



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

July 17, 1998

MEMORANDUM

TO: RON M. HARRIS
PRESS OFFICER
PRESS OFFICE

FROM: ROBERT J. COSTA *cc: for RJC 7-17-98*
ASSISTANT STAFF DIRECTOR
AUDIT DIVISION

SUBJECT: PUBLIC ISSUANCE OF THE FINAL AUDIT REPORT ON
CHICAGO'S COMMITTEE FOR '96

Attached please find a copy of the final audit report and related documents on the Chicago's Committee for '96 which was approved by the Commission on June 25, 1998

Informational copies of the report have been received by all parties involved and the report may be released to the public.

Attachment as stated

cc: Commissioners
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Office of General Counsel
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CONFIDENTIAL

REPORT OF THE AUDIT DIVISION
ON
CHICAGO'S COMMITTEE FOR '96

Approved June 25, 1998



FEDERAL ELECTION COMMISSION

999 E STREET, NW

WASHINGTON, DC

2025 RELEASE UNDER E.O. 14176

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**REPORT OF THE AUDIT DIVISION ON
CHICAGO'S COMMITTEE FOR '96
EXECUTIVE SUMMARY**

Chicago's Committee for '96 (Host Committee) registered with the Federal Election Commission on August 16, 1994 as the Host Committee for the presidential nominating convention for the Democratic Party.

The audit was conducted pursuant to Section 9008.54 of Title 11 of the Code of Federal Regulations which directs the Commission to conduct an examination and audit of each host committee registered under 11 CFR §9008.51.

The findings of the audit were presented to the Committee at an exit conference held on July 25, 1997 and in the Exit Conference Memorandum (ECM). The Committee's responses to the findings are contained in the audit report.

The following is an overview of the findings contained in the audit report.

APPARENT CONVENTION EXPENSES PAID BY THE HOST COMMITTEE AND CITY OF CHICAGO- 26 U.S.C. §9008(h), 11 CFR §9008.3(a)(4)(vii), 11 CFR §9008.7(a)(4), 11 CFR §9008.12(b)(3) and (b)(7), 11 CFR §9008.52 (c), 11 CFR §104.3(a). The Audit staff identified payments totaling \$2,580,742, made by the Host Committee and the City of Chicago for certain production and telecommunications expenses which did not appear to fall within the categories of permissible expenses which could be paid by the Host Committee or the City of Chicago. The production payments, which totaled \$1,455,407, were made to six vendors for services such as providing a public address system, constructing camera platforms and lighting, providing stagehands, riggers, projectionists, electricians, teamsters, etc. Based on the Democratic National Convention Committee's response to its ECM, the Audit staff conceded that audio services, including a public address system, provided by one vendor could be permissibly paid. The Commission determined that services provided by the remaining five vendors were permissible Host Committee expenditures. Regarding the telecommunications expenses, the Commission determined that payments totaling \$726,835 for the DNCC's local and long distance telephone charges could not be permissibly paid by the Host Committee or City of Chicago.

IN-KIND CONTRIBUTIONS TO THE HOST COMMITTEE VIEWED AS APPARENT CONVENTION EXPENSES- 11 CFR §9008.(b)(3), 11 CFR §9008.7(a)(4)(ix). The Audit staff identified an "electronic voting system" contributed by AT&T, valued at \$150,000, and a "credentials management system" contributed by the Polaroid Corporation, valued at \$15,000, which appeared to be items which should have been paid for by the DNCC. The Commission determined however, that the use of funds for a voting tabulation system was a permissible Host Committee expense. In addition, based on the Host Committee's response to the ECM, the Audit staff concluded that the credentials management system was a security measure and, as such, did not result in a prohibited in-kind contribution.

NUMBERS WITHIN VISA CARD



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WASHINGTON, D.C. 20463

**REPORT OF THE AUDIT DIVISION
ON
CHICAGO'S COMMITTEE FOR '96**

I. BACKGROUND

A. AUDIT AUTHORITY

This report is based on an audit of Chicago's Committee for '96 (the Committee or Chicago '96). The audit sought to determine whether there has been compliance with the provisions of the Federal Election Campaign Act of 1971, as amended (the Act). The audit was conducted pursuant to 11 CFR §9008.54 which states that the Commission shall conduct an examination and audit of each host committee registered under 11 CFR §9008.51.

B. AUDIT COVERAGE

The audit covered the period from August 11, 1994 through March 31, 1997. During this period, the Committee's reports reflect an opening cash balance of \$-0-, total receipts of \$21,481,973, total disbursements of \$20,960,388, and a closing cash balance of \$552,928.

C. COMMITTEE ORGANIZATION

Chicago '96 incorporated as an Illinois not-for-profit corporation on April 28, 1994, registered with the Federal Election Commission (FEC) on August 16, 1994, and applied for 501(c)(3) tax-exempt status during March, 1995. The Treasurer of the Committee is Walter K. Knorr. The Committee established and maintains its headquarters in Chicago.

The Committee used ten bank accounts to handle its financial activity. From these accounts, the Committee made approximately 1,600 disbursements. The Committee received approximately 1,363 contributions from individuals and local businesses, totaling about \$14,559,452. In addition, the Committee reported receiving 348 in-kind contributions, totaling approximately \$6,739,224.

