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FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

SEP 21 2000

MEMORANDUM

AGENDA ITEM
For Meeting of: 9-28-00

TO: The Commission

THROUGH: James A. Pehrkon
Staff Director

FROM: Lawrence M. Noble
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SUBJECT: Soft Money Rulemaking; Analysis, Recommendations and Draft Final Rules

I. INTRODUCTION

On July 13, 1998, the Commission published a Notice of Proposed Rulemaking ("NPRM") seeking comment on proposed rules relating to the receipt and use of prohibited and excessive contributions by party committees, also known as "soft money." The Commission held a public hearing on November 18, 1998, to receive testimony on the NPRM.

The Office of General Counsel has prepared this memorandum on the issues raised in the soft money rulemaking. The memo summarizes the comments and testimony received, reviews the applicable law, and makes recommendations for Commission action.

II. EXECUTIVE SUMMARY

In summary, the Office of General Counsel recommends that the Commission take the following actions:[1]

1) **Issue new rules to prohibit the receipt and use of soft money by national party committees, including the Senate and House campaign committees, with certain limited exceptions.**

As will be discussed in detail below, the Office of General Counsel believes that individuals, corporations, and labor organizations are making soft money donations to the national party committees in a manner which circumvents the prohibitions and limitations in the Federal Election Campaign Act, 2 U.S.C. 431 et seq. ["FECA" or "the Act"], that these donations are increasing in frequency and amount, and that the resulting use of soft money by the national party committees is having a significant influence on federal elections.

Therefore, we recommend that the Commission revise the current rules to prohibit the receipt of soft money by national party committees, with certain limited exceptions, in order to reduce the influence of soft money in federal elections.

Specifically, we recommend that the Commission prohibit the national party committees from operating nonfederal accounts, and require them to make all disbursements from funds that are permissible under the FECA, subject to two exceptions: (1) An exception for the building fund accounts authorized by the FECA that applies to all national party committees, including the Senate and House campaign committees; and (2) An exception that allows national party committees other than the Senate and House campaign committees to maintain a second nonfederal account to be used exclusively for the purpose of making direct donations to nonfederal candidates, or to make direct disbursements solely for the purpose of expressly advocating the election or defeat of clearly identified nonfederal candidates.

We have prepared draft final rules that would implement these recommendations. See 11 CFR 102.5, 106.1, 106.5, below. We recommend that these rules be promulgated with an effective date of January 1, 2001.

2) **Make no substantive changes to the current allocation rules for state and local party committees.**

The Office of General Counsel has examined the rulemaking record and concluded that it is premature to recommend changes to the allocation rules applicable to state and local party committees. As will be discussed in detail below, most of the evidence of the use of soft money to influence federal elections involves

[1] Our formal recommendations are set out on page 43 of the document.

soft money raised and spent by the national party committees, either directly or through transfers to state and local committees. There is less evidence that state and local party committees are using significant amounts of soft money for this purpose. We believe the changes we recommend above regarding national party committees will address many of the significant soft money issues. If so, restrictions on state and local party committee allocation may be unnecessary.

We are aware that limiting soft money donations to the national party committees without limiting state and local party committee allocation may simply redirect the flow of soft money to state and local committees, and may not reduce the overall amount used to influence federal elections. However, we believe the Commission would be better served by waiting for evidence of such a shift before further considering changes in the allocation rules for these entities. We also recognize that the legislative history of the FECA could be read to limit the Commission's authority over allocation by state and local party committees.

Therefore, we recommend that the Commission adopt a step-by-step approach, and defer any revisions to the state and local party committee allocation rules until the impact of the draft final rules regarding national party committees can be determined.

