disbursement from its federal account or its separate allocation account in payment for a joint federal and non-federal expense or activity.

The rules regarding the percentages to be used in the allocation of shared expenses for administrative and generic voter drives; exempt activities; and direct fundraising costs are described respectively under sections 106.5(d), (e) and (f) of Title 11 of the Code of Federal Regulations. Administrative and voter drive percentages are calculated on the ratio of the federal offices expected on the ballot to total federal and non-federal offices expected on the ballot in the next general election to be held in the committee's state. State and local party committees in states that do not hold federal and non-federal elections in the same year shall allocate the costs of generic voter drives according to the ballot composition method based on a ratio for that calendar year. Exempt activities are allocated according to the proportion of time or space devoted in a communication to federal candidates or elections as compared to the total time or space devoted in a communication to all federal or non-federal candidates or elections. Fundraising costs shall be allocated based on the ratio of funds received into a federal account to its total receipts from each fundraising program or event.

BACKGROUND

The Audit staff reviewed disbursements from both the federal and non-federal accounts during the audit period to evaluate compliance with 106.5(g) and to determine if the federal account paid its share of allocable expenses. From the federal accounts the MRSC expended funds for shared administrative, fundraising, and exempt activities, and in support of federal candidates. For the non-federal activity, 100% reviews of disbursements were performed on three separate accounts. One account was used by the MRSC as the non-federal operating account. This account supported non-federal candidates, transferred funds to the federal allocation account for shared activities,

and expended funds for a 1994 GOTV phone bank (see Shared Expenses Paid from the Non-federal Operating Account). The remaining two non-federal accounts were considered by the MRSC to be non-campaign accounts, composed mainly of corporate contributions. It is the opinion of the Audit staff that all three accounts were used to pay expenses which were, at least in part, shared expenses with the federal account. Thus it is clear that the MRSC makes disbursements in connection with both federal and non-federal elections and must allocate its administrative expenses pursuant to 11 CFR §106.5(a)(2).

1. Michigan Republican State Committee Administrative Account

The MRSC maintains an account entitled "Michigan Republican State Committee Administrative Account"². According to the MRSC, funds expended from the Administrative Account do not impact federal, state, or local elections. Therefore, it considers such transactions to be non-campaign related. Further, receipt and disbursement transactions are not included in its federal or state disclosure reports. The Administrative Account was open during the entire audit period (1995-1996).

The State of Michigan does not permit corporate or labor union contributions to be used for non-federal elections. However, on August 21, 1979, the Michigan Secretary of State issued a declaratory ruling concerning corporate expenditures at a state political party convention. A corporation proposed spending funds for expenses related to a state convention. The expenses included but were not limited to hotel rooms, food, beverages, telephone and travel, and were to be made for the purpose of influencing the decisions of the delegates to the convention with respect to the adoption of certain resolutions and the election of individuals to office within the state party. In part, the declaratory ruling stated that since none of the offices at stake at this particular convention were public offices and none of the resolutions to be adopted were ballot questions, the expenditures in question were not prohibited and also did not need to be reported or recorded as expenditures under the Act (reference to the state of Michigan law).

A Manual For Political Party Committees published by the Michigan Department of State Bureau of Elections, April 1990, commonly referred to as the "green book," at page 14 states political party committees may accept funds from an incorporated source if the corporation clearly designates the funds for the committee's administrative expenses. These funds must be deposited in a separate account maintained by the committee solely for administrative purposes. Finally, another manual published by the Michigan Department of State Bureau of Elections in February 1990, for independent political and ballot question committees, at page 8, states a Ballot Question Committee may receive corporate funds or be entirely funded by a corporation. At page 40 of this manual, it states a corporation is allowed to spend corporate funds to support or

² This account was open during the previous election cycle (93/94) and was reviewed during the FEC's audit of that period. Problems noted in that audit are similar to the problems noted herein.

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oppose ballot questions. The corporation must register a Ballot Question Committee within 10 calendar days after it spends \$500 or more in a calendar year to support or oppose ballot issues.

a. Overview of Expenditures

According to MRSC records, during the 1995-96 election cycle, as well as the previous cycle, expenses paid from the Administrative Account related to the annual Michigan Republican State Convention, Michigan Republican State Committee Meetings, conferences, and Republican National Committee State Chair Conferences. Such expenses included but were not limited to air travel, reimbursements for mileage, hotel costs, food, beverage, entertainment, supplies and invitations. During 1995 and 1996, a total of 625 checks amounting to \$1,059,348 were written from the Administrative Account.

From the Administrative Account the MRSC also paid for expenses such as legal fees to its general counsel for an unsuccessful defense of the MRSC in a libel suit brought against it by a former elected state official. Upon losing its case, the Administrative Account also posted the required bond for the amount of the settlement. Throughout 1995 and 1996, the Administrative Account paid the legal expenses related to Michigan Ballot Proposition A, an amendment to Michigan's Bingo Act, and paid the interest, fees and principle on non-federal loans. During 1995 and 1996 the Administrative Account also made transfers to the MRSC's building fund for mortgage payments, and sponsored receptions at the Governor's Mansion for high dollar donors and for a previous MRSC chairman. Certain other good will gestures and gifts were also not considered shared expenses. In all, the MRSC paid a total of 225 checks in the amount of \$626,703 for expenses which the Audit staff has deemed to be for solely non-federal activities.

b. Expenditures Apparently Related to Shared Federal and Non-Federal Activities

During the 1993-1994 election cycle, many of the disbursements from the Administrative Account were deemed to be for allocable expenses. A similar review of 1995-1996 disbursements produced a similar result. It is the Audit staff's opinion that during 1995 and 1996 the MRSC spent a total of \$271,150 for administrative expenses that require allocation between the federal and non-federal accounts. Included in this amount are payments for federal tax preparation and the annual audits of all MRSC accounts, monthly legal expenses incurred by the MRSC's legal counsel for items such as courier services and photocopying not directly related to any specific non-federal case and compensation in 1995 and 1996 to Gary Reed or Reed Governmental Consulting.³ Other expenditures included in this amount total

³ Based upon the audit of the 1993-1994 election cycle, Gary Reed was the fundraiser for the Account. In that audit, payments made to Gary Reed were considered shared activity.

approximately \$100,000 paid for such items as hotel bills, catering, and festivities costs related to the 1996 Republican National Convention in San Diego, California.