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D. AUDIT SCOPE AND PROCEDURES

The audit of the Committee included testing of the following general categories:

1. The receipt of contributions from prohibited sources, those from outside of the Chicago Metropolitan Area;
2. proper disclosure of contributions from individuals to include the itemization of contributions when required, as well as, the completeness and accuracy of the information disclosed;
3. proper disclosure of disbursements including the itemization of disbursements when required, as well as, the completeness and accuracy of the information disclosed;
4. review of the disbursements to determine compliance with the requirements of 11 CFR §9008.52(c) (see Findings II(A) and (B));
5. proper disclosure of committee debts and obligations;
6. the accuracy of total reported receipts, disbursements and cash balances as compared to committee bank records;
7. adequate recordkeeping for committee transactions; and,
8. other audit procedures that were deemed necessary in the situation.

As part of the Commission's standard audit process, an inventory of committee records is conducted prior to the audit fieldwork. This inventory is conducted to determine if the auditee's records are materially complete and in an auditable state. Based on our review of records presented, it was concluded that the records were materially complete and fieldwork began immediately.

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

II. AUDIT FINDINGS AND RECOMMENDATIONS

A. CONVENTION-RELATED EXPENDITURES

Section 9008.52(c) of Title 11 of the Code of Federal Regulations states, in part, that contributions received by host committees may be used for the following: to defray those expenses incurred for the purpose of promoting the suitability of the city as a

convention site; to defray those expenses incurred for welcoming the convention attendees to the city, such as expenses for information booths, receptions, and tours; to defray those expenses incurred in facilitating commerce, such as providing the convention and attendees with shopping and entertainment guides and distributing the samples and promotional material specified in 11 CFR 9008.9(c); to defray the administrative expenses incurred by the host committee, such as salaries, rent, travel, and liability insurance; and to provide the national committee use of an auditorium or convention center and to provide construction and convention related services for that location such as: construction of podiums; press tables, false floors, camera platforms; additional seating; lighting, electrical, air conditioning and loudspeaker systems; offices; office equipment; and decorations.

Further, contributions may be used to defray the cost of various local transportation services, including the provision of buses and automobiles; to defray the cost of law enforcement services necessary to assure orderly conventions; to defray the cost of using convention bureau personnel to provide central housing and reservation services; to provide hotel rooms at no charge or a reduced rate on the basis of the number of rooms actually booked for the convention; to provide accommodations and hospitality for committees of the parties responsible for choosing the sites of the conventions; and to provide other similar convention-related facilities and services.

Section 9008.7(a)(4) of Title 11 of the Code of Federal Regulations states that "Convention expenses" include all expenses incurred by or on behalf of a political party's national committee or convention committee with respect to and for the purpose of conducting a presidential nominating convention or convention-related activities.

On August 4, 1994, the City of Chicago (the City) and the Democratic National Convention Committee, Inc. (DNCC) entered into an written agreement (the Convention Contract or Contract). One section of this agreement provided for the establishment of a host committee to serve, in part, as a separate fund to satisfy the financial obligations of the City specified in the Contract, and, for securing cash and in-kind contributions necessary to obtain goods and services needed for the Convention. As mentioned previously, the Committee registered with the FEC shortly thereafter.

On August 19, 1996, the City and the DNCC amended the Contract, in part, with a budget revision entitled "Chicago '96/City Budget." Each expense classification in the revised budget was identified by line number, line item, total amount budgeted, total cash spent, and total in-kind contributions allocated to that line item. The Audit staff's review of management controls disclosed that the Committee's disbursements records included memoranda which identified expenditures made on behalf of the DNCC and the budget line number to which each expense should be allocated. The apparent objective of these controls was to facilitate managerial reporting and compliance with the budget.

During a review of the Committee's disbursement records, the Audit staff identified payments to eight vendors totaling \$2,055,732 which appear to be for convention-related expenditures and not for items noted above at 11 CFR §9008.52(c). Furthermore, the Committee obtained written concurrence from the DNCC for all of the payments. Expenses defrayed fell into one of two major budgetary classifications: production expenses or telecommunications costs.

The issue of the permissibility of these payments was addressed in Exit Conference Memoranda resulting from the audits of both Chicago '96 and the DNCC. Both committees, as well as the City of Chicago, were given an opportunity to respond to the Memoranda, and, information provided by them is incorporated in the discussions below.

In response to the respective Exit Conference Memoranda, both the Committee and the DNCC argued that all of the expenses discussed below are covered by one of the categories of permissible host committee expenses at 11 CFR §9008.52(c)(1) or, referring to 11 CFR §9008.52(c)(1)(xi), are "similar" to expenses covered by one of the permissible expense categories. To read 11 CFR §9008.52(c)(1) as broadly as both committees propose would effectively negate the limitation on convention expenses at 26 U.S.C. §9008(d); the prohibition on contributions to a convention committee that has received the full federal payment (11 CFR §9008.6(a)); the prohibition on the use of corporate contributions in connection with federal elections at 2 U.S.C. §441b; and the Commission's clear statement in the *Explanation and Justification (E&J)* supporting the provisions contained in 11 CFR §9008.52(c)(1) that allowing the host committee to pay selected convention expenses is "intended to be a very narrow exception to the statutory limitation on convention expenses."¹

1. Production Expenses

Pursuant to the Contract, the City agreed to provide, among other things, the following production hardware and related services to the DNCC: "a lighting system and the services of lighting consultants and a lighting designer to operate the system;" "an audio system (including but not limited to microphones at each delegation and all audio feeds) and the services of audio consultants and an audio designer to operate the system;" "the broadcast on one of the City's cable television stations gavel to gavel coverage of the Convention and special programming directly related to the Convention" provided that the "station shall make available to the DNCC a tape of such coverage... without charge for rebroadcast, display, or other rights;" and, "all necessary production control personnel, including camera persons, grips, video control and tape operators, audio and video maintenance engineers, chyron operators, video and utility personnel, riggers, gaffers, property master and such other production assistants as may be required."

