



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

2009-08-25
A07-05
August 25, 2009

MEMORANDUM

AGENDA ITEM

To: The Commission

Through: Robert A. Hickey
Staff Director *APSC RH*

From: John D. Gibson *JG*
Chief Compliance Officer

Joseph F. Stoltz *JFS*
Assistant Staff Director
Audit Division

Alex R. Boniewicz *AB*
Audit Manager

By: Jim Miller *JM*
Lead Auditor

For Meeting of 07-01-10

Subject: Report of the Audit Division on the Tennessee Republican Party Federal Election Account (A07-05)

This document was originally circulated July 9, 2009. Discussions with some Commissioners' Offices have indicated the need for some clarifying editorial changes to the report. These changes, which have been grey-shaded to highlight them, appear on pages 13, 15 and 16. Therefore, we are withdrawing the prior circulation of this document and simultaneously resubmitting the attached revised document.

Recommendation

The Audit staff recommends that the report be approved.

This report is being circulated on a tally vote basis. Should an objection be received, it is recommended that the report be considered at the next regularly scheduled open session. If you have any questions, please contact Jim Miller or Alex Boniewicz at 694-1200.

Attachments:

Report of the Audit Division on the Tennessee Republican Party Federal Election Account Legal Analysis, dated June 15, 2009



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

January 1, 2005 – December 31, 2006

Why the Audit Was Done

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

Future Action

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

About the Committee (p. 2)

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

Financial Activity (p. 2)

- **Receipts**
 - Contributions from Individuals \$ 3,483,766
 - Contributions from Other Political Committees 367,326
 - Transfers from Affiliated/Other Party Committees 2,743,200
 - Transfers from Non-federal Account 555,805
 - All Other Receipts 22,980
 - **Total Receipts** \$ 7,173,077
- **Disbursements**
 - Operating Disbursements \$ 6,686,254
 - All Other Disbursements 406,753
 - **Total Disbursements** \$ 7,093,007

Findings and Recommendations (p. 3)

- Misstatement of Financial Activity (Finding 1)
- Contributions from Unregistered Political Organizations (Finding 2)
- Apparent Coordinated Party Expenditures (Finding 3)
- Disclosure of Expenditures for Salary and Wages (Finding 4)

¹ 2 U.S.C. §438(b).

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

January 1, 2005 – December 31, 2006



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Part I

Background

Authority for Audit

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

Scope of Audit

This audit examined:

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

Changes to the Law

On December 1, 2005, the Commission voted to amend its rules to require state, district and local party committees to pay as administrative expenses the salaries, wages and fringe benefits of employees who spend 25 percent or less of their compensated time in a month on federal election activity (FEA) or activity in connection with a federal election (“covered employees”). The previous regulation that allowed party committees to use non-federal funds for salaries and wages for covered employees was struck down in *Shays v. FEC*. The revised rule became effective on January 19, 2006. (See Finding 4, Disclosure of Expenditures for Salary and Wages).

Part II Overview of Committee

Committee Organization

Important Dates	Tennessee Republican Party Federal Election Account
• Date of Registration	October 23, 1975
• Audit Coverage	January 1, 2005 - December 31, 2006
Headquarters	Nashville, Tennessee
Bank Information	
• Bank Depositories	Three
• Bank Accounts	12 Federal and 6 Non-federal accounts
Treasurer	
• Treasurer When Audit Was Conducted	Ed Roberson
• Treasurer During Period Covered by Audit	Joe R. Arnold (thru 2/17/05) Ed Roberson (2/18/05 to present)
Management Information	
• Attended Commission Campaign Finance Seminar	Yes
• Used Commonly Available Campaign Management Software Package	Yes
• Who Handled Accounting and Recordkeeping Tasks	Paid staff

Overview of Financial Activity (Audited Amounts)

Cash on hand @ January 1, 2005	\$ 5,973
Receipts	
○ Contributions from Individuals	\$ 3,483,766
○	
○ Contributions from Other Political Committees	367,326
○ Transfers from Affiliated/Other Party Committees	2,743,200
○ Transfers from Non-federal Account	555,805
○ All Other Receipts	22,980
Total Receipts	\$ 7,173,077
Disbursements	
○ Operating Disbursements	\$ 6,686,254
○ All Other Disbursements	406,753
Total Disbursements	\$ 7,093,007
Cash on hand @ December 31, 2006	\$ 86,043

Part III

Summaries

Findings and Recommendations

Finding 1. Misstatement of Financial Activity

On its reports as originally filed with the Commission, TRP significantly underreported receipts by \$2,227,811 and disbursements by \$1,440,129 for calendar year 2006. In addition, a comparison of TRP's amended reported figures to bank records revealed a misstatement of receipts, disbursements and cash-on-hand in both 2005 and 2006. For 2005, TRP overstated beginning cash on hand by \$33,780, understated receipts by \$117,371, understated disbursements by \$77,948 and understated ending cash on hand \$5,643. In 2006, receipts were understated by \$459,936, disbursements understated by \$159,582 and the ending cash on hand was understated by \$294,475. In response to the interim audit report recommendation, TRP amended its reports to materially correct the misstatements noted above.