In addition to these administrative expenses, the Audit staff determined that funds from the Administrative Account were used to pay administrative expenses such as costs incurred for the annual state convention,⁴ various state committee and RNC chair meetings, and other conferences held in 1995 and 1996. The MRSC also paid administrative expenses related to its 1995 Mackinaw Conference. In all, the Administrative Account paid a total of \$142,423 (\$123,413 in 1995 and \$19,010 in 1996) in costs related to these events such as mileage reimbursements, banquet and lodging expenses, badge holders, supplies, and sound and lighting.

With respect to the state conventions, RNC chair meetings, conferences and state committee meetings it appears that campaign-related components (federal and non-federal) existed. For example, with respect to the 1995 annual state convention, an article in the *Detroit Free Press* notes:

The attack began on Feb 4th, the day Heintz was elected state chair at a GOP convention at Cobo Hall. In an alliterative burst that brought cheers from delegates, she labeled Bonior “a whiney, wacky, wimpy, wasteful, worn-out, washed-up, windbag wimp” and promised that he’ll “take the biggest fall.”

Although the MRSC apparently considers this convention to be non-campaign related, according to this article, federal election activity was of major interest during the Convention. In May of 1996, Susan Heintz would resign her position as the Chairman of the MRSC and run against Bonior in the election for the 10th District Congressional seat. As concerns the 1995 Mackinaw conference, other articles reviewed stated that then Speaker of the House Newt Gingrich was a speaker and the conference was attended by then-Republican Presidential Primary candidates Bob Dole, Pete Wilson, Phil Gramm and Arlen Specter. At a minimum it appears that these administrative expenses were in connection with both federal and non-federal elections. As a result, the costs must be allocated between the federal and non-federal accounts. The proper allocation ratio is the ballot composition method specified at 11 CFR §106.5(d).

Based upon our review, the expenses noted above (general operating expenses - \$271,150; state conventions and committee meeting/conferences - \$142,423) relate to shared federal and non-federal activities and are allocable as administrative expenses. The Audit staff calculated that \$155,090 [(\$271,150 +

⁴ It should be noted that the Audit staff requested agendas for State committee meetings on two occasions, but to date, the agendas have not been forthcoming.

\$142,423) x 37.5%⁵] represents the federal share and requires repayment to the non-federal account. At the Exit Conference the Audit staff provided MRSC officials with schedules that detailed the review of this account. A MRSC official stated that the Mackinaw conference consists of a State meeting on Friday night and that the rest of the weekend is typically social. The representatives had no other comments with regard to the other categories of expenditures.

2. Shared Expenses Paid from the Non-Federal Operating Account

The Audit staff's review of the non-federal operating account (Operating Account) disclosed 86 payments totaling \$10,951 made to various businesses on June 5, 1995. These payments were reimbursements for the use of telephones for get-out-the-vote (GOTV) activities during 1994. During a previous election cycle, the MRSC operated a similar GOTV phone bank, but at that time had reimbursed the businesses from both the federal and non-federal accounts.

At the time of the review and at the Exit Conference, the Audit staff requested a copy of the script for this phone bank so that a determination could be made as to possible allocable activity. To date, the MRSC has not provided the requested documentation.⁶ Absent documentation to prove otherwise, the Audit staff considers the payments to be for shared activity benefiting both federal and non-federal candidates. The federal share of this activity would be \$2,431 ($\$10,951 \times 22.2\%$ ⁷).

3. Shared Expenses Paid from the Non-Federal Account, Republican National Convention

The MRSC opened a non-federal account, Republican National Convention (Convention Account), on February 16, 1996. During 1996 the Convention Account received \$90,300 and made disbursements totaling \$78,538 for expenses associated with activities during the Republican National Convention in San Diego, CA.

Although some receipts were designated as deposits for hotel rooms during the convention, and some receipts were from individuals, the bulk of the receipts were from corporate entities. Contributions from one of the corporate sponsors were made under the specific conditions that the donations would support functions held solely for social purposes, no attempt would be made to influence the outcome of the convention or to advocate the election or defeat of any candidate, and would not be used to defray any delegate's subsistence expenses. Correspondence and annotations

⁵ The allocation percentage for administrative expenses is 37.5%. The percentage is the ratio of federal offices to total federal and non-federal offices on the ballot in the 1996 general election.

⁶ The script provided for the 1992 GOTV activity urged voters to support, among other Republicans, President George Bush.

⁷ Since these disbursements relate to the 1993-1994 election cycle, the 22.2% administrative allocation ratio for that period is applied here.

associated with other contributions included phrases such as "House Republican event at the National Convention," "RNC Michigan House Reception," "Michigan delegation luncheon," "toward the activities at the National Republican convention" or "for San Diego Convention." Many contributions included no discernible purpose; these receipts were generally payable to "Republican National Convention Michigan Account."

Expenses paid from this account included consultant fees, room deposits, travel reimbursements, entertainment and reception expenses, printing costs, radio rentals, teleprompter, supplies, and bus transportation. Invoice and receipt documentation indicate that the Convention Account funded catering and entertainment expenses for at least three events between August 11 and August 13. Transportation for the Michigan delegation was funded by the account for a fourth event on August 11. Souvenirs or gifts paid for from this account included 550 picture frames with engraved plaques reading "1996 Republican National Convention," 550 printed items described as "96 Convention Program," 550 printed T-shirts, and printed beach towels. The Convention Account also paid for the design of a national convention logo. Other printing costs included invitations to four events/receptions. Included within travel reimbursements was a \$968 payment for hotel expense to a person listed as a delegate to the Republican National Convention. Finally, the Convention Account paid shipping costs for material sent from MRSC to "1996 Rep[ublican] Nat[ional] Conv[ention] - Youth Programs."

The Audit staff provided the MRSC with a schedule of disbursements from this account at the Exit Conference and requested that the MRSC justify the non-federal nature of the expenditures. The MRSC official had no comment at that time.

In response to the Exit Conference, the MRSC asserted that the functions were sponsored by corporations "...to meet with Republican National Convention delegates, federal and state elected officials, Republican Party officials, and the press. No part of any function paid for from the Republican National Convention Account was used to attempt to influence the outcome of the Convention, for official Convention events, for soliciting contributions, or for expressly advocating the election or defeat of a candidate for Federal office. Further, none of the functions sponsored by the corporations contributing to the Republican National Convention Account had as its purpose the defrayal of any delegate's subsistence expenses during the Convention."