¹ See 44 Fed Reg 63,038 (Nov. 1, 1979)

The Audit staff's review of the Committee's disbursements records identified payments to six vendors totaling \$1,455,407. Furthermore, documents obtained by the Audit staff indicate that the City of Chicago paid an additional \$233,500.² These payments were apparently made in execution of the Convention Contract's provisions related to production, and, the Committee's expenditures are discussed in detail below.

a. **Audiotek Corporation**

The Audit staff identified one disbursement to Audiotek Corporation dated August 19, 1996 in the amount of \$113,500. Committee internal memoranda allocated the payment to budget line item "32-Audio." According to the Committee's contract with Audiotek, the vendor was to provide public address systems, press and media feed distribution systems, delegate microphone selection systems, and on site technicians for the convention.

b. **Automated Studio Lighting**

The Audit staff identified four payments to Automated Studio Lighting totaling \$299,016 from July through October of 1996. Committee records disclosed that all but one of the payments was allocated to budget line item "31-Lighting." The remaining disbursement in the amount of \$48,070 was allocated to budget line "19-Production Personnel." Vendor invoices reviewed by the Audit staff supported the Committee's expense classifications.

c. **Chicago Scenic Studios, Inc.**

The Audit staff identified two payments to Chicago Scenic Studios during August and November of 1996 totaling \$615,083. The Audit staff's review of Committee records disclosed that both disbursements were allocated to budget line item "19-Production Personnel." Vendor documentation confirmed that all charges submitted were for production labor. A proposal from the vendor described labor services to be provided as stagehands, riggers, teamsters, projectionists, broadcast engineers, cameramen, carpenters, and decorators for the convention.

d. **Theatrical Resources, Inc.**

The Audit staff identified one payment in the amount of \$132,808 to Theatrical Resources, Inc. made during July, 1996. A review of Committee records disclosed that the disbursement covered payroll for riggers and electricians working during July and August, 1996 pursuant to a contract between the DNCC and the

² These disbursements are outside of the scope of this audit report, however, we do note that pursuant to 11 CFR §9008.53(b) expenditures made by a municipality or government agency should also meet the requirements of 11 CFR §9008 52(c) Additional details on payments by the City are contained in the audit report on the DNCC

vendor. The expense was allocated to budget line "19-Production Personnel." A separate review of the convention committee's records disclosed that the DNCC subsequently paid this vendor a total of \$59,848 with three additional checks written during September, 1996 and February, 1997.

e. VANCO Lighting Services

The Audit staff identified one payment in the amount of \$175,000 to VANCO lighting services during July, 1996. A review of Committee records disclosed that the expense was allocated to budget line "31-Lighting." Vendor invoicing described the services provided during July and August 1996 as a "rigging package" and identified the Convention as the "show" to be supported by VANCO.

f. Vari-Lite, Inc.

The Audit staff identified one payment in the amount of \$120,000 to Vari-Lite, Inc. during August, 1996. A review of Committee records disclosed that the expense was allocated to budget line "31-Lighting." Vendor invoicing identified the Convention to be the "producer" using automated lighting and technical support provided during July and August of 1996. The Audit staff also reviewed City memoranda asserting the equipment provided to be "lighting instruments, border and cyclorama striplights, follow spotlights, floodlights, special effects lighting, spotlights, etc." for the Convention.

In the ECM, the Audit staff concluded that payments to the vendors described above are not expenses properly paid by a host committee pursuant to 11 CFR §9008.52(c). Rather, they are convention expenses that should have been paid by the DNCC pursuant to 11 CFR §9008.7(a) for reasons discussed below.

As noted previously, some of the aforementioned disbursements relate to salaries for electricians and other individuals for labor such as rigging cameras and lighting. Although 11 CFR §9008.52(c) allows a host committee to defray salaries and convention related expenses such as construction of camera platforms and lighting, the Audit staff believes that the expenses paid by the Committee related to rigging cameras, automated lighting, and audio systems with the stated purpose of providing media feeds or cable broadcasts are not the same as building a platform from which cameras can be used for the television production. Furthermore, the Committee defrayed DNCC contracted labor costs unrelated to rigging or construction, i.e., projectionists, broadcast engineers, and cameramen. Whereas the Committee made numerous other disbursements, separate from the production expenditures, relating to construction of podiums, platforms and other facilities at the Convention center, the disbursements in this case appear to be related to the overall processes of television production and broadcasting.