(For more detail, see p. 4)

Finding 2. Contributions from Unregistered Political Organizations

A review of all contributions from unregistered political organizations indicated that TRP received \$114,395 in contributions that may not have been made with permissible funds. TRP refunded \$38,125 of these, but not in a timely manner. In response to the interim audit report recommendations, TRP materially complied with the Audit staff's recommendation by providing copies of the front and back of the negotiated contribution refund checks totaling \$71,845, and provided six check stubs, totaling \$4,325, for contribution refunds issued but not yet negotiated. The Committee did not address \$100 of these unregistered political contributions. (For more detail, see p. 7)

Finding 3. Apparent Coordinated Party Expenditures

TRP appeared to have exceeded the 2006 coordinated party expenditure limit by \$721,093. In response to the interim audit report, TRP provided a description of the procedure used for handling the non-allocable mail program. In response to the interim audit report, TRP provided additional documentation to support that there was volunteer involvement with the mail program. If these disbursements were considered not to have met the volunteer exemption, then TRP would have made an excessive coordinated contribution to Bob Corker for Senate in the amount of \$716,093. (For more detail, see p. 8)

Finding 4. Disclosure of Expenditures for Salary and Wages

TRP did not maintain monthly logs, time sheets or affidavits for its employees. Absent such documentation it is not possible to determine whether the salaries must be paid wholly from the federal account or may be paid from the non-federal account or allocated between the federal and non-federal accounts as administrative expenses. In response to the interim audit report recommendations, TRP provided some additional affidavits which stated that the employee did not spend more the 25% of compensated time on federal election activities and amended its reports which materially corrected the disclosure of the above salaries and payroll taxes. (For more detail, see p. 14)

Part IV

Findings and Recommendations

Finding 1. Misstatement of Financial Activity

Summary

On its reports as originally filed with the Commission, TRP significantly underreported receipts by \$2,227,811 and disbursements by \$1,440,129 for calendar year 2006. In addition, a comparison of TRP's amended reported figures to bank records revealed a misstatement of receipts, disbursements and cash-on-hand in both 2005 and 2006. For 2005, TRP overstated beginning cash on hand by \$33,780, understated receipts by \$117,371, understated disbursements by \$77,948 and understated ending cash on hand \$5,643. In 2006, receipts were understated by \$459,936, disbursements understated by \$159,582 and the ending cash on hand was understated by \$294,475. In response to the interim audit report recommendation, TRP amended its reports to materially correct the misstatements noted above.

Legal Standard

Contents of Reports. Each report must disclose:

- The amount of cash on hand at the beginning and end of the reporting period;
- The total amount of receipts for the reporting period and for the calendar year;
- The total amount of disbursements for the reporting period and for the calendar year; and
- Certain transactions that require itemization on Schedule A (Itemized Receipts) or Schedule B (Itemized Disbursements). 2 U.S.C. §434(b)(1), (2), (3), (4) and(5).

Facts and Analysis

1. Originally Reported Activity for 2006

As illustrated below, on the original disclosure reports filed with the Commission, TRP significantly underreported receipts and disbursements for calendar year 2006.

Comparison of Originally Reported 2006 Activity to Reconciled Bank Totals			
	Reported	Bank Records	Discrepancy
Receipts	\$3,463,205	\$5,691,016	\$2,227,811 understated
Disbursements	\$4,274,905	\$5,715,034	\$1,440,129 understated

Amended reports filed with the Commission showed a significant increase in financial activity. The Audit staff discussed the increased activity issue with the TRP Controller. In his written response, the Controller agreed that the figures originally reported by TRP were understated; nevertheless, he did not believe this finding was warranted. The Controller explained that he attended an FEC conference in Florida in the summer of 2006 and inquired about what committees should do if, due to time constraints, they are unable to file the reports timely and

accurately. The response was similar to the feedback he received from the Reports Analysis Division (RAD)² later on that year. According to the Controller, he was again told to file the report on time and submit an amended report with the correct figures on a later date.

Although it may be preferable to file a timely report that is incomplete rather than file nothing, the filing of a report that is materially misstated does not relieve the Treasurer of the obligation to file reports that are both timely and accurate. Amended reports were filed between 20 and 75 days after the original reports were filed that partially corrected the errors.

2. (Amended) Reported Activity for 2005 & 2006

The Audit staff reconciled (amended) reported activity to bank records for calendar years 2005 and 2006. The following charts outline the discrepancies for the beginning cash balances, receipts, disbursements, and the ending cash balances. The succeeding paragraphs explain why the differences occurred, if known.

2005 Committee Activity			
	Reported	Bank Records	Discrepancy
Beginning Cash Balance @ January 1, 2005	\$39,753	\$5,973	\$33,780 Overstated
Receipts	\$1,364,689	\$1,482,060	\$117,371 Understated
Disbursements	\$1,300,024	\$1,377,972	\$77,948 Understated
Ending Cash Balance @ December 31, 2005	\$104,418	\$110,061	\$5,643 Understated

The beginning cash on hand was overstated by \$33,780 and is unexplained, but likely resulted from prior period discrepancies.

The understatement of receipts was the result of the following:

• Receipts from the Republican National Committee (RNC) not reported	\$ 20,300
• Transfer from the non-federal account not reported	5,000
• Receipt from an individual not reported ³	100,000
• Unexplained difference	(7,929)
Net understatement of receipts	<u>\$ 117,371</u>

² When committees call for guidance on what to do when they are unable to file a complete report timely, RAD advises them to file as complete of a report as possible by the deadline, and then to file an amended report as soon as possible with any omitted information.

³ The excessive portion of this contribution (\$90,000) was timely resolved by transfer to the non-federal account.

The understatement of disbursements was the result of the following:

• Transfers to non-federal account not reported ⁴	\$ 91,864
• Unexplained difference	<u>(13,916)</u>
Net understatement of disbursements	<u>\$ 77,948</u>

The \$5,643 understatement of the closing cash on hand was the result of the misstatements described above.