As with some of the expenses discussed above, these costs, at a minimum, represent general party activity and/or party building. Although there is no evidence that specific disbursements are related solely to State and local elections, solely to Federal elections, or that any candidate's election or defeat was advocated, the expenditures were made for party sponsored events held in conjunction with a National Nominating Convention which selected a federal candidate. Therefore, at a minimum, these expenses must be allocated between the federal and the non-federal accounts as

party administrative expenses. The Audit staff calculated the federal share of this activity to be \$29,452 (\$78,538 x 37.5%), based on the allocation ratio for administrative activity.

In the Interim Audit Report, the Audit staff recommended that the MRSC:

- Demonstrate that the disbursements originating from the Administrative Account (\$413,572), the Operating Account (\$10,951), and the Convention Account (\$78,538) are not expenditures as defined at 11 CFR §100.8(a); or,
- file Schedules H4 disclosing as memo entries the shared expenditures which originated from these accounts (\$503,061); and
- using funds from its federal account(s) reimburse the non-federal account \$183,353 [(\$413,572 x 37.5%)+(\$78,538 x 37.5%)+(\$10,951 x 22.2%)-\$3,619⁸] and provide evidence of such reimbursement.
- If the MRSC lacks the funds to reimburse the non-federal account, then disclose the amount owed on Schedule D as a debt.

As part of its response to the recommendations contained in the Interim Audit Report, the MRSC explains that the Michigan Campaign law excludes party administrative expenses from its coverage, and suggests that the same is true under Federal law. Included in the MRSC response is a discussion of various Advisory Opinions issued by the Commission. The MRSC correctly pointed out that in Advisory Opinion 1982-14, the Commission concluded that the influencing of the reapportionment decisions of a state legislature, although a political process, is not considered election-influencing activity subject to the requirements of the Act. Also referenced was Advisory Opinion 1993-9 which addressed the proposal to establish a building fund, maintained as a "separate segregated" account into which only designated contributions would be deposited. Also, included was a reference to Advisory Opinion 1983-37 in which the Commission determined that the Massachusetts Democratic State Committee could establish a fund that would not be subject to the Act's limitations, prohibitions, or disclosure requirements. The monies in this fund could be used only for the purpose of defraying legal costs of defending legal actions brought by candidates against the Massachusetts Democratic State Committee and would have to be maintained separately from funds used for federal elections. Finally, the MRSC cited Advisory Opinion 1996-39 in which the Commission determined that a legal fund could defer expenses of defending the legal sufficiency of the nominating petitions qualifying a candidate for the primary election ballot.

⁸ This amount represents a net under reimbursement by the non-federal accounts for other administrative and fundraising expenses.

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Using the above cited opinions, and the analogy to Michigan law, MRSC concludes that the FEC has determined that such activities do not influence any Federal election to trigger compliance with the FECA. Therefore the above cited activity is beyond the scope of the FECA. The MRSC contends that, with the exception of certain items, "the disbursements from the Account are not made for the purpose of influencing any election for Federal office."

Although MRSC may be correct with respect to Michigan law, Federal law takes a different view. The Act, Commission regulations, and past Advisory Opinions exclude from coverage specific types of expenses, and only those. Coverage of the Act goes beyond those things that meet the definition of an "expenditure". Section 434(b)(4) of Title 2 of the United States Code states that political committees are required to report for the reporting period and for the calendar year the total amount of all **disbursements** and all **disbursements** in a number of categories. Likewise, the requirement that certain transactions be individually itemized on the disclosure reports of committees such as MRSC speaks in terms of disbursements. Most relevant to this situation, Commission regulations also use the term disbursement when speaking about the need to allocate expenses between federal and non-federal accounts for those committees that, as MRSC does, fund activity in connection with both federal and non-federal elections. Section 106.5 of Title 11 of the Code of Federal Regulations, Allocation of expenses between federal and non-federal activities by party committees, uses the terms disbursements, costs, and expenses rather than expenditure. Therefore, the fact that many of the disbursements discussed above do not, in the opinion of MRSC, meet the definition of expenditure, is not relevant to the need for allocation between the federal and non-federal accounts.

The response then addressed specific types of expenses paid from the Administrative Account in an effort to demonstrate that the payments questioned in the Interim Audit Report were not subject to the requirements of the Act.

Conventions, Meetings, And Conferences

The Audit staff identified \$142,423 in expenses associated with the annual state convention, various committee meetings and conferences which appeared to require allocation between the MRSC's federal and non-federal accounts as administrative expenses. In addition, evidence gathered establishes that there was at least some federal content at many of the events. The MRSC, in its response, asserted that the Audit Division preliminarily determined that these expenses were made for the purpose of influencing an election for federal office based on newspaper articles. Citing *Common Cause v FEC*⁹ and various Michigan campaign finance law cases, the MRSC argues that the FEC should ignore second hand accounts in newspaper articles as reliable evidence that the MRSC conducted electioneering activity during the conventions, meetings, and conferences. Clearly, newspaper articles are not the evidentiary material of choice.

⁹ No. 85-968, Slip Op. (D.D.C. June 25, 1986) reprinted in Federal Election Campaign Finance Guide (CCH), ¶9235.

However, requests for materials from the MRSC produced nothing and the newspaper accounts of the proceedings at some of the meetings and events were the only available information. It is significant that the MRSC response did not dispute any of the newspaper accounts referenced in the Interim Audit Report. Finally, the newspaper accounts were used only to establish that the events were not entirely focused on non-federal efforts. In many cases the costs of the events are allocable as administrative expenses.

The MRSC cited numerous court cases establishing the “express advocacy” test. It also refers to the interim report where the audit staff cites “federal election activity was of major interest during the Convention” and the activities benefit the Party as a whole and therefore have both federal and non-federal components. The MRSC suggests that the “major interest” and the “benefit the Party as a whole” standard does not replace the “express advocacy” test. The relevant requirements are in 11 CFR 106.5 that require committees that make disbursements in connection with both federal and non-federal elections to allocate expenses in various categories including administrative expenses.

Next MRSC contended, based on its reading of the Advisory Opinion 1978-46, that unless there is fundraising related to a campaign for Federal office or any communication expressly advocating the election or defeat of a clearly identified candidate for Federal office, the activity and attendant expenses cannot be regarded as for the purpose of influencing a Federal election. MRSC concludes that the lack of fundraising and electioneering at internal political party gatherings, the expenses associated with the State Convention, MRSC meetings, and conferences, are not “expenditures” for the purpose of the FECA.

The test that MRSC references may be relevant to the determination of whether certain expenditures are contributions to specific candidates for Federal office, but not to whether a disbursement is an administrative expense or a generic voter drive expense which includes activities that urge the general public to register to vote, vote or support candidates of a particular party, or associated with a particular issue without mentioning a specific candidate. These types of expenses require reporting and allocation between the federal and non-federal accounts without the express advocacy and clearly identified candidate test having been met.