3) **Clarify the rules regarding solicitations of party committee contributions by federal candidates and officeholders.**

The Office of General Counsel believes that funds donated to party committees in response to a solicitation by a federal candidate or officeholder should be subject to the prohibitions and limitations of the Act, unless the donor specifically designates the donation for a nonfederal account. In our view, current section 102.5(a)(3) states this principle. However, this provision has been subjected to differing interpretations. Therefore, we urge the Commission to revise section 102.5(a)(3) to clarify that amounts received in response to party committee solicitations made by federal candidates and officeholders will be subject to the prohibitions and limitations of the Act, unless they are expressly designated for an otherwise permissible nonfederal account or building fund account of the recipient committee. We also recommend including a parallel provision for national party committees. See sections 102.5(a)(3) and (c)(3) of the draft final rules. We recommend that these changes be promulgated with an effective date of January 1, 2001.

III. BACKGROUND

The Act limits the amount that individuals can give to candidates, political committees and political parties for use in federal elections. 2 U.S.C. § 441a. The Act also prohibits corporations and labor organizations from contributing their general treasury funds for these purposes. 2 U.S.C. § 441b. Federal contractors are also prohibited from making these contributions. 2 U.S.C. § 441c, 11 CFR 115.2(a). Note that, under 2 U.S.C. §§ 441b

and 441e, national banks, Congressionally-chartered corporations, and foreign nationals are prohibited from making contributions in connection with any election to any political office.

In contrast, some state campaign finance statutes allow corporations and labor organizations to make contributions to state and local candidates, and also allow individuals to make contributions to state and local candidates in amounts that would exceed the dollar limits in 2 U.S.C. § 441a. In addition, the Act's prohibition on contributions by federal contractors does not apply to contributions made in connection with state or local elections. 11 CFR 115.2(a).

Today, most party committees receive some contributions that are permissible under the FECA and also receive other contributions that are not permissible under the Act if they are to be used in connection with federal elections. Contributions that are permissible under the FECA are often referred to as "hard money" contributions. Contributions that are not permissible, i.e., individual contributions in excess of the section 441a dollar limits, all corporate and labor organization general treasury contributions, and contributions from federal contractors, are often referred to as "soft money," and are to be used exclusively for state and local campaign activity or other party committee activities that do not influence federal elections.

Typically, party committees set up separate bank accounts into which they deposit the hard and soft money contributions they receive. Hard money contributions are to be deposited into a federal account, and soft money contributions are to be deposited into a non-federal account. Some party committees have a federal account and multiple non-federal accounts. However, since 2 U.S.C. §§ 441b and 441e prohibit national banks, Congressionally-chartered corporations, and foreign nationals from making contributions in connection with any election to any political office, contributions from these entities to a party committee's non-federal accounts are also prohibited.

It is usually a relatively simple matter for the party committee to distinguish between hard and soft money contributions and segregate them in separate bank accounts. However, it can be more difficult to distinguish between a party committee's federal and non-federal expenses, because many party committee activities benefit both federal and non-federal candidates. For example, when a party committee conducts a get-out-the-vote drive urging people to support the party's candidates, it presumably increases the turnout of voters who favor that party's candidates. If there are both federal and non-federal candidates on the ballot, the drive benefits both the federal and the non-federal candidates. Consequently, if the party committee pays the costs of such a drive entirely with soft dollars, the committee is using prohibited contributions to benefit federal candidates. This would violate the contribution prohibitions and limitations in the FECA.

Since early in its history, the Commission has struggled with the fact that many party functions have an impact on both federal and non-federal elections, and has sought to give force and effect to the FECA's prohibitions and limitations by requiring party committees to pay at least a portion of the cost of these "mixed" activities with hard dollars. For example,

in Advisory Opinion 1975-21, the Commission required a local party committee to use hard dollars to pay for a portion of its administrative expenses and voter registration costs. The Commission said that even though some party functions do not relate to any particular candidate or election, "these functions have an indirect effect on particular elections, and since monies contributed to fulfill these functions free other money to be used for contributions and expenditures in connection with Federal elections, it is appropriate to ascribe a certain portion of the administrative functions of a party organization to Federal elections during time periods in which Federal elections are held." Id.

The Commission incorporated part of Advisory Opinion 1975-21 into regulations promulgated in 1977. The regulations required political committees active in both federal and non-federal elections to allocate their administrative expenses between separate federal and non-federal accounts "in proportion to the amount of funds expended on federal and non-federal elections, or on another reasonable basis." 11 CFR 106.1(e) (1978). Sections 106.1 and 106.5 of the current rules contain updated versions of these regulations.