2006 Committee Activity			
	Reported	Bank Records	Discrepancy
Beginning Cash Balance @ January 1, 2006	\$104,418	\$110,061	\$5,643 Understated
Receipts	\$5,231,080	\$5,691,016	\$459,936 Understated
Disbursements	\$5,555,452	\$5,715,034	\$159,582 Understated
Ending Cash Balance @ December 31, 2006	-\$208,432 ⁵	\$86,043	\$294,475 Understated

The understatement of receipts resulted from the following:

• Receipts from other (mostly unregistered) political committees not reported	\$ 49,000
• Receipts from the RNC not reported	183,900
• Transfers from the non-federal account not reported	128,949
• The total per Schedule A for itemized contributions from individuals (\$107,174) exceeded the amount reported (\$97,174) on the Detailed Summary Page for the Post-General Report	10,000
• Unexplained difference	<u>88,087</u>
Understatement of receipts	<u>\$ 459,936</u>

The understatement of disbursements resulted from the following:

• Transfers to non-federal account not reported	\$ 14,050
• Net errors in reporting of disbursements to various vendors	75,523
• Unexplained difference	<u>70,009</u>
Understatement of disbursements	<u>\$ 159,582</u>

The \$294,475 understatement of the closing cash on hand was the result of the misstatements described above.

⁴ This amount includes the \$90,000 transfer to the non-federal resolving the excessive contribution discussed in footnote 3.

⁵ The negative cash balance resulted from reporting errors; the balance in the bank was never negative. This column does not foot as a result of a discrepancy between the ending reported cash balance of one report and the beginning cash on the succeeding report (an \$11,522 understatement by TRP). On March 26, 2007, after the Audit Notification Letter dated March, 15, 2007, TRP amended this report and corrected the cash on hand balance.

The Audit staff discussed the misstatements for 2005 and 2006 with TRP's representatives during the exit conference and presented them with copies of relevant workpapers. TRP representatives stated that corrective amendments would be filed.

Interim Audit Report Recommendation and Committee Response

The Audit staff recommended TRP provide any additional information or written comments that it considered relevant to the misstatement of activity on its original reports filed for 2006 and amend its reports to correct the misstatements for 2005 and 2006 as noted above. TRP should also have amended its most recently filed report to correct the cash on hand balance with an explanation that the change resulted from a prior period audit adjustment and TRP should have reconciled the cash balance of its most recent report to identify any subsequent discrepancies that may have impacted the \$294,475 adjustment recommended by the Audit staff. TRP amended its reports to materially correct the misstatements noted above. Its response did not provide any additional comments on the misstatements of activity on its reports as originally filed. TRP has indicated that it will be amending the most current report to correct the cash on hand balance.

Finding 2. Contributions from Unregistered Political Organizations

Summary

A review of all contributions from unregistered political organizations indicated that TRP received \$114,395 in contributions that may not have been made with permissible funds. TRP refunded \$38,125 of these, but not in a timely manner. In response to the interim audit report recommendations, TRP materially complied with the Audit staff's recommendation by providing copies of the front and back of the negotiated contribution refund checks totaling \$71,845 and provided six check stubs, totaling \$4,325, for contribution refunds issued but not negotiated. The Committee did not address \$100 of these unregistered political contributions.

Legal Standard

- A. Party Committee Limits.** A party committee may not receive more than a total of \$10,000 per year from any person except that a multicandidate political committee may not contribute more than \$5,000. 2 U.S.C. §441a(a)(1)(D) and 11 CFR §§110.1(a) and (c)(5), 110.2(d) and 110.9.
- B. Handling Contributions That Appear Impermissible or Excessive.** If a committee receives a contribution that appears to be impermissible or excessive, the committee must either:
1. Return the questionable check to the donor; or
 2. Deposit the check into its federal account and:
 - Keep enough money in the account to cover all potential refunds;
 - Keep a written record explaining why the contribution may be illegal;

- Include this explanation on Schedule A if the contribution has to be itemized before its legality is established. 11 CFR §103.3(b)(3), (4) and (5).

Facts and Analysis

During the review of contributions, the Audit staff identified 31 unregistered political organizations that made 37 contributions totaling \$114,395 to TRP, of which \$38,125 was refunded in an untimely manner. TRP did not have any records available to show that these contributions from unregistered political organizations were made with permissible funds. One of these unregistered political organizations (Republican Governors Association Federal PAC) contributed \$50,225 to TRP and therefore exceeded the \$10,000 contribution limit by \$40,225 if the contribution was determined to have been made with permissible funds. TRP did refund \$225 of this excessive contribution, but not in a timely manner.

The Audit staff discussed this matter with TRP's representatives during the exit conference and presented them with copies of relevant workpapers. TRP representatives stated that they would review the schedules and comply accordingly.

Interim Audit Report Recommendation and Committee Response

The Audit staff recommended TRP provide evidence demonstrating that the contributions in question were made with permissible funds and not excessive. Alternatively, TRP should have refunded the impermissible funds and/or excessive contribution and provided evidence of such refunds (copies of the front and back of the negotiated refund checks). If funds were not available to make the necessary refunds, TRP should have disclosed the refunds due on Schedule D (Debts and Obligations) until funds became available to make the refunds.

In response to the interim audit report recommendations, TRP materially complied with the Audit staff's recommendation by providing copies of the front and back of negotiated contribution refund checks totaling \$71,845. In addition, it provided six check stubs, totaling \$4,325, for contribution refunds issued but not yet negotiated. TRP did not address \$100 of these unregistered political contributions.

Finding 3. Apparent Coordinated Party Expenditures

Summary

TRP appeared to have exceeded the 2006 coordinated party expenditure limit by \$721,093. In response to the interim audit report, TRP provided a description of the procedure used for handling the non-allocable mail program. In response to the interim audit report, TRP provided additional documentation to support that there was volunteer involvement with the mail program. If these disbursements were considered not to have met the volunteer exemption, then TRP would have made an excessive coordinated contribution to Bob Corker for Senate in the amount of \$716,093.