MRSC also cites Advisory Opinions 1986-6, 1982-35, 1983-37, to support the proposition that internal political party gatherings, even though they may directly influence Federal elections, are not subject to the FECA. According to MRSC, in the present situation, there is no allegation, nor can there be, that the State Convention, MRSC meetings, and conferences, all of which are internal political party gatherings, somehow influenced Federal elections.

Most of the advisory opinions cited by the MRSC were issued by the Commission prior to the effective date (January 1, 1991) of the Commission’s

regulations for allocating expenses that jointly benefit both federal and non-federal candidates and elections.¹⁰ As noted above, these regulations provide for the allocation of expenses by political party committees that make disbursements in connection with both federal and non-federal elections. The allocable expense categories include administrative expenses, fundraising costs, exempt activities expenses, and the cost of generic voter drives. More specifically, party committees that make disbursements in connection with federal and non-federal elections shall allocate expenses for administrative expenses not attributable to a clearly identified candidate, including rent, utilities, supplies, and salaries. Advisory Opinion 1993-21. The Commission's Explanation and Justification for 11 CFR §106.5 contains the following guidance regarding administrative expenses:

“Please note that all administrative expenses must be allocated between federal and non-federal accounts, if incurred by a committee that makes disbursements in connection with both federal and non-federal elections, and that chooses to pay any portion of such disbursements from its non-federal account.”

The \$142,423 in expenses for various meeting and conferences questioned in the Interim Audit Report do fall into the general category of administrative expenses and therefore are subject to the requirements of the Act. Further as explained above, based on the information available, the events had federal as well as non-federal components. These types of expenses were also allocated by the Commission in the audit report covering the 1993 and 1994 election cycle.

Audit And Legal Expenses

With respect to the audit expenses questioned in the Interim Audit Report (\$30,167), the MRSC contended that payment of such expenses are subject to the Act only in the case where they (1) directly further the election of any designated candidate for Federal office, or (2) assist the political committee in its compliance with the Act. According to the Committee, “the purpose of the audits is ... to verify to the officers and members of the MRSC that the financial statements are appropriately stated and that the MRSC staff is conforming with generally accepted accounting principles.” The Committee then concluded, there is no basis to designate payments from the Account for these audit expenses as subject to the Act.

Expenses related to an audit of Committee accounts, both federal and non-federal, fall clearly into the administrative expense category, and pursuant to 11 CFR §106.5 (a)(2)(i) are allocable between the federal and non-federal accounts.

¹⁰ Advisory Opinions 1992-5 (candidate's participation in a series of public affairs forums), 1993-9 (preemption of Michigan State law with respect to the prohibitions on corporate donations to the Michigan Republican State Committee's building fund), 1996-39 (legal fund could defer expenses in defending legal sufficiency of nominating petitions) were issued after 1/1/91.

Regarding legal expenses questioned by the Audit staff (\$8,123), the Committee restated the two factors cited with respect to audit expenses and added a third - are associated with compliance or audit matters under the Act. The Committee cited examples of legal expenses which the Commission determined as not subject to the requirements of the Act, such as legal defense: (1) to a charge of slander; (2) civil action alleging violation of the Appropriations Act, Hatch Act, an infringement of constitutional rights; (3) and a congressman charged with both criminal conduct and violations of rules of the House of Representatives.¹¹ In addition, according to MRSC the FEC in Advisory Opinion 1990-6 acknowledged that state laws concerning manner of qualification of candidates, dates and places of elections, voter registration, voting fraud and candidates' personal financial disclosure are outside the scope of the FECA.

The MRSC's General Counsel states that he reviewed the reimbursed legal expenses questioned by the Audit staff and to the best of his knowledge an insignificant amount of reimbursed expenses could qualify as 'expenditures,' which he estimated to have been, at most, 5% or \$406 which should be reimbursed from the federal account. The remainder, \$7,717, in reimbursed expenses did not concern federal candidates or the Act. No documentation beyond an affidavit signed by the Committee's General Counsel was provided.

While it is true the Commission, in advisory opinions, has concluded that certain types of activity and the legal expenses related thereto are not subject to the Act's recordkeeping, reporting and other requirements, the type of activity was clearly defined (e.g., a possible denial of access to the primary ballot of the state of Massachusetts involving a party rule, AO 1982-35). Moreover, for such activity a segregated fund would have to be established and maintained apart from other political committee funds. For example in Advisory Opinion 1983-37, the Commission concluded that "[t]o the extent monies in the fund will be used only for the purposes described, and will be maintained separately from funds used for Federal elections, the Party's legal expense fund would not be subject to the Act's limitations ..."

Given the expenses at issue, totaling \$38,290, are not identified or documented as being for a purpose indistinguishable from any approved by the Commission, the Audit staff views the expenses as administrative expenses, and like the audit expenses discussed above, subject to the requirements of the Act and Commission regulations.

The MRSC presented almost identical explanations for these types of expenses when questioned in the audit report covering the 1993 and 1994 election cycle. The Commission determined that those expenses were allocable between the federal and non-federal accounts.

¹¹ The Committee cited Advisory Opinions 1981-13, 1980-4, and 1979-37.

Fundraising For The Administrative Account

The Committee conceded that since certain disbursements from the Administrative Account were mistakenly made and constitute expenditures under the Act, a certain percentage of the fundraiser's salary should be reimbursed from the Committee's federal account to the Administrative Account. The MRSC made payments for the fundraiser's salary of \$2,675 and calculated that 5.3% or \$142 should be reimbursed from the federal account. MRSC used the ratio of the fundraiser's salary to the total expenditures made from the Administrative Account to determine this percentage.

The fundraiser's salary should not be allocated based on a ratio of federal expenditures to all expenditures from the Administrative Account. As a result, the Audit staff's considers the entire amount of the fundraiser's salary (\$2,675) a shared administrative expense. These fundraising expenses, as well as all other allocable expenses discussed above should not have been paid from the Administrative Account.

Again, the MRSC presented the same explanation for these expenses in the audit report covering the 1993 and 1994 election cycle, which were also determined allocable by the Commission.

Lobbying

MRSC paid Reed Governmental Consulting, Inc. \$20,904 in 1995 and \$25,000 in 1996. According to MRSC the compensation for Gary Reed's fundraising efforts was different than the compensation paid to Reed Governmental Consulting, Inc.. The payments to Reed Governmental Consulting, Inc. were for lobbying and not electioneering. MRSC cites Advisory Opinions 1978-36 and 1983-4, to support that the FEC recognizes that lobbying expenses are not expenditures under the FECA.