Categories of permissible host committee expenses enumerated at 11 CFR §9008.52(c)(1) deal with preparing the convention site to host the convention and to promote the convention city. In contrast, production expenditures made by the Committee directly facilitated television and other media coverage of Convention proceedings through press feeds and cable broadcasts. Instead of merely preparing the convention center premises or promoting the City of Chicago, these expenditures aided the Democratic Party in bringing its message to the public in hope of influencing support for the political party hosting the convention and its candidate for President. Furthermore, expenditures related to putting on a stage "production" to be seen by the country are clearly costs of conducting a convention as described at 11 CFR §9008.7(a) and not the type of disbursement envisioned under the host committee regulations. Consequently, in the ECM, the Audit staff concluded that the total amount of \$1,455,407 paid by the Committee for production expenses results in an in-kind contribution to the DNCC.

In the ECM, the Audit staff recommended that the Committee provide documentation to demonstrate that the payments described above were allowable Committee expenses pursuant to 11 CFR §9008.52(c) and did not result in prohibited in-kind contributions to the DNCC. Also, for these specific items, the Committee was to address whether these disbursements would have been necessary for the convention hall if not for the television production requirements. If the Committee elected to view any of the aforementioned expenses as allocable in part to permissible activities, then documentation supporting the Committee's basis for such allocation was to be presented.

In its response to the ECM, Chicago '96 disagreed that the payments described above resulted in a prohibited contribution to the DNCC. The Committee asserted that 11 CFR §9008.52(c)(1) "is not intended to be all-inclusive, but is intended instead to provide a general representation of the convention facilities and services for which cash and in-kind contributions could be used." Noting that 11 CFR §9008.52(c)(1)(xi) permits host committees to provide "other similar convention-related facilities and services," the Committee asserts that all of the production expenditures described above were directly related to work performed at the site of the Convention and an adjacent media pavilion, and therefore, in accordance with the regulations.

Additionally, the Committee contended that "the host committee necessarily must support the objectives of a political party's convention committee" in order to achieve its principal purposes of encouraging commerce and projecting a favorable image of the convention city. From this, the Committee concludes that "the facilitation of television and media coverage by a host committee is reasonable and proper." Noting that the regulations permit host committees to pay for television and media-related items such as press stands and television platforms, the Committee argued that it would be "illogical to propose that certain other items which accomplish the exact same purpose" are prohibited.

The DNCC in its response also challenged the Audit staff's position, stating "it is clear that these expenses were of a type that the Commission's regulations explicitly and specifically provide may be paid for by the Host Committee or the City." The DNCC summarized payments to each vendor, asserting that "[a]ll of the expenses at issue were incurred for lighting or sound equipment used within the Convention Hall, or for services or equipment directly involved in constructing and preparing the podium." Citing 11 CFR §9008.52(c)(1)(v) and (xi), the DNCC concluded that "[i]t could not be clearer that the items for which these six vendors were paid are within the scope of this subsection."

Furthermore, the DNCC asserts in its response that the "Audit Division has completely misperceived the purposes of these expenditures," adding that "[m]uch of the labor and equipment involved would have been required even if the Convention had never been broadcast." The response goes on to say that "to the extent that sound, lighting, and other electrical equipment was [emphasis added by DNCC] needed or used to facilitate television, radio or cable broadcast of the Convention proceedings, the expenses of such equipment are manifestly a permissible expense under section 9008.52(c)(1)(v)."

According to the DNCC, "[n]othing in the language, prior history or Explanation or Justification for the current regulations in any way suggests any limitation on the Host Committee's ability" to defray expenses "related to facilitating broadcast or other press coverage of the Convention, as distinct from other expenses of constructing and preparing the Convention Hall." The DNCC concludes that the Audit staff had "no basis for such a distinction," adding that there is "no possibility" that any committee "could have been aware of any such distinction by reading the regulations."

Of special interest was a section of the DNCC's response providing details regarding the Host Committee's payment to Audiotek Corporation. According to the DNCC, services provided by this vendor comprised "public address systems, wiring and speakers so that people in all parts of the Hall could hear the proceedings while they were taking place, delegate microphone selection systems, a hearing impaired wireless system for the Hall (so that hearing-impaired persons within the Hall could follow the proceedings), amplification for the orchestra playing within the Hall, and labor to install and assist in the operation of this on-site sound equipment." Based on these additional details, the Audit staff concluded Audiotek's services were essentially similar to "loudspeaker systems," and therefore permissible under 11 CFR §9008.52(c)(1)(v).

Regarding the remaining five vendors, however, other statements in the DNCC's response confirm that at least some portion of the disbursements at issue was used to facilitate television, radio or cable broadcast of the Convention proceedings. Furthermore, other than Audiotek, the responses from both the DNCC and Chicago '96 failed to offer any new documentation or bases for allocation which identify those parts of the expenses that would have been required even if the

Convention had never been broadcast, as recommended in the ECM. The Audit staff believes that the regulations, together with explanatory material published in the *Federal Register*, form a reasonable basis for its position, and therefore, concludes that Chicago '96 made a prohibited in-kind contribution to the DNCC in the amount of \$1,341,907 [\$1,455,407-\$113,500].

On April 23, 1998 the Commission, during its consideration of the audit report on the 1996 Committee on Arrangements for the Republican National Convention, voted that the use of funds, for such services as provided by the remaining five vendors discussed above, is a permissible host committee expense.