Legal Standard

A. Limits on Contributions Made by National Parties.⁶ National party committees must comply with the contribution limits below:

- \$5,000 per election to a House or Presidential campaign.⁷
- \$35,000 to a Senate campaign for the entire campaign period. This limit is shared by the national party committee and the Senate campaign committee.
- \$5,000 per year to a separate segregated fund (corporate or labor PAC) or a nonconnected committee.
- Unlimited transfers to other party committees. 2 U.S.C. §441a(a) and (a)(h).

B. Limits on Contributions Made by State and Local Party Committees.

- A state party committee shares its limits with local party committees in its state unless a local committee can demonstrate its independence. 11 CFR §110.3(b)(3).
- State and local party committees must comply with the contribution limits below:
 - \$5,000 per election to a Federal campaign if the contributing committee has qualified as a multicandidate committee (see below).
 - \$2,100 per election to a Federal campaign if the contributing committee has not qualified as a multicandidate committee.
 - \$5,000 per year to a separate segregated fund (corporate or labor PAC) or a nonconnected committee.
 - Unlimited transfers to other party committees. 2 U.S.C. §441a(a).

C. Coordinated Party Expenditures. National party committees and state party committees are permitted to purchase goods and services on behalf of candidates in the general election—over and above the contributions that are subject to contribution limits described above. Such purchases are referred to as “coordinated party expenditures.” They are subject to the following rules:

- The amount spent on “coordinated party expenditures” is limited by statutory formulas that are based on the Cost of Living Adjustment (COLA) and the voting age population.
- Party committees are permitted to coordinate the spending with the candidate committees.
- The parties may make these expenditures only in connection with the general election.
- The party committees—not the candidates—are responsible for reporting these expenditures.
- If the party committee exceeds the limits on coordinated party expenditures, the excess amount is considered an in-kind contribution, subject to the contribution limits described above.
- A national or state party committee may assign all or part of its coordinated party spending authority to another party committee. 2 U.S.C. §441a(d) and 11 CFR §§109.32(b) and 109.33(a).

⁶ A party’s national committee, Senate campaign committee, and House campaign committee are each considered a national party committee, and each one has a separate limit except with respect to Senate campaigns.

⁷ This assumes the national party committee has qualified as a multicandidate committee.

D. Coordinated Communication. A communication is coordinated with a candidate, an authorized committee, a political party committee, or an agent of any of the foregoing when the communication:

1. Is paid for by a person other than that candidate, authorized committee, political party committee, or agent of any of the foregoing.
2. Satisfies at least one of the content standards in paragraph (c) of this section. One of the four content standards described in this section as satisfying this requirement is a public communication that expressly advocates the election or defeat of a clearly identified candidate for Federal office.
3. Satisfies at least one of the conduct standards in paragraph (d) of this section. One of the six conduct standards described in this section as satisfying this requirement is common vendor if all of the following statements are true:
 - The person paying for the communication contracts with or employs a commercial vendor to create, produce, or distribute the communication.
 - That commercial vendor has provided certain services to the candidate in the current election cycle. Such services include the development of media strategy; selection of audiences; polling; fundraising; developing the content of a public communication; producing a public communication; identifying voters or developing voter lists, mailing lists, or donor lists; selecting personnel, contractors, or subcontractors; or consulting or otherwise providing political or media advice; and
 - That commercial vendor uses or conveys to the person paying for the communication: information about the candidate's campaign plans, projects, activities, or needs and that information is material to the creation, production, or distribution of the communication; or information used previously by the commercial vendor in providing services to the candidate and that information is material to the creation, production, or distribution of the communication. 11 CFR §109.21(a)(1), (2) and (3), (c)(3), and (d)(4).

E. Expressly Advocating Definition. Expressly advocating means any communication that:

1. Uses phrases such as “vote for”, “re-elect”, “support”, “cast your ballot for”, “vote against”, or words which in context can have no other reasonable meaning than to urge the election or defeat of one or more clearly identified candidate(s); or
2. When taken as a whole could only be interpreted by a reasonable person as containing advocacy of the election or defeat of one or more clearly identified candidate(s). 11 CFR §100.22.

F. Volunteer Activity for Party Committee. The payment by a state committee of a political party of the costs of campaign materials (such as pins, bumper stickers, handbills, brochures, posters, party tabloids or newsletters, and yard signs) used by such committee in connection with volunteer activities on behalf of any nominee(s) of such party is not a contribution or disbursement, provided that the following conditions are met:

1. Such payment is not for cost incurred in connection with any broadcasting, newspaper, magazine, bill board, direct mail, or similar type of general public communication. The term direct mail means any mailing(s) by a commercial vendor or any mailing(s) made from commercial lists.

2. The portion of the payment allocable to federal candidates must be paid with federal funds.
3. Such payment is not made from contributions designated by the donor to be spent on behalf of a particular candidate for Federal office.
4. Such materials are distributed by volunteers and not by commercial or for profit operations.
5. If made by a political committee such payments shall be reported by the political committee as a disbursement.
6. The exemption is not applicable to campaign materials purchased by the national party committees. 11 CFR §100.87 (a), (b), (c), (d), (e) and (g) and 11 CFR §100.147 (a), (b), (c), (d), (e) and (g).

Facts and Analysis

The Audit staff reviewed all disbursements related to various forms of media to determine whether TRP complied with applicable regulations regarding the production and dissemination of printed material and radio and television advertisements. If it contained Federal candidate support, the Audit staff reviewed the supporting documentation to determine if evidence was found which would suggest that coordination with the candidate might exist. During this review, the Audit staff noted that the coordinated party expenditure limit for the state of Tennessee in the 2006 cycle for a Senate candidate was \$362,200. As cited above, the national party committee and state party committees each have separate coordinated expenditure limits for a total combined limit in Tennessee of \$724,400. By a letter dated September 1, 2006, the Tennessee Republican Party assigned their limit to the National Republican Senatorial Committee (NRSC). NRSC spent most of this combined limit on media totaling \$714,630 that supported Bob Corker for Senate.