In two opinions issued after AO 1975-21, the Commission took an even more restrictive view of the use of soft money for registration and get-out-the-vote drive activity. In its response to Advisory Opinion Request 1976-72, the Commission said that "even though the Illinois law apparently permits corporate contributions for State elections, corporate/union treasury funds may not be used to defray any portion of a registration or get-out-the-vote drive conducted by a political party." Thus, the Commission concluded that this type of activity would have to be paid for with hard dollars. In its response to Advisory Opinion Request 1976-83, the Commission reached a similar conclusion.

However, in Advisory Opinion 1978-10, the Commission modified its position. In that opinion, the Commission concluded that the costs of voter registration and GOTV drives should be allocated in the same manner as party administrative expenditures. In reaching this conclusion, the Commission superseded Re: AOR 1976-72 and 1976-83 and said that corporate and union treasury funds could be used for the portion of the costs allocated to the party committee's non-federal account.

In Advisory Opinion 1979-17, the Commission recognized the ability of a national party committee to establish a separate account to be used "for the deposit and disbursement of funds designated specifically and exclusively to finance national party activity limited to influencing the nomination or election of candidates for public office other than elective 'federal office.'" Thus, the Commission concluded that a national party committee could accept corporate contributions "for the exclusive and limited purpose of influencing the nomination or election of candidates for nonfederal office."

The 1979 amendments to the Federal Election Campaign Act sought to encourage the participation of state and local party committees in federal elections by carving out exceptions to the definitions of contribution and expenditure for certain volunteer, voter registration and get-out-the-vote activity conducted by these committees. Under sections 431(8)(B)(x) and 431(9)(B)(viii), payments for the costs of campaign materials used in

connection with volunteer activities on behalf of the party's nominee are not contributions or expenditures so long as the payments do not finance any general public political advertising, and are made from contributions that are permissible under the Act but were not designated for a particular candidate. Sections 431(8)(B)(xii) and 431(9)(B)(ix) contain the same rule for voter registration and get-out-the-vote drive costs conducted by the committee on behalf of its presidential and vice-presidential nominees. These provisions supplement a similar provision for slate cards and sample ballots that existed in the Act prior to the 1979 amendments. 2 U.S.C. §§ 431(8)(B)(v) and 431(9)(B)(iv). Since then, these activities have collectively been referred to as "exempt activities." The House Report accompanying the 1979 amendments recognizes the ability of state and local party committees to allocate the costs of slate card and volunteer activities in certain circumstances. H.R. Rep. No. 96-422 at 8, 9 (1979).

In 1984, the Commission received a petition for rulemaking from Common Cause seeking new rules relating to the use of soft money. The petition requested that the Commission take action to address what the petitioner alleged was the use of soft money by national party committees to influence federal elections. The Commission published a Notice of Availability on January 4, 1985, and subsequently published a Notice of Inquiry on December 18, 1985. See 50 FR 477 (Jan. 4, 1985), 50 FR 51535 (Dec. 18, 1985). These two notices sought comments from the public on the issues raised in the petition. The Commission also held a public hearing on January 29, 1986, at which several witnesses testified.

After reviewing the petition, the comments and the witness' testimony, the Commission denied the Common Cause petition, concluding that neither the petition nor the comments "constitute concrete evidence demonstrating that the Commission's regulations have been abused so that funds purportedly raised for use in nonfederal elections have in fact been transferred to the state and local level with the intent that they be used to influence federal elections." Notice of Disposition, 51 FR 15915 (Apr. 29, 1986).

Common Cause challenged the Commission's denial of the petition in U.S. District Court. In court, Common Cause asserted that no allocation method is permissible under the FECA. Consequently, Common Cause argued, the Commission's denial of the petition was arbitrary and capricious under the Administrative Procedure Act, 5 U.S.C. § 706. Common Cause also argued that allowing committees to allocate on a reasonable basis was contrary to law because it failed to ensure proper allocation between federal and non-federal accounts.