Again, the advisory opinions cited by the MRSC were issued by the Commission prior to the effective date (January 1, 1991) of the Commission's regulations for allocating expenses that jointly benefit both federal and non-federal candidates and elections.

Holiday Cards, Gifts, And Miscellaneous

The MRSC asserted that 42 expenses for holiday cards, gifts, charities, State committee meetings, social events at the 1996 National Convention, staff social functions, and similar types of expenses, totaling \$164,472 do not constitute expenditures under the Act. The reasoning for this position apparently is that these expenses were not campaign related.

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The Audit staff reviewed the MRSC's specific explanations and documentation relating to these disbursements and allowed that seven items totaling \$19,129 were disbursements for transfers to the non-federal Republican National Committee (\$10,100), the non-federal Victory Council (\$5,500), payments for non-federal legal issues (\$1,989), a cancellation fee for an event (\$900), and payment for the non-federal Campaign Managers Academy (\$640). The disbursements to charitable organizations were in payment for ads. The other expenses, in the Audit staff's opinion, are also classified properly as administrative expenses. The adjustment to the amount owed the federal committee is thus reduced by \$7,173 ($\$19,129 \times 37.5\%$), leaving \$394,443 ($\$413,572 - \$19,129$) as administrative expenses paid from the Administrative Account and a reimbursable amount of \$147,917 ($\$155,090 - \$7,173$) for disbursements from this account.

As explained above, party committees that make disbursements in connection with federal and non-federal elections shall allocate expenses for administrative expenses not attributable to a clearly identified candidate, including rent, utilities, supplies, and salaries. Advisory Opinion 1993-21. The types of administrative expenses cited are illustrative and cannot be viewed as inclusive.

As stated, it is the opinion of the Audit staff that expenditures for activities such as independent reviews of committee accounts, staff salaries, staff outings, holiday cards, gifts, etc., clearly fall within the general category of "administrative expenses" as noted at 11 CFR §106.5 (a)(2)(i).

Expenditures Not Being Challenged by MRSC

MRSC acknowledged that there were additional expenditures totaling \$55,612 which relate to shared federal and non-federal activities at the administrative ratio (37.5%). The MRSC also acknowledged the previously mentioned \$406 in legal expenses and \$142 in fundraising expenses from Mr. Reed's salary that should be reimbursed from the federal account. The MRSC calculated the total amount owed by the federal account as \$21,402 ($(\$55,612 \times 37.5\%) + \$406 + \$142$). As an act of good faith MRSC's federal account reimbursed this amount to the Administrative Account. A copy of the check and deposit receipt was included with the response.

Shared Expenses Paid from the Non-Federal Operating Account

MRSC did not respond to section II.B.1.b.2. of the Interim Audit Report, which discussed expenses for telephone bank expenses related to the 1994 election. It also did not provide the copy of the requested telephone script. Therefore, the Audit staff is still of the opinion that the federal share of this activity is \$2,431.

Payments from the Republican National Convention Account

MRSC reasserted most of what was stated in the response to the Exit Conference. It argues that the receptions or hospitality suites were held solely as social functions for individuals in the San Diego area attending the Convention and were not an attempt to influence the outcome of the Convention, or to solicit contributions, or to advocate the election or defeat of any candidate. At each function the corporate sponsor was prominently listed and not the MRSC. The MRSC also disagreed with the reference to these activities as "party sponsored events". According to MRSC these events were not general party-building, but were social functions sponsored by "named corporations" and the events are substantially similar to the circumstances addressed by the Commission in Advisory Opinion 1983-23.

Again, the advisory opinions cited by the MRSC were issued by the Commission prior to the effective date (January 1, 1991) of the Commission's regulations for allocating expenses by committees that make disbursements in connection with both federal and non-federal candidates and elections. The National Nominating Convention selects a federal candidate, and therefore any general party sponsored function in connection with that federal election must, at a minimum, be allocated between the federal and non-federal accounts at the administrative (ballot composition) ratio. The MRSC's contention that the events at the Convention were social functions is not relevant to the requirement that the associated expenses be allocated. It is still the Audit staff's opinion that the federal share of this activity is \$29,452 ($\$78,538 \times 37.5\%$), based on the allocation ratio for administrative expenses.

In conclusion the MRSC did not comply with the recommendations in the Interim Audit Report. It did make a partial reimbursement to the non-federal account of \$21,402, and the Audit staff agrees that \$7,173 represents solely non-federal expenses and are not allocable. MRSC should still reimburse the non-federal account \$154,778 ($\$183,353 - \$21,402 - \$7,173$).

C. REPORTING AND ITEMIZATION OF RECEIPTS AND DISBURSEMENTS

1. Transfers from Non-Federal to Federal Account and Related Disbursements

Sections 106.5(g)(1)(i), (ii)(A), and (3) of Title 11 of the Code of Federal Regulations state, in part, committees that have established separate federal and non-federal accounts under 11 CFR 102.5(a)(1) or (b)(1)(i) shall pay the entire amount of an allocable expense from its federal account and transfer funds from its non-federal account to its federal account solely to cover the non-federal share of that allocable expense; or shall establish a separate allocation account into which funds from its federal and non-federal accounts shall be deposited solely for the purpose of paying the allocable expenses of joint federal and non-federal activities. A political committee that transfers funds between accounts and pays allocable expenses according to this section shall report each such transfer and disbursement pursuant to 11 CFR 104.10(b).

The MRSC did not disclose on Schedule H3 (Transfers from Non-Federal Accounts) transfers from its non-federal checking account to its federal payroll account for non-federal payroll. These transfers totaled \$284,919 (\$88,291 in 1995 and \$196,628 in 1996). In addition, the MRSC did not report the related payroll disbursements totaling \$284,919 on Schedule H4 (Joint Federal/Non-Federal Activity Schedule). Although these payments were for non-federal payroll, because the payments were made from a MRSC federal account they require disclosure. During fieldwork the MRSC was unable to provide a complete list of the non-federal personnel and could not detail their duties for the 1995-1996 election cycle.

In addition, the MRSC did not itemize on Schedule H3 transfers from the non-federal operating account to the federal allocation account for the non-federal share of several disbursements to vendors. These under-reported transfers totaled \$520 in 1995 and \$633,719 in 1996. The 1996 disbursements were payments to Multi Media Services and Strategic Media Services. Finally, the MRSC failed to report on Schedule H3 the non-federal share of in-kind transfers received from the Republican National Committee in 1996. The non-federal share of these transfers totaled \$12,745.