During this review, the Audit staff identified disbursements to one vendor, Creative Direct, LLC, for the production, printing and mailing of numerous direct mail pieces. TRP disclosed these disbursements either as federal election activity disbursements or federally funded operating disbursements. These disbursements to Creative Direct, LLC totaled \$721,093 and were incurred during the period September through November of 2006. All of these disbursements were in support of Bob Corker for Senate or in opposition to his opponent Congressman Harold Ford, Jr. Bob Corker's campaign used this same vendor for direct mail disbursements which totaled \$680,570 and were incurred during the period April through September of 2006. NRSC also utilized this same vendor for a coordinated expenditure incurred on September 7, 2006, totaling \$66,417.

For the coordinated expenditure standard to apply, two conditions must be met: Content and Conduct. TRP appeared to have met the content standard, since the disbursements were for a public communication that expressly advocated the election or defeat of a clearly identified candidate for federal office. Although there was no language such as "vote for" or "defeat" in the material, the Audit staff determined that it could only be interpreted by a reasonable person as containing advocacy of the election of Bob Corker for Senate or the defeat of Harold Ford, Jr. For example, one of the direct mail pieces contains a picture of Bob Corker and discusses his plan for securing the borders and cracking down on illegal immigration on one side; the other side has a picture of his opponent and states, among other things, "Too bad Liberal Congressman

Harold Ford is all talk – no action on illegal immigration.” Another direct mail piece pictures Congressman Ford and notes that when he “...did show up to vote, he VOTED AGAINST the recent TAX CUTS for Tennessee families.” The piece also states that he is “Tennessee’s Most Liberal Congressman.”

TRP also met one of the types of conduct to satisfy the conduct standard: Common Vendor. All three committees (NRSC, Bob Corker for Senate, and TRP) used a common vendor, Creative Direct, LLC.

- NRSC reported a coordinated expenditure for direct mail costs totaling \$66,417 on September 7, 2006.
- Bob Corker for Senate incurred direct mail costs totaling \$680,570 during April through September of 2006.
- TRP incurred direct mail costs totaling \$721,093 during September through November of 2006.

Although there was no documentation to indicate that Creative Direct, LLC conveyed information about the candidate’s campaign plans or needs to TRP, there was sufficient evidence to suggest that coordination might have existed.

At the exit conference, the Audit staff discussed this matter with TRP’s representatives who stated they would review their records. Subsequently, the Audit staff provided a schedule of the \$721,093 possible coordinated expenditures for their review.

Subsequent to the exit conference, the Audit staff sent letters to TRP and Creative Direct, LLC, which contained questions to clarify whether there was coordination. The responses from TRP and Creative Direct, LLC indicated that they considered the direct mailings to be exempt volunteer activities. TRP stated: “We thought these were exempt. We had an official candidate, it was in the General, all processed and stamped in Tennessee, it was non-allocable, paid with Tennessee Victory funds, used volunteers.” Creative Direct’s response indicated its services were limited to the preparation of mail and handouts that would be used in connection with volunteer activities.

Interim Audit Report Recommendation and Committee Response

The Audit staff recommended TRP provide evidence that detailed if there was substantial volunteer involvement and discussed whether volunteers did any of the separation and distribution activities for the mailers such as: unpacking, bundling, sorting by zip code or other types of sorting, bagging, tagging, wrapping, loading, weighing, or delivering the mailers to the Post Office; or evidence to support that no coordination existed between TRP and Bob Corker for Senate. This evidence could have included samples of material produced and printed by Creative Direct, LLC for each of the committees, i.e. NRSC and Bob Corker for Senate; and a statement from the vendor detailing how orders were placed and how it avoided information sharing among these three clients. If the evidence provided indicated there was volunteer involvement or that no coordination occurred, then no further action was recommended. However, if the evidence provided indicated that coordination did occur, then the Audit staff recommended that TRP seek reimbursement from the candidate in the amount of \$716,093.⁸

⁸ TRP did not contribute to Bob Corker for Senate; therefore, the amount of reimbursement sought should be \$716,093 (\$721,093-\$5,000).

In response to the interim audit report, TRP provided a description of the procedure used for handling the non-allocable mail program during the fall of 2006. The response noted that volunteers at the Victory Field office were recruited by TN GOP Victory staff and organized to complete the following tasks:

- Volunteers unloaded the boxes of unstamped and unaddressed mail from wrapped pallets, taking them into the Victory office.
- Volunteers stacked the boxes inside the office.
- Volunteer Team Leader opened boxes and stacked the unmarked mail on a series of tables for volunteers to stamp.
- Volunteers sitting at the tables applied the Tennessee Republican Party indicia or stamp with a hand operated ink stamp to each piece of mail.
- Volunteers placed the mail pieces back into boxes after they had been hand stamped with the Tennessee Republican Party's indicia.
- Volunteers stacked the boxes of stamped mail near the door.
- Volunteers loaded the boxes back onto the truck for delivery to the mail house to address the mail pieces.

The response stated that during this process a volunteer physically touched each piece of mail to apply the hand operated ink stamp that was used to apply the non-profit indicia for postage used by the Tennessee Republican Party. Additionally, volunteers unloaded the delivery of unstamped mail pieces, unpackaged the mail pieces from boxes for stamping, repackaged the mail pieces after stamping and reloaded the delivery trucks with the stamped mail.