The court rejected Common Cause's first argument, saying that the Act cannot be read to prohibit allocation. Common Cause v. FEC, 692 F. Supp. 1391, 1395 (D.D.C. 1987). However, the court then agreed that the Commission's policy of allowing state party committees to allocate slate card expenses on any reasonable basis was contrary to law, "since Congress stated clearly in the FECA that all monies spent by state committees on these activities vis-à-vis federal elections must be paid for 'from contributions subject to the

limitations and prohibitions of this Act.'" Id. (quoting 2 U.S.C. §§ 431(8)(B)(x)(2) and (xii)(2), 431(9)(B)(viii)(2) and (ix)(2)). The court said that

> [t]he plain meaning of the FECA is that any improper allocation of nonfederal funds by a state committee would be a violation of the FECA. Yet, the Commission provides no guidance whatsoever on what allocation methods a state or local committee may use; . . . Thus, a revision of the Commission's regulations to ensure that any method of allocation used by state or local party committees is in compliance with the FECA is warranted.

Id. at 1396.

The court directed the Commission to replace the "any reasonable basis" allocation method with more specific allocation formulas that would ensure that only contributions subject to the limitations and prohibitions of the Act are used to influence federal elections. However, the court also acknowledged that the Commission could "conclude that no method of allocation will effectuate the Congressional goal that all moneys spent by state political committees on those activities permitted in the 1979 amendments be 'hard money' under the FECA. That is an issue for the Commission to resolve on remand." Id. (emphasis in original).

In a subsequent order, the same court stated that "'[s]oft money' denotes contributions to federally regulated campaign committees in excess of the aggregate amounts permitted for federal elections by the FECA; these contributions, even if directed to national campaign entities, are permissible if the money is not to be used in connection with federal elections." Common Cause v. FEC, 692 F.Supp. 1397, 1398 (D.D.C. 1988).

The Commission initiated a rulemaking in response to the court's decision in which it made several efforts to obtain input from the regulated community. In addition to the two comment periods and public hearing held before the court's decision, the Commission sought comments on proposed rules through a new Notice of Proposed Rulemaking published on September 29, 1988. 53 FR 38012. The Commission also held another public hearing on the proposed rules on December 15, 1988, at which a cross section of the regulated community had an opportunity to testify. The Commission took the additional step of sending questionnaires to the chairs of all the Democratic and Republican state party committees, and also sought input from the chief fundraisers for each of the major political parties during the 1988 election year.

The Commission issued final rules in 1990 and put them into effect on January 1, 1991. Methods of Allocation Between Federal and Non-Federal Accounts; Payments; Reporting, 55 FR 26058 (June 26, 1990). These rules currently govern the allocation of expenses between federal and non-federal accounts. They seek to address the issue of soft money in two ways.

First, the current rules replace the "any reasonable basis" allocation method with specific allocation methods to be used to pay the costs of activities that impact both federal and nonfederal elections. The method to be used depends on the type of committee incurring the expense and the type of activity for which expenses are to be allocated.

National party committees, other than the Senate and House campaign committees, are required to allocate a minimum of 60% of their administrative expenses and costs of generic voter drives to their federal accounts each year (65% in presidential election years). 11 CFR 106.5(b). In addition, national party committees must allocate the costs of each combined federal and non-federal fundraising program or event using the funds received method described in 11 CFR 106.5(f).

Senate and House campaign committees are required to allocate their administrative and generic voter drive expenses using a funds expended formula, subject to a 65% minimum federal percentage, 11 CFR 106.5(c), and, like the national party committees, they must allocate the costs of each combined federal and non-federal fundraising program or event using the funds received method described in 11 CFR 106.5(f), with no minimum federal percentage required.