2. Receipts from Political Committees and Interest

Section 434(b)(2)(D), (F) and (J) of Title 2 of the United States Code states, in part, that each report under this section shall disclose for the reporting period and calendar year the total amount of all contributions from other political committees, transfers from other political party committees, and interest.

Section 434(b)(3)(A) and (B) of Title 2 of the United States Code states that each report shall disclose the identification of each person (other than a political committee) who makes a contribution to the reporting committee during the reporting period, whose contribution or contributions have an aggregate amount or value in excess of \$200 within the calendar year, or in any lesser amount if the reporting committee should so elect, together with the date and amount of any such contribution. Each report shall also disclose any political committee which makes a contribution to the reporting committee during the reporting period, together with the date and amount of any such contribution.

The Audit staff reviewed receipts and determined that the MRSC failed to report and itemize, as required, four contributions from political committees in 1995 totaling \$3,240 and two contributions from political committees in 1996 totaling \$1,200. In 1996 the MRSC also failed to report and itemize the federal share of in-kind transfers from the Republican National Committee totaling \$7,647. Finally, the MRSC failed to report and itemize interest receipts totaling \$12,271.

3. Disbursements - Operating Expenditures, In-Kind Contributions, Transfers, and Independent Expenditures

Sections 434(b)(4)(A) and (C) and (5)(A) and (C) of Title 2 of the United States Code state, in part, that each report shall disclose for the reporting period and the calendar year: the total amount of all expenditures made to meet candidate or committee operating expenses; the total amount of all transfers to affiliated committees; the name and address of each person to whom an expenditure in an aggregate amount or value in excess of \$200 within the calendar year is made by the reporting committee to meet a candidate or committee operating expense, together with the date, amount and purpose of such operating expenditure; and the name and address of each affiliated committee to which a transfer is made, together with the date and amount of such transfers.

Section 104.10(b)(4) of Title 11 of the Code of Federal Regulations states, in part, that a political committee that pays allocable expenses shall also report each disbursement from its federal account or its separate allocation account in payment for a joint federal and non-federal expense or activity. In the report covering the period in which the disbursement occurred, the committee shall state the full name and address of each person to whom the disbursement was made, and the date, amount and purpose of each such disbursement.

The Audit staff review of disbursements determined that, in addition to the non-federal payroll discussed above, the MRSC failed to report and itemize bank charges and disbursements to vendors totaling \$13,601 in 1995 and \$742,861 in 1996. The disbursements in 1996 included two payments to Multi Media Services (\$722,470) for which the H3 transfers were underreported by \$451,657. The other disbursements in 1996 (seven totaling \$20,391) represent the required disclosure of disbursements relating to in-kind contributions by the Republican National Committee.

The MRSC failed to report and itemize one transfer for \$3,300 in 1995 and three transfers totaling \$10,200¹² in 1996 to the non-federal account. Finally, a transfer for \$36,000 to the Republican National Committee was not reported or itemized as required in 1995.

Lastly, the MRSC failed to itemize on Schedule E (Itemized Independent Expenditures) a disbursement for \$80,842 on behalf of a federal candidate. The Schedule E also requires notarization.

At the Exit Conference the Audit staff provided to the MRSC schedules which detailed the reporting omissions discussed above for each line number of the disclosure reports. The MRSC officials agreed to amend the 1995 and 1996 reports to disclose correctly the receipts and disbursements noted above.

In the Interim Audit Report it was recommended that the MRSC file amended Schedules A, B, E, H3, and H4 for the calendar years 1995 and 1996

¹² One \$5,000 transfer was related to a \$5,000 receipt from an individual which was deposited by mistake into the Federal account. Neither the receipt nor the transfer was reported.

disclosing the contributors, transferors, payees, transferees, dates and amounts for the receipts, payments and transfers discussed above.

In response to the Interim Audit Report, the MRSC filed all Schedules as recommended.

D. MISSTATEMENT OF FINANCIAL ACTIVITY

Section 434(b)(1)(2) and (4) of Title 2 of the United States Code states, in part, that a political committee shall disclose the amount of cash on hand at the beginning of the reporting period and the total amount of all receipts and all disbursements for the reporting period and calendar year.

The Audit staff's reconciliation of reported financial activity to bank records for the calendar years 1995 and 1996 revealed the following misstatements:

1. 1995 Misstatement

Beginning cash on hand was overstated by \$72,858, the result of reporting discrepancies in prior periods.¹³

Receipts were understated by \$91,495. The components of the misstatement are as follows:

Reported Receipts		\$3,064,747
Contributions from Political Committees not reported	\$ 3,240	
Transfers from non-federal account to federal payroll account not reported	\$88,291	
Transfer from non-federal account to federal allocation account not reported	\$ 520	
Reconciling item	<u>\$ (556)</u>	
Total Adjustments		<u>\$ 91,495</u>
Correct reportable receipts		<u>\$3,156,242</u>

Disbursements were understated by \$127,162.06. The components of the misstatement are as follows:

Reported disbursements		\$2,724,634
Non-federal salaries paid from allocation account	\$ 88,291	
Transfer to RNC not reported	\$ 36,000	
Transfer to non-federal account not reported	\$ 3,300	
Payments to vendors and bank charges not reported	\$ 10,695	
Payments to Ameritech over-reported (net)	\$ (11,201)	

¹³ The overstatement of beginning cash is the combined effect of reporting errors within beginning cash in 1993 and receipts and disbursements in 1993 and 1994.

Reconciling item	\$ 77	
Total Adjustments		\$ 127,162
Correct reportable		<u>\$2,851,796</u>

Ending cash on hand was overstated by \$108,524, resulting from the misstatements detailed above. The correct ending cash was \$407,446.

2. 1996 Misstatement

Beginning cash on hand was overstated by \$108,524, carried forward from 1995.