2. Telecommunications

Section 9008.7(a)(4)(x) of Title 11 of the Code of Federal Regulations states that "Convention Expenses" include all expenses incurred by or on behalf of a political party's national committee or convention committee with respect to and for the purpose of conducting a presidential nominating convention or convention-related activities. Such expenses include administrative and office expenses for conducting the convention, including stationery, office supplies, office machines, and telephone charges; but exclude the cost of any services supplied by the national committee at its headquarters or principal office if such services are incidental to the convention and not utilized primarily for the convention.

As mentioned above, 11 CFR §9008.52(c) permits host committees to provide the national committee use of a convention center and convention related services for that location such as offices and office equipment. Additionally, the E&J states, in part, that the revised rules at 11 CFR §9008.52(c) do not permit host committees or municipalities to pay the convention committee's or the national party's overhead and administrative expenses related to the convention.³

Pursuant to the Convention Contract the City agreed: to provide the DNCC with a telecommunications system; to provide the DNCC with a cellular phone system; and, to pay for all long distance service charges incurred by the DNCC at the Convention facilities. The Audit staff's review of disbursements disclosed that the Committee and City made substantial payments on behalf of the DNCC for telephone installation and service. Because telephone installation costs are allocable to office equipment, and therefore, are permissible host committee expenses pursuant to 11 CFR §9008.52(c)(1)(v), the following discussion focuses on telephone service charges.

Committee records documented payments totaling \$600,325 for local and long distance telephone service. Furthermore, documents obtained by the Audit

³ See 59 Fed Reg. 33,614 (June 29, 1994)

staff indicate that the City of Chicago paid an additional \$126,510.⁴ These payments were apparently made in execution of the Contract's provisions related to telecommunications, and, the Committee's expenditures are discussed in more detail below.

a. Ameritech

The Audit staff identified 10 payments to Ameritech, which net of refunds to the Committee from the vendor, totaled \$512,637. A review of the invoices disclosed that all of the billings were local telephone service charges for Convention telephone numbers or accounts apparently assigned to the DNCC. Furthermore, internal Committee memoranda attributed all of the expenses to the DNCC.

b. AT&T

The Audit staff identified 15 payments to AT&T totaling \$87,688. A review of the invoices disclosed that all of the billings were long distance telephone service charges for Convention telephone numbers or accounts apparently assigned to the DNCC. Furthermore, internal Committee memoranda attributed all of the expenses to the DNCC.

In the ECM, the Audit staff concluded that service charges for telephone calls made by the DNCC in support of its operations were a convention overhead expense which did not contribute to preparation of convention center premises or promotion of the City of Chicago. Therefore, the total amount of \$600,325 paid by the Committee for telephone service charges resulted in an in-kind contribution to the DNCC. The Audit staff also recommended that the Committee provide documentation to demonstrate that the payments for telephone service charges were allowable Committee expenses pursuant to 11 CFR §9008.52(c) and did not result in prohibited in-kind contributions to the DNCC.

In its response to the ECM, the Committee stated that that the telecommunications systems "existed for the benefit of Chicago '96" and that without having provided these services, it would have been impossible for the Committee to fulfill its obligations under the Convention Contract. The Committee asserted that the "telecommunications system served to accomplish a wide variety of tasks directly related to the Convention" including construction as well as security. The Committee concludes that expenditures for the phone charges "fall within the parameters of 11 C.F.R. Section 9008.52(c)," and therefore, it was appropriate to pay for them.

⁴ These disbursements are outside of the scope of this audit report. however, we do note that pursuant to 11 CFR §9008.53(b) expenditures made by a municipality or government agency should also meet the requirements of 11 CFR §9008.52(c) Additional details on payments by the City are contained in the audit report on the DNCC

The DNCC took a different approach in its response, arguing that “by any reasonable reading, the regulation on its face [emphasis in original] authorizes the host committee to pay for the costs of telephone service for the Convention.” In the DNCC’s opinion, “[t]o say that the costs of office telephones are not an overhead or administrative expense but that the costs of using the telephones are such an expense is to draw a distinction that no reasonable reading of the plain language of the regulation would support.” The DNCC then criticized the “language of the Explanation and Justification (E&J),” declaring that it should “not be given precedence over the plain language of the regulation,” and that “the E&J language is itself ambiguous.”

Despite arguments presented above, the Audit staff believes that the E&J offers a reasonable starting point for applying the regulations as intended by the Commission. The Audit staff further concludes that charges for local and long distance telephone calls made by the DNCC are most appropriately classified as administrative and overhead expenses of the convention committee and not construction or security expenses benefiting the host committee. Therefore, the total amount of \$600,325 paid by the Chicago '96 results in an in-kind contribution to the DNCC.

B. IMPERMISSIBLE USE OF IN-KIND CONTRIBUTIONS

Section 9008.52(c)(1) of Title 11 of the Code of Federal Regulations states, in part, that local businesses (excluding banks), local labor organizations, and other local organizations or individuals may donate funds or make in-kind donations to a host committee to be used for the purposes described at the beginning of Finding II.A.

In the Convention Contract, the City agreed, in part, to provide the DNCC with “an electronic voting system for use in the Convention Hall” and “a photo security system to control access to the Convention Offices.” During a review of the Committee’s donor records, the Audit staff identified in-kind contributions from two vendors totaling \$165,000. In the ECM, the Audit staff stated that contributed equipment appears to have been used for convention-related purposes pursuant to terms of the Contract and not for items noted above at 11 CFR §9008.52(c)(1) as discussed below.