State and local party committees must allocate (1) their administrative expenses and generic voter drive costs using the ballot composition method, described in 11 CFR 106.5(d); (2) the costs of communications exempt from the contribution and expenditure definitions under 11 CFR 100.7(b) (9), (15) or (17), and 100.8(b) (10), (16) or (18), according to the proportion of time or space devoted to federal and nonfederal candidates in the communication, 11 CFR 106.5(e); (3) expenses incurred in joint fundraising activities using the funds received method, 11 CFR 106.5(f); and (4) direct candidate support activity according to the time or space devoted to each candidate in the communication. 11 CFR 106.1. The new rules also set up procedures to be used by all three types of committees to pay for their mixed activities.

Second, the rules impose additional reporting requirements in order to enhance the Commission's ability to monitor the allocation process. All three types of party committees are required to report their allocations of administrative expenses, voter drive costs, fundraising costs and costs of exempt activities, and also to itemize any transfer of funds from their non-federal to their federal or allocation accounts. In addition, all six national party committees are now required to disclose the financial activities of their nonfederal accounts. Specifically, the committees are required to report all nonfederal receipts and disbursements. The Commission believed this additional reporting would help to ensure that impermissible funds were not used for federal election activities.

On May 20, 1997, the Commission received a petition for rulemaking from five Members of the United States House of Representatives urging the Commission "to modify its rules to help end or at least significantly lessen the influence of soft money." On June 5, 1997, the Commission received a second petition for rulemaking relating to soft money, this one submitted by President Clinton. President Clinton's petition asks the Commission to

"ban soft money" and "adopt new rules requiring that candidates for federal office and national parties be permitted to raise and spend only 'hard dollars.'" The Commission published a Notice of Availability in the Federal Register announcing that it had received the petitions and inviting the public to submit comments on them. 62 FR 33040 (June 18, 1997). The comment period closed on July 18, 1997. The Commission received 188 comments in response to the Notice of Availability.

On July 13, 1998, the Commission published a Notice of Proposed Rulemaking ("NPRM") seeking comment on proposed rules relating to soft money. In an effort to generate a full range of views, the NPRM sought comment on two options for addressing issues relating to soft money, and also sought comments on three variations on the second of these two options.

The first option set out in the NPRM was to make no changes to the current rules. Under the first option, the national parties would continue to be prohibited from receiving and using soft money in connection with federal elections. However, they could continue to raise soft money for a variety of purposes related to nonfederal elections. The national party committees could continue operating nonfederal accounts.

The second option set out in the NPRM was to revise the current rules. The NPRM proposed revisions to sections 102.5, 106.1 and 106.5 that would address the issues raised in the petitions and in the comments received in response to the Notice of Availability. The proposed revisions consisted of a core proposal, and three variations on the core proposal.

The core proposal was directed primarily at soft money donations to national party committees. It would prohibit the receipt and use of soft money by the national party committees by revising section 102.5 to eliminate all national party committee nonfederal accounts other than the building fund accounts specifically authorized in the FECA. Under this approach, the national party committees would be required to defray all of their expenses, other than building fund expenses, entirely with hard dollars. However, the core proposal would not change the allocation rules for state and local party committees.

The core proposal would also clarify section 102.5(a)(3) relating to solicitations by federal candidates and officeholders. The proposed clarification would emphasize that funds donated to party committees in response to a solicitation by a federal candidate or officeholder would be subject to the prohibitions and limitations of the Act, unless the donor specifically designates the donation for a nonfederal account.

The first variation on the core proposal was also directed at soft money donations to the national committees. This variation would create an exception to the prohibition on national party committee nonfederal accounts in section 102.5 of the core proposal. This exception would allow national party committees to raise soft money for the limited purpose of making direct or earmarked contributions to state and local candidates. If incorporated into the core proposal, variation one would modify proposed section 102.5(c). Otherwise, the core proposal would remain intact.

The second and third variations on the core proposal were directed at the use of transferred funds by state and local party committees. Variation two would supplement the prohibition on national party committee nonfederal accounts set out in the core proposal by seeking to ensure that hard money transferred from a national to a state or local party committee is spent by the recipient committee using the rules applicable to the national committee, rather than the state or local committee's more favorable allocation ratios. Specifically, variation two would revise section 106.5 to require the national committee to earmark transferred funds for a particular activity, and would require the recipient committee to finance the identified activity entirely with hard dollars.