In the Audit staff's opinion, the limited participation by volunteers detailed by TRP does not appear to meet the requirements of the volunteer materials exemption. In fact, this level of volunteer activity is specifically addressed by MUR 2559 (Oregon Republican Party) and MUR 2288 (Shimizu for Congress) as not substantial enough for the volunteer exemption to apply. However, the Commission recently considered the volunteer exemption in the context of MUR 5598 (Utah Republican Party) which had very similar facts to the volunteer activity described by TRP. In its decision, the Commission did not expressly conclude whether the volunteer exemption had, or had not, been met; rather it cited the complicated history relative to the volunteer exemption and dismissed the matter in an exercise of its prosecutorial discretion. The Commission also indicated a need for more detailed guidance to clarify the volunteer exemption. If these disbursements were considered not to have met the volunteer exemption, then TRP would appear to have made an excessive coordinated contribution to Bob Corker for Senate in the amount of \$716,093; however, no further corrective action is necessary to resolve this finding.

Finding 4. Disclosure of Expenditures for Salary and Wages

Summary

TRP did not maintain monthly logs, time sheets or affidavits for its employees. Absent such documentation it is not possible to determine whether the salaries must be paid wholly from the federal account or may be paid from the non-federal account or allocated between the federal and non-federal accounts as administrative expenses. In response to the interim audit report recommendations, TRP provided some additional affidavits which stated that the employee did not spend more the 25% of compensated time on federal election activities and amended its reports which materially corrected the disclosure of the above salaries and payroll taxes.

Legal Standard

A. Accounts for Federal and Non-federal Activity. A party committee that finances political activity in connection with both federal and non-federal elections shall establish two accounts (federal and non-federal) and allocate shared expenses, those that simultaneously support federal and non-federal election activity between the two accounts. Alternatively, the committee may conduct both federal and non-federal activity from one bank account, considered a federal account. 11 CFR §102.5(a)(1)(i).

B. Paying for Allocable Expenses. Commission regulations offer party committees two ways to pay for allocable shared federal/non-federal expenses.

- They may pay the entire amount of the shared expense from the federal account and transfer funds from the non-federal account to the federal account to cover the non-federal share of that expense; or
- They may establish a separate, federal allocation account into which the committee deposits funds from both its federal and non-federal accounts solely for the purpose of paying the allocable expenses of shared federal/non-federal activities. 11 CFR §106.5(g)(1)(i) and (ii)(A).

C. Reporting Allocable Expenses. A political committee that allocates federal/non-federal expenses must report each disbursement it makes from its federal account (or separate allocation account) to pay for a shared federal/non-federal expense. Committees report these kinds of disbursements on Schedule H4 (Joint Federal/Non-Federal Activity Schedule). 11 CFR §104.10(b)(4).

D. Costs allocable by State party committees between Federal and Non-federal accounts (Effective prior to January 19, 2006). State party committees must pay salaries and wages from funds that comply with State law for employees who spend 25% or less of their time in any given month on federal election activity. 11 CFR §106.7(c)(1).

E. Costs allocable by State party committees between Federal and Non-federal accounts (Effective on January 19, 2006). State party committees must either pay salaries, wages, and fringe benefits for employees who spend 25% or less of their time in a given month on Federal election activity with funds from their Federal account, or with a combination of funds from their federal and non-federal accounts. 11 CFR §106.7(c)(1), as amended January 19, 2006.

F. Allocation Ratios and Record-Keeping for Administrative Expenses. The percentages used for such allocations vary based on whether a Presidential and/or a Senate candidate appears, or doesn't appear, on the ballot in any even year. For the period 2005-2006, which included an even year in which a Senate candidate, but no Presidential candidate, appeared on the ballot, TRP chose the appropriate percentage, 21%, for a State committee to allocate administrative expenses to their Federal account. Committees must keep a monthly log of the percentage of time each employee spends in connection with a Federal election. 11 CFR §106.7(d)(1) and (2)(iii).

Facts and Analysis

The Audit staff's review of payroll expenses indicated that TRP did not maintain monthly logs, time sheets or affidavits for its employees that worked for either the federal or non-federal accounts. Therefore, based on the regulatory change effective January 19, 2006 (See page 1, Changes to the Law), the Audit staff applied the following to assess salary expenditures:

1. For salary and payroll tax payments made before January 19, 2006:
If there is a monthly log, time sheet or affidavit which states that:
 - the time spent on federal activity is less than or equal to 25%, the payment can be made from the non-federal account and it requires nothing further of the federal committee; or
 - the time spent on federal activity exceeds 25%, or for which there is no documentation indicating a lesser percentage, the federal committee must disclose these payments on Schedule B, Line 30b, as non-allocable Federal Election Activity (FEA). Should such payments during this period be made from the non-federal account, an appropriate memo Schedule B should be filed.

2. For salary and payroll tax payments made on or after January 19, 2006:
If there is monthly log, time sheet or affidavit which states that:
 - the time spent on federal activity each month is none, or 0%; this may be paid by the non-federal account and requires nothing further of the federal committee; or
 - the time spent on federal activity is less than or equal to 25%; this payment must be made from the federal account and disclosed by the federal committee on Schedule H4 as allocable administrative activity, for which reimbursement may be sought at the administrative ratio. Should such payments during this period be made from the non-federal account, an appropriate memo Schedule H4 should be filed; or
 - the time spent on federal activity exceeds 25%, or for which there is no documentation indicating a lesser percentage, the federal committee must disclose these payments on Schedule B, Line 30b, as non-allocable FEA activity. Should such payments during this period be made from the non-federal account, an appropriate memo Schedule B should be filed.