1. AT&T

The Audit staff identified an in-kind contribution from AT&T of an “electronic voting system” valued at \$150,000 by the vendor which appears to have been used for convention-related purposes and not for items noted above at 11 CFR §9008.52(c)(1). The donated voting system fulfilled Convention budget line number “70-Electronic Voting.”

The Committee asserted that the electronic voting system “enabled state delegations to have interactive contact with leadership and other personnel on the convention podium itself.” According to the Committee, the voting system was used in the United Center as a part of the actual convention services in accordance with the

Convention Contract. A Democratic National Convention press release issued during November, 1995 confirmed that AT&T was designated as an official technology provider, and that delegates would be using AT&T integrated technology on the Convention floor.

In the ECM, the Audit staff found that the donation of a voting system provided the DNCC with the same benefit as if the host committee had paid a convention expense, and therefore, was an impermissible use of host committee resources. Categories of permissible uses for contributions to host committees, expenses enumerated at 11 CFR §9008.52(c)(1), involve preparing the convention site to host the convention and promoting the convention city. In contrast, the equipment donated by AT&T was used to provide Democratic Party leadership with rapid tabulation of delegate voting. This enhancement to political operations at the Convention served a partisan function in conflict with the host committee regulations. Therefore, the Audit staff concluded that use of the voting system valued at \$150,000 results in a prohibited in-kind contribution to the DNCC. Also, the Audit staff recommended in the ECM that the Committee provide documentation to demonstrate that the electronic voting system was put to permissible uses pursuant to 11 CFR §9008.52(c) and did not result in prohibited in-kind contributions to the DNCC.

In response to the above, Chicago '96 described its obligation to provide a delegate voting system under the Convention Contract as part of the "actual convention services." The Committee disagreed that the voting system's furtherance of a partisan party function would prohibit its use by the DNCC, arguing that "because a convention naturally must serve one political party or another, it is implicitly understood that the convention itself is partisan while a host committee remains nonpartisan." Also, Chicago '96 stated its understanding that "similar Voting Systems have been donated for past conventions and no regulatory problems have been raised." As a result, the Committee concluded that the delegate voting system "falls squarely within the parameters of 11 C.F.R. Section 9008.52(c)."

In response to a conference held at the close of audit fieldwork, the DNCC verified that "(t)he electronic system used to count the votes of delegates at the Convention" served as "a core part of the physical systems needed to run the convention." Later, in its response to the ECM, the DNCC pointed out that 11 CFR §§9008.52(c)(1)(v) and (vi) permit the Host Committee to pay for office equipment in the convention hall as well as similar convention-related facilities and services. According to the DNCC, "[t]here is no logical difference between telephone receivers used to communicate information to the podium and a computerized system that does the same thing." The DNCC finds it "difficult to imagine a 'facility' more 'related' to the Convention than a system for counting delegate votes." The DNCC also rejects the Audit staff's position on the grounds that "[t]o say that a voting system is an 'enhancement to political operations' contributes nothing to an analysis of permissibility of this expenditure, since virtually every [emphasis added by DNCC] expenditure... specifically allowed by section 9008.52(c)(1)(v) could be said to 'enhance' political operations."

The responses above do not demonstrate that the in-kind contribution was permissible under the regulations. Furthermore, they confirm that the Audit staff correctly interpreted the basic purpose of the electronic voting system. In light of this, the Audit staff concluded that use of the voting system, valued at \$150,000, results in a prohibited in-kind contribution to the DNCC.

On January 22, 1998, the Commission, during its consideration of the audit report on the San Diego Host Committee/Sail to Victory San Diego '96, voted that the use of funds for a voting tabulation system was a permissible host committee expense.

2. Polaroid Corporation

Section 9008.7(a)(4)(ix) of Title 11 of the Code of Federal Regulations states that "Convention expenses" include all expenses incurred by or on behalf of a political party's national committee or convention committee with respect to and for the purpose of conducting a presidential nominating convention or convention-related activities. Such expenses include expenses for printing convention programs, a journal of proceedings, agendas, tickets, badges, passes, and other similar publications.

In the ECM, the Audit staff identified an in-kind contribution from Polaroid Corporation of a "credentials management system" assigned a value of \$15,000 by the vendor. According to Polaroid's proposal, the system would capture and maintain a text and image database of all DNCC and host committee employees. Included in the \$15,000 valuation were six months rental of the system, labor, logo scanning, training, shipping, and card design. According to DNCC training materials, the credentials were to be worn by every attendee, and, the passes granted five levels of access, designated by credential color, to different sections of the convention facility.

The Audit staff concluded that the donation of the credentials management system provided the DNCC with the same benefit as if the host committee had paid a convention expense, and consequently, is not a permissible use of host committee resources as defined at 11 CFR §9008.52(c)(1). As a result, the Committee apparently made a prohibited in-kind contribution of \$15,000 to the DNCC. Also, it was recommended in the ECM that the Committee provide documentation to demonstrate that the credentials management system was put to permissible uses pursuant to 11 CFR §9008.52(c) and did not result in prohibited in-kind contributions to the DNCC.