Receipts were understated by \$864,068. The components of the misstatement are as follows:

Reported receipts		\$5,686,069
Transfers from non-federal account to payroll account not reported	\$ 196,628	
Transfers from non-federal account to allocation account for payments to Multi Media Services not reported	\$ 451,657	
Transfer from non-federal account to allocation account not reported for payment to Strategic Media Services	\$ 182,062	
Interest not reported	\$ 12,271	
In-kind contributions from RNC not reported	\$ 20,391	
Contribution from an individual not reported	\$ 5,000	
Contributions from Political Committees not reported	\$ 1,200	
Reconciling item	<u>\$ (5,142)</u>	
Total Adjustments		\$ 864,068
Correct reportable		<u>\$6,550,135</u>

Disbursements were under-reported by \$949,596. The components of the misstatement are as follows:

Reported disbursements		\$5,982,298
Payments to Multi Media for media buys featuring Bob Dole in cooperation with the Republican National Committee	\$ 722,470	
Non-federal salaries paid from allocation account	\$ 196,628	
Transfers to non-federal account under-reported	\$ 10,200	
Interaccount transfer reported as disbursement	\$ (1,861)	
In-kind contributions not reported as disbursements	\$ 20,391	
Reconciling item	<u>\$ 1,768</u>	
Total Adjustments		\$ 949,596
Correct reportable		<u>\$6,931,894</u>

Ending cash on hand was overstated by \$194,054, resulting from the reporting errors detailed above. The correct ending cash was \$25,687.

At the Exit Conference the MRSC was provided schedules which detailed the reporting errors discussed above. MRSC officials agreed to file amended reports to correct the errors noted above.

The Interim Audit Report called for the MRSC to file comprehensive amended reports for calendar years 1995 and 1996 correcting the misstatements noted above. In addition, it was recommended that the MRSC amend its most recently filed report to correct the ending cash on hand.

The MRSC filed the requested comprehensive amended reports for calendar years 1995 and 1996 which corrected the misstatements. On March 21, 2000 the Committee filed an amended summary page for the 1999 Year End Report to correct the ending cash on hand.

02.07.05.2964



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

February 28, 2000

MEMORANDUM

TO: Robert J. Costa
Assistant Staff Director
Audit Division

THROUGH: James A. Pehrkon
Staff Director

FROM: Lawrence M. Noble
General Counsel

BY: Kim Leslie Bright
Associate General Counsel

Lorenzo Holloway
Assistant General Counsel

Susan L. Kay
Attorney

Dawn Anderson
Legal Intern

SUBJECT: Proposed Final Audit Report on Michigan Republican State Committee
(LRA #523)

I. INTRODUCTION

The Office of General Counsel has reviewed the proposed Final Audit Report for the Michigan Republican State Committee ("the Committee") submitted to this Office on January 24, 2000. The following memorandum summarizes our comments on the proposed Report.¹ We concur with the findings in the proposed Report that are not discussed in the following memorandum. If you have any questions, please contact Susan Kay, the attorney assigned to this audit.

¹ The Office of General Counsel recommends that the Commission consider this document in open session since the report does not include matters exempt from public disclosure. See 11 C.F.R. § 2.4.

II. MEDIA EXPENDITURES

The Audit Division has included information in the proposed Report that relates to payments made by the Committee to certain media vendors for advertisements broadcast during the 1996 election cycle. The Audit Division considered these advertisements to be in-kind contributions by the Republican National Committee ("RNC") to Dole for President, Inc. ("DFP") in the context of the DFP audit. According to information available to the Audit Division, and included in the DFP Audit Report, the RNC transferred funds to state party committees including the Michigan Republican State Committee. According to the Audit Division, the RNC transferred to the Committee's accounts the exact amount reflected on invoices from media vendors just prior to each payment by the Committee. The Audit staff has not included a finding against the Committee related to these disbursements in view of the position taken by the Commission with respect to these advertisements in the DFP audit and in other recent decisions by the Commission. While it is appropriate to include this summary of the issue in the Report of the Committee so that the Report is complete and accurate, this issue is no longer being considered by the Commission in any context. Therefore, this Office recommends that the Audit Division raise with the Commission the question of the advisability of including a discussion of this issue in the pending audit report. See Memorandum to Robert J. Costa on Media Advertisement Issues in Pending Audits, dated February 18, 2000.

III. SHARED EXPENSES PAID FROM NON-FEDERAL ACCOUNTS (Finding II.B.)

A. Administrative Account (II.B.1)

The cover memorandum to the proposed Final Audit Report directs this Office's attention to the issue of shared expenses from the Committee's administrative account. The Committee maintained a non-federal account, the Michigan Republican State Committee Administrative Account ("Administrative Account"). The Audit Division contends that the Committee made expenditures for federal activity from this account and these expenditures should have been shared between federal and non-federal accounts pursuant to 11 C.F.R. § 106.5.²

The expenditures at issue include \$271,150 for expenses such as payments for federal tax preparation and the annual audits of all committee accounts, monthly legal expenses incurred by the Committee's legal counsel for courier services and

² According to the Audit staff, similar disbursements made by the Committee during the 1993-1994 election cycle were deemed to have been allocable expenses. The Committee made the same arguments in response to the earlier audit and the Audit staff rejected those arguments in the 1993-94 Final Audit Report which was approved by the Commission on February 9, 1999. The Audit staff maintains its position that the Committee must allocate disbursements from this account. The Audit staff also identified shared expenses from two other non-federal accounts.

photocopying, compensation to a Gary Reed or Reed Governmental Consulting, and hotel bills, catering and festivities costs related to the 1996 Republican National Convention in San Diego, California. In addition to these expenses, the Audit staff determined that funds from this account in the amount of \$142,423 were used to pay for the annual state convention, various state committee and RNC chair meetings and other conferences held in 1995 and 1996, including the 1995 Mackinac Conference.

The Committee maintains that this is a non-campaign account and not subject to the Federal Election Campaign Act ("FECA") because the funds in the account were not spent for the purpose of influencing any election for Federal office or for the purpose of influencing the nomination or election of a state candidate. In support of its argument that the Administrative Account was a non-campaign account, not subject to the FECA, the Committee references Commission advisory opinions that allow for the establishment of specific non-campaign accounts in which funds may be maintained that are not subject to the FECA. *See* Advisory Opinion ("AO") 1982-14 (Commission determined that receipts and disbursements from a reapportionment account would not constitute contributions or expenditures since influencing reapportionment decisions is not considered election-influencing activity subject to the FECA), AO 1983-37 (Commission determined that a legal defense fund could be maintained so long as it was maintained separately from funds used for federal elections); AO 1993-9 (Commission held that creating a building fund is not done for the purpose of influencing an election)³; AO 1996-39 (Commission determined that a legal fund could be established for purposes of defending the legal sufficiency of the nominating petitions qualifying a candidate for the primary election ballot). According to the Committee, its Administrative Account did not make expenditures for the purpose of influencing a federal election, and therefore it is entitled to the same status as a building fund account, a reapportionment account or a legal defense fund account, all of which have been approved by the Commission.