The results of the Audit staff's review of salary and payroll taxes, to include consideration of affidavits provided **at the time of the interim audit report**, are as follows:

1. Salary and payroll tax payments made from the non-federal account:
 - With respect to salary payments from this account totaling \$23,114, TRP provided affidavits which stated that four individuals spent less than or equal to 25% of their time per month on federal activities during the period on or after January 19, 2006. In addition, there were payroll tax payments of \$6,096 which relate to these salary payments paid during this period. Therefore, TRP is required to disclose as memo entries on Schedule H4 the salary payments of \$23,114 and tax payments of \$6,096.
 - TRP failed to provide documentation detailing the time spent on federal activities for employees whose earnings totaled \$207,048 for the period before January 19, 2006 and \$37,792 for the period on or after January 19, 2006. In addition, there were payroll tax payments of \$53,198 which relate to the salary payments, totaling \$207,048, paid during the period before January 19, 2006 and the \$9,968 payroll tax payments that relate to the \$37,792 salaries paid on or after January 19, 2006. Absent the supporting documentation, TRP was required to disclose these salary and payroll tax payments as memo entries on Schedule B, Line 30b.
2. Salary and payroll tax payments made from the federal account:
 - TRP failed to provide supporting documentation detailing the time spent on federal activities for employees whose earnings totaled \$23,194 for the period before January 19, 2006 and \$665,209 for the period on or after January 19, 2006. In addition, payroll tax payments of \$2,314 which relate to the salary payments, totaling \$23,194, paid during the period before January 19, 2006 and \$161,923 payroll tax payments that relate to the \$665,209 salaries paid on or after January 19, 2006. TRP reported these salary and tax payments as allocable expenses on Schedule H4. Absent the supporting documentation, TRP should have disclosed these salary and tax payments on Schedule B, Line 30b for both periods.

The Audit staff compared reimbursements received from the non-federal account for its share of allocable activity and made certain other adjustments. This analysis indicated there was no funding of federal activity by the non-federal accounts as a result of the activity discussed above.

The Audit staff discussed this matter with TRP's representatives during the exit conference, and presented them with copies of relevant work papers. TRP representatives stated that they would review the schedules and amend its reports accordingly.

Interim Audit Report Recommendation and Committee Response

The Audit staff recommended TRP provide monthly logs or time sheets from each employee for each month worked attesting to the time spent by the employee for the period employed by TRP, or affidavits from each employee which provide information similar to a monthly log about employee activities, and amend its disclosure reports accordingly. If no additional documentation was provided, TRP should have amended its disclosure reports as detailed above.

In response to the interim audit report recommendations, TRP provided some additional affidavits which stated that the **employees** did not spend more than 25% of compensated time on

federal election activities and amended its reports which materially corrected the disclosure of the above salaries and payroll taxes.



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20543

June 15, 2009

MEMORANDUM

TO: John D. Gibson
Chief Compliance Officer

Joseph F. Stoltz
Assistant Staff Director

FROM: Christopher Hughey *pch*
Deputy General Counsel

Lawrence L. Calvert, Jr. *[Signature]*
Associate General Counsel

Lorenzo Holloway *[Signature]*
Assistant General Counsel
For Public Finance and Audit Advice

Delanie DeWitt Painter *[Signature]*
Attorney

SUBJECT: Final Audit Report on Tennessee Republican Party (LRA # 745)

I. INTRODUCTION

The Office of General Counsel has reviewed the Final Audit Report ("Proposed Report") on the Tennessee Republican Party ("TRP"). We offer the following comments regarding Finding 3 (Excessive Coordinated Party Expenditures) in the Proposed Report. We concur with the Audit staff that TRP did not meet the volunteer materials exemption and recommend that the Audit staff revise the Proposed Report to: 1) summarize the Commission's actions in MUR 5598; and 2) state that it appears that TRP might have made an excessive coordinated contribution of \$716,093 but no further corrective action by TRP is necessary to resolve this finding. We concur with the remaining findings and issues in the Proposed Report not specifically addressed in this memorandum. If you have any questions, please contact Delanie DeWitt Painter, the attorney assigned to this audit.¹

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

II. DIRECT MAIL EXPENSES DID NOT MEET THE VOLUNTEER MATERIALS EXEMPTION (Finding 3)

The Proposed Report concludes that TRP exceeded the coordinated party expenditure limits by \$716,093 because it paid for direct mail supporting Bob Corker for Senate which, the auditors contend, meets the content and common vendor conduct standards for coordinated expenditures. See 11 C.F.R §§ 109.37, 109.21. TRP assigned its coordinated party expenditure limitation to the National Republican Senatorial Committee, which spent most of the combined limit on media supporting Bob Corker for Senate. The auditors questioned whether TRP disbursements to Creative Direct, LLC for direct mail which appears to support Bob Corker were excessive coordinated expenses because the Corker campaign had previously used the same vendor. In response to Audit questions, TRP and Creative Direct indicated that they considered the direct mailings to be exempt volunteer activities. See 2 U.S.C. § 431(8)(B)(ix) and (9)(B)(viii); 11 C.F.R. §§ 100.87 and 100.147. In determining whether mailings qualify for the volunteer materials exemption, the Commission has considered whether there was sufficient volunteer involvement based on the specific facts and circumstances of the case, even where there was some involvement by a commercial vendor. If the direct mail pieces qualify for the volunteer materials exemption, the possible "common vendor" coordination issue would be immaterial because exempt activity may be coordinated, and TRP would not have exceeded the coordinated party expenditure limitations by paying for the direct mail.