In its response to the ECM, the Committee disagreed that the use of the credentials management system was not in compliance with 11 CFR 9008.52(c). The Committee asserted that the system "related directly to the security services necessary to ensure safety and orderly conduct for the convention staff and participants." and therefore, came under provision which allow host committees to defray the costs of law enforcement services necessary to ensure orderly conventions. According to the

Committee, the system “provided photo identification passes for a variety of personnel working at the 320 North Clark location (which housed both Chicago ’96 and the DNCC, as well as numerous other city and state offices and courtrooms) as well as at the United Center,” the site of the convention. The DNCC’s response addressed this issue in a similar manner.

In order to clarify representations made above, the Audit staff contacted both committees. Statements made by representatives of the DNCC and Chicago ’96, along with documents contained in the audit workpapers, corroborate that the credentials management system generated identification cards which were used exclusively as a security measure for employees of both committees to gain access to the 320 North Clark Street office facility and United Center, but only during construction and preparation phases leading up to the Convention. There was no evidence that the credentials management system assisted the DNCC in managing the movement of delegates or other personnel once inside the Convention. Accordingly, the Audit staff concludes that the use of the donated credentials management system was within the scope of 11 CFR §9008.52(c)(1)(vii) and did not result in a prohibited in-kind contribution to the DNCC.

CONFIDENTIAL

Received
2/23/98



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

February 23, 1998

MEMORANDUM

TO: Robert J. Costa
Assistant Staff Director
Audit Division

THROUGH: John C. Surina
Staff Director

FROM: Lawrence M. Noble
General Counsel

Kim L. Bright-Coleman *KBC*
Associate General Counsel

Rhonda J. Vosdigh *RJ*
Assistant General Counsel

Delbert K. Rigsby *DKR*
Attorney

SUBJECT: Proposed Audit Report on the Chicago Committee for '96 (LRA #510)

1. INTRODUCTION

The Office of General Counsel has reviewed the proposed Audit Report on the Chicago Committee for '96 ("Host Committee"), which was submitted to this Office on December 29, 1997.¹ This memorandum summarizes our comments on the proposed Audit Report.² Some of the issues discussed in the proposed Audit Report and herein overlap with issues in the proposed Audit Report on the Democratic National Convention Committee, Inc. ("Convention

¹ Comments from this Office are due on February 23, 1998.

² Since the proposed Audit Report concerns the audit of a host committee, this Office recommends that the Commission consider this document in open session in accordance with 11 C.F.R. §§ 9008.54, 9007.1(e)(1) and 9038.1(e)(1).

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Committee").³ Many issues discussed herein also overlap with this Office's comments on the Audit Report for the San Diego Host Committee, which were submitted to the Audit Division on November 19, 1997. This Office's opinions remain the same as the opinions stated in the comments on the San Diego Host Committee Audit Report in regard to the limitations on permissible host committee expenses. However, the analysis in the audit reports of the Host Committee and the Convention Committee should be the same as the Commission's ultimate decisions in the audits of the San Diego Host Committee and the Convention on Arrangements of the Republican National Convention. This Office concurs with the findings in the proposed Audit Report for the Chicago Host Committee that are not discussed separately in this memorandum. If you have any questions, please contact Delbert K. Rigsby, the attorney assigned to this review.

II. CONVENTION-RELATED EXPENDITURES (II.A)⁴

The proposed Report states that the Host Committee appears to have made impermissible expenses by paying five vendors for television production expenses in the amount of \$1,341,907. The proposed Report states that such television production expenses are not permissible host committee expenditures because they are not included in the expenses listed in 11 C.F.R. § 9008.52(c), and were not used to promote the city or prepare the convention site for the convention. The principal objectives of a host committee are to encourage commerce in the convention city, project a favorable image of the city for convention attendees and defray convention expenses. 11 C.F.R. § 9008.52. Host committees may receive donations and in-kind contributions from local businesses and organizations to defray convention expenses set forth in 11 C.F.R. § 9008.52(c). The national committee of a political party may receive public funds to pay for its convention and is limited in the amount which it may spend on the convention. 26 U.S.C. § 9008 and 11 C.F.R. § 9008.8. The Explanation and Justification (E & J) for 11 C.F.R. § 9008.7, which concerns the limitations on convention spending, states that the payment of convention expenses by the host committee is "intended to be a narrow exception to the statutory limitation on convention expenses." 44 Fed. Reg. 63038 (November 1, 1979).

This Office concurs with the proposed Report that the Commission intended for 11 C.F.R. § 9008.52(c) to be interpreted narrowly. A broad interpretation of 11 C.F.R. § 9008.52 would be inconsistent with the limitation on convention expenses in 11 C.F.R. § 9008. The proposed Report relies upon the E & J for 11 C.F.R. § 9008.52(c)(1) in reaching its conclusion that the Host Committee's payment of the television production expenses appear to be impermissible and result in prohibited in-kind contributions to the Convention Committee.

³ The proposed Audit Report for the Convention Committee was submitted to this Office on January 7, 1998 and comments are due from this Office on March 4, 1998.

⁴ Parenthetical references are to the relevant section of the proposed Audit Report.