The Commission has concluded, in the context of advisory opinions, that certain types of activities and legal expenses are not subject to the requirements of the FECA. *See* AOs: 1982-14, 1983-37, 1993-9, 1996-39. However, these advisory opinions appear to be limited to their particular circumstances.⁴ A party committee that makes disbursements in connection with nonfederal elections and also makes disbursements in connection with federal elections is required to allocate all of their administrative disbursements. 11 C.F.R. § 106.5(a)(2); *see* Explanation and Justification for 11 C.F.R. 106.5(a), 55 Fed. Reg. 26063 (January 26, 1990). Although the Committee claims that the Administrative Account was not established to be used in connection with any election activity, the Committee concedes that some funds were expended from the

³ Pursuant to the FECA, building funds may be established that are not for the purpose of influencing the election of any candidate in any particular election for Federal office." *See* 2 U. S. C. § 431(8)(B)(viii).

⁴ *See* Concurring Opinion of Vice Chairman Wold and Commissioners Elliott and Mason on AO 1999-11.

account in connection with a federal election.⁵ Therefore, the Committee made expenditures in connection with a federal election and must follow the Commission's rules at 11 C.F.R. § 106.5 for allocating expenses between the federal and non-federal accounts. 11 C.F.R. § 106.5.⁶

Once a Committee makes disbursements in connection with a federal election, the committee must follow the "detailed instructions as to how [it] must allocate [its] administrative expenses and costs for combined federal and non-federal activity." Explanation and Justification for 11 C.F.R. § 106.5, 55 Fed. Reg. 26061 (June 26, 1990). The allocation rules only apply to committees that make disbursements in connection with federal and nonfederal elections. *Id.* Therefore, the expenses from the Administrative Account should be allocated in accordance with 11 C.F.R. § 106.5.

B. Republican National Convention Account (II.B.3)

The proposed Audit Report includes a finding related to another of the Committee's non-federal accounts, the Republican National Convention Account ("Convention Account"). The Audit Division believes that "party sponsored events held in conjunction with a National Nominating Convention, in a convention city cannot be said to be non-political." The Audit Division further contends that as party building or general party activity, these expenses must be allocated between the federal and the non-federal accounts.

The Audit Division determined that the federal share of this activity is \$29,452 based on the allocation ratio for administrative expenses. Expenses paid from this account related to the 1996 Republican National Convention and included consultant fees, room deposits, travel reimbursements, printing costs, supplies, bus transportation, and souvenirs and gifts made out as "1996 Republican National Convention" or "96 Convention Program."

The Committee maintains that the receptions or hospitality suites were held solely as social functions for individuals in the San Diego area attending the Convention and

⁵ Although the Committee has claimed that a portion of the disbursements it made in connection with a federal election were mistakenly made, the regulations do not address the issue of whether the committee must intend to make disbursements in connection with the federal election to fall within the ambit of the allocations rules.

⁶ In addition, the Audit staff indicates that Committee Chairman Heintz made what appeared to be campaign related comments against Mr. Bonior at the state convention, Newt Gingrich spoke at the state Mackinac conference, and Presidential Primary candidates attended the conference. Although, the mere presence of federal candidates at state conventions and conferences may not indicate federal activity, the fact that Chairman Heintz made federal campaign related comments at the state convention appears to indicate that federal election activity was a component of the state convention. However, this analysis is not necessary since the committee has conceded making federal disbursements from the account.

were not an attempt to influence the outcome of the Convention, or to solicit contributions, or advocate the election or defeat of any candidate.

The Commission's allocation rules do not address the issue of specifically what must be shown to prove disbursements were made in connection with a federal election. *This Office recognizes that while it may appear that party committees inherently make disbursements in connection with both federal and non-federal elections, it is possible that a party committee makes purely non-federal expenditures. Thus, to require all administrative disbursements made by the Committee to be allocated may be too far reaching without evidence of disbursements for specific federal activity. However, to the extent that the facts set forth in the proposed Audit Report show that some disbursements were made from this account in connection with a federal election, then the Committee must allocate all disbursements made from this account.*

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FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

April 18, 2000

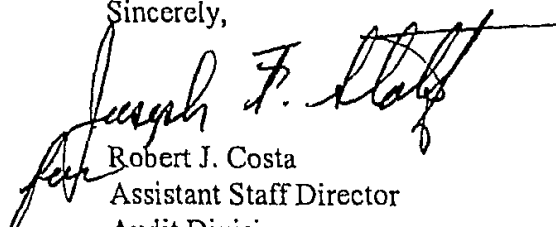
Mr. William H. Gnodtke, Treasurer
Michigan State Republican Party
2121 E. Grand River
Lansing, MI 48912

Dear Mr. Gnodtke:

Attached please find the Final Audit Report on Michigan State Republican Party. The Commission approved the report on April 13, 2000.

The Commission approved Final Audit Report will be placed on the public record on April 21, 2000. Should you have any questions regarding the public release of the report, please contact the Commission's Press Office at (202) 694-1220. Any questions you have related to matters covered during the audit or in the report should be directed to Ms. Cornelia Riley or Mr. Russ Bruner of the Audit Division at (202) 694-1200 or toll free at (800) 424-9530.

Sincerely,


Robert J. Costa
Assistant Staff Director
Audit Division

Attachment as Stated

cc: Ms. Henrietta Tow, Assistant Treasurer
Mr. Eric E. Doster

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CHRONOLOGY

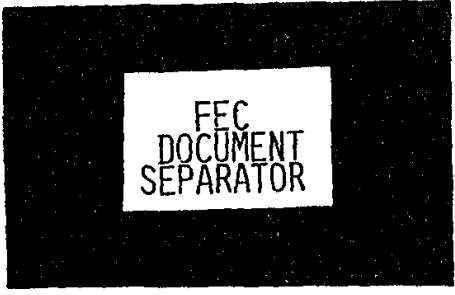
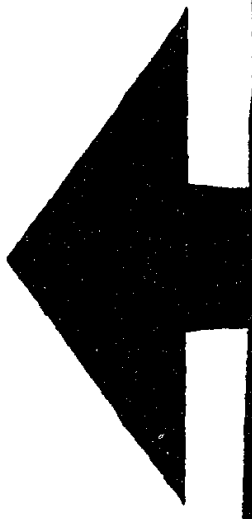
MICHIGAN REPUBLICAN STATE COMMITTEE

Audit Fieldwork	Nov. 9 to Dec. 16, 1998
Interim Audit Report to the Committee	Sept. 15, 1999
Response Received to the Interim Audit Report	Nov. 2, 1999
Final Audit Report Approved	April 13, 2000

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