The Interim Audit Report ("IAR") requested additional information about the volunteer activities. In response, TRP described its procedures at the Victory Field office. TRP recruited volunteers and organized them to complete the following tasks: 1) unloaded boxes of unmarked mail (without stamps and addresses) from wrapped pallets and carried them into the office; 2) stacked the boxes in the office; 3) sat at tables and applied the Tennessee Republican Party non-profit postage indicia with a hand operated ink stamp to each piece of mail; 4) placed the mail pieces back into boxes after they had been stamped with the party indicia; 5) stacked the boxes of mail near the door and 6) loaded the truck for delivery to the mail house to address the mail. A Volunteer Team Leader opened the boxes and stacked the mail on tables for the volunteers to stamp. TRP stated that during this process a volunteer physically touched each piece of mail to hand stamp it with the non-profit party indicia. The Audit Division concludes that this "limited participation" by volunteers does not meet the requirements of the volunteer materials exemption and that TRP made an excessive coordinated contribution and should seek reimbursement from Bob Corker for Senate in the amount of \$716,093.

Following the Commission's approval of the IAR, the Commission considered the volunteer materials exemption in the context of Matter Under Review ("MUR") 5598. See Statement of Reasons of Commissioners Petersen, Bauerly, Hunter and Weintraub in MUR 5598, Utah Republican Party et al. (April 9, 2009) ("MUR 5598 SOR"). That matter had very similar facts to the volunteer activity described by TRP here. In the Utah Republican Party ("URP") case, this Office concluded that the volunteer activity was not sufficient to meet the volunteer materials exemption. URP claimed that its mailers met the volunteer materials exemption because volunteers processed, sorted, and hand-stamped the mail pieces and delivered

them to the post office for mailing, but this Office's investigation found that URP's volunteers only stamped the bulk mail permit indicia on the mailers and helped load boxes of mailers into a truck that took the mailers back to the mail vendor, which then printed addresses, sorted them by postal route and delivered them to the post office for mailing. *Id.* at 3. The majority of the Commission neither accepted nor rejected this Office's legal analysis but instead, concluded that there is great confusion in the regulated community about how much volunteer involvement is necessary to qualify for the exemption. The four Commissioners concluded that they "voted to dismiss this matter against all parties in an exercise of our prosecutorial discretion." MUR 5598 SOR at 2, citing *Heckler v. Chaney*, 470 U.S. 821, 831 (1985). The Commissioners explained:

The Office of the General Counsel concluded that the URP's mailers did not qualify for the exemption. URP stated that it believed that its actions were consistent with the exemption, and given the complicated history of the application of the volunteer materials exemption, we voted to dismiss this matter in an exercise of our prosecutorial discretion. *See Heckler v. Chaney* 470 U.S. 821, 831 (1985). We plan to issue more detailed guidance to clarify the volunteer materials exemption and the circumstances in which it applies.

Id. at 4.

MUR 5598 is not cited in the Proposed Report, but is only noted in the cover memorandum to this Office, which states that the Audit staff concluded that TRP did not meet the requirements for the volunteer materials exemption because the MUR 5598 SOR "is inconclusive as it does not address whether the activity by the volunteers did, or did not, meet the requirements for the exemption."

This Office concurs with the Audit Division's conclusion that TRP's volunteer activity was not sufficient to meet the volunteer materials exemption. Our conclusion is consistent with this Office's analysis of the similar facts in MUR 5598. In both matters, the volunteers did little more than stamping the indicia on the direct mail pieces, and it appears that most of the processing and mailing was done by the direct mail vendor. This Office does not believe such minimal volunteer activity is sufficient to meet the volunteer materials exemption. Nevertheless, the Proposed Report should also acknowledge the outcome of MUR 5598. While the Commission did not expressly conclude in MUR 5598 that the volunteer activity was substantial enough to meet the volunteer materials exemption, it also did not conclude that the activity was *not* substantial enough to meet the exemption. Rather, the Commission discussed the "complicated history of the application of the volunteer materials exemption" and indicated a need for "more detailed guidance to clarify the volunteer materials exemption and the circumstances in which it applies." MUR 5598 SOR at 4. In the absence of that additional Commission guidance clarifying the application of the volunteer materials exemption, we do not

Memorandum to Joseph F. Stoltz
Final Audit Report
Tennessee Republican Party (LRA 745)
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think this finding should be pursued further in the audit process or in any other context that might otherwise be appropriate.²

We recommend that the Audit Division revise the Proposed Report at Finding 3. in two ways. First, the finding should summarize the Commission's actions in MUR 5598. Second, the finding should be less definitive about the potential violation and conclude that it appears that TRP might have made an excessive coordinated contribution of \$716,093 but no further corrective action by TRP is necessary to resolve this finding.

² Currently, the volunteer materials exemption issue is not the subject of any proposed rulemaking. If the Audit Division believes that this audit should be the vehicle in which the Commission issues this guidance, then the Audit Division should indicate this in the cover memorandum that forwards the Audit Report to the Commission.

CASE INDEX FORM

CASE NO. & NAME: A07-05 Tennessee Republican Party Federal Election Account

STAFF ASSIGNED: Alex Boniewicz, Audit Manager
Jim Miller, Lead Auditor

TELEPHONE: Audit - 202-694-1200

<u>DATE</u>	<u>DOCUMENT</u>
February 8, 2007	RAD Referral
February 28, 2007	Audit Scope Determination
August 13, 2008	Interim Audit Report Legal Analysis
September 30, 2008	Interim Audit Report
April 1, 2009	Response to Interim Audit Report
June 15, 2009	Legal Analysis on Final Audit Report
August 25, 2009	Final Audit Report

The above documents can be found at the following server location:
\\Ntsrv1\ voting ballot matters\Audit\Tennessee Republican Party Federal Election Account

If you have any questions, please contact Alex Boniewicz at 694-1200.