Furthermore, in concluding that most of the television production expenses do not appear to be permissible host committee expenses, the proposed Audit Report states that such expenses are for lighting and personnel costs for the television production and broadcasting of the convention and not for infrastructure costs to prepare the convention site to host the convention. The proposed Report considers infrastructure costs to prepare the convention site as permissible host committee expenses pursuant to 11 C.F.R. § 9008.52(c)(v). Production personnel costs are considered impermissible host committee expenses. The Host Committee did not submit additional documentation, as requested by the Audit staff in the Exit Conference Memorandum, to demonstrate that the television production expenses were permissible host committee expenses.⁵

The proposed Audit Report also states that the Host Committee appears to have made impermissible expenses in the amount of \$600,325 for local and long distance telephone charges. The proposed Report concludes that local and long distance telephone charges are administrative and overhead expenses of the convention committee and not construction or security expenses benefiting the Host Committee. In its response to the Exit Conference Memorandum, the Host Committee argued that the telecommunications system and the telephone charges are an integral part of a construction and convention-related service and should be considered a permissible host committee expense. While office equipment is considered a permissible host committee expense, 11 C.F.R. § 9008.52(c)(v), telephone charges are considered administrative and office expenses. 11 C.F.R. § 9008.7(a)(4)(x). Thus, the Audit staff found that the telephone equipment and installation of the telephone system were permissible host committee expenses, but the service charges were not permissible host committee expenses.

This Office concurs with the proposed Audit Report that the telephone charges appear to be impermissible expenses. To support its conclusion that the telephone charges are overhead expenses, the proposed Report cites the Explanation and Justification for 11 C.F.R. § 9008.52(c), which states that the regulation "does not permit host committees . . . to pay the convention committee's or the national party's overhead and administrative expenses related to the convention." However, this Office believes that this section of the proposed Report should also discuss 11 C.F.R. § 9008.7(a)(4), which defines convention expenses that are permitted to be paid with public funds received by the convention committee. Administrative and office expenses, specifically telephone charges, are listed as such types of expenses. 11 C.F.R. § 9008.7(a)(4)(x).

⁵ The Host Committee only submitted additional documentation regarding Audiotek, one of the vendors. After reviewing the additional documentation, the Audit staff concluded that the payment to Audiotek was a permissible host committee expense because the equipment provided was essentially a loudspeaker system.

III. IMPERMISSIBLE USE OF IN-KIND CONTRIBUTIONS (II.B)

The proposed Report concludes that an electronic voting system provided by AT&T to the Host Committee resulted in an apparent prohibited in-kind contribution to the convention committee in the amount of \$150,000 because it is not an expense listed within 11 C.F.R. § 9008.52, and was not used to promote the city or prepare the convention site for the convention. In its response to the Exit Conference Memorandum, the Host Committee stated that this service was a part of its obligation to provide convention services and should be considered a permissible host committee expense.

This Office has discussed with the Audit staff whether there is any documentation indicating that the voting system was a part of a larger computer system that performed other functions, such as an electronic bulletin board for delegates to receive messages and the ability to obtain information about restaurants and tourist sites in the city. If the voting system was part of a larger integrated system with multiple functions, an argument can be made that it should be considered a permissible host expense and not an in-kind contribution to the Convention Committee. In the audit of the San Diego Host Committee, the Audit staff was able to specify the amount of funds (\$44,067) that were spent solely on the voting system even though it was a part of a larger computer system. The Audit staff concluded that the expense of \$44,067 was an impermissible host committee expense. During the Commission meeting on January 22, 1998, the Commission voted to allow \$44,067 spent on the voting tabulation system as a permissible host committee expense.

The documentation provided by the Chicago Host Committee indicates that the sole purpose of the electronic voting system was to tabulate votes. If the electronic voting system was a separate system whose sole function was to tabulate votes, it would seem that the voting system was an impermissible host committee expense. However, to be consistent with the Commission's decision regarding the electronic voting system in the San Diego Host Committee Audit Report, this Office recommends that the proposed Audit Report be revised to state that the electronic voting system appears to be a permissible host committee expense.



FEDERAL ELECTION COMMISSION
WASHINGTON, D C 20463

July 7, 1998

Mr. Walter K. Knorr, Treasurer
Chicago's Committee for '96
City Hall Room 501
121 North LaSalle Street
Chicago, IL 60602

Dear Mr. Knorr:

Attached please find the Audit Report on Chicago's Committee for '96. The Commission approved the report on June 25, 1998.

The Commission approved Audit Report will be placed on the public record on July 15, 1998. Should you have any questions regarding the public release of the report, please contact Ron Harris of the Commission's Press Office at (202) 694-1220.

Any questions you may have related to matters covered during the audit or in the audit report should be directed to Rick Halter or Wanda Thomas of the Audit Division at (202) 694-1200 or toll free at (800) 424-9530.

Sincerely,

A handwritten signature in black ink, appearing to read "Robert J. Costa".

Robert J. Costa
Assistant Staff Director
Audit Division

cc: Kiplund Kolkmeier, Esq.
Don Davis
Attachment as stated

Chronology
Chicago's Committee for '96

Audit Fieldwork	4/14/97 - 5/7/97
Exit Conference Memorandum to the Committee	7/25/97
Response to Exit Conference Memorandum Received	10/26/97
Audit Report Approved	6/25/98

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PLATE NUMBER 10-10

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