Variation three of the core proposal was also directed at the use of transferred funds by state and local party committees, and served similar purposes. This variation would supplement the prohibition on national party committee nonfederal accounts set out in the core proposal by requiring state and local party committees to finance their mixed activities entirely with hard dollars.

The Commission received 73 comments in response to the NPRM. Of the 73 comments received, 42 comments expressed either general support for limits on soft money or specific support for the proposed limits set out in the NPRM. The commenters supporting the proposed rules were the American Bar Association House of Delegates, the Brennan Center for Justice, Common Cause, Congressman Martin Meehan, Democracy South, the Democratic National Committee, the Opticians Association of America, Public Campaign, the District of Columbia Bar Association Section on Administrative Law, and 31 other individual commenters.

In contrast, 29 comments expressed either general opposition to limits on soft money or specific opposition to the proposed rules set out in the NPRM. The commenters opposing the proposed rules were the Americans Back In Charge Foundation, the Claremont Institute, the Fair Government Foundation, the James Madison Center for Free Speech, the National Republican Senatorial Committee, Professor Bradley Smith, the Republican National Committee, Senator Mitch McConnell, the Thomas County Republican Party, the state Republican Party organizations of Georgia, Iowa, Missouri, Montana, Nebraska, New Hampshire, New Mexico, Ohio, Tennessee, Texas and Virginia, and nine other individual commenters.

On November 18, 1998, the Commission held a public hearing on the proposed soft money rules. Representatives of the American Bar Association House of Delegates, the Americans Back In Charge Foundation, the Brennan Center for Justice, Common Cause, the James Madison Center for Free Speech and the National Republican Senatorial Committee testified at the hearing. Congressman Martin Meehan also testified on his own behalf. The comments submitted and the testimony received will be summarized below.

The Office of General Counsel reviewed the results of several research studies conducted by outside entities in analyzing the comments and the issues raised in the NPRM.

These materials were selected for their relevance to the issues raised in the NPRM, and in one instance, because the study was submitted by a commenter. The following reports were used in our analysis:

- Investing in the People's Business: A Business Proposal for Campaign Finance Reform, Committee for Economic Development (1999) ("CED Report")

- Issue Advocacy Advertising During the 1997-1998 Election Cycle, Jeffrey D. Stranger & Douglas G. Rivlin, Annenberg Public Policy Center (1999) ("Annenberg Study")

- Money and Politics Survey, Princeton Survey Research Associates for the Center for Responsive Politics, <http://www.opensecrets.org/pubs/survey/s2.htm>[2] ("Princeton Survey")

- Outside Money: Soft Money & Issue Ads in Competitive 1998 Congressional Elections, David Magleby & Marianne Holt (1999) ("Outside Money")

- Memorandum of the Tarrance Group to the National Association of Business PACs, submitted in Comments of the National Republican Senatorial Committee, Appendix of Exhibits, Vol. I ("Tarrance Group Memorandum"). This Memorandum regarding public attitudes on the issue of campaign finance reform was submitted in support of the commenter's position that the proposed rules set out in the NPRM were unconstitutional.

Copies of these materials are available upon request. We have included Internet citations where available. The results of our analysis are set out below.

Finally, we note that we have made use of the Final Report of the Committee on Governmental Affairs: Investigation of Illegal or Improper Activities in Connection with 1996 Federal Election Campaigns, S. Rep. No. 105-167, 105th Cong., 2d Sess. (March 10, 1998). This Report was generated by the Committee on Governmental Affairs of the United States Senate, Chaired by Senator Fred Thompson of Tennessee, following an investigation of campaign financing practices in the 1995-96 election. The Report contains an extensive discussion of the findings of both the majority and minority Members of the Committee. The findings contained in the Report will be discussed more fully below. Citations will be to portions of the "Thompson Committee Majority Report" or "Thompson Committee Minority Report," as appropriate.

IV. ANALYSIS

A. The Commission's Statutory Authority to Limit Soft Money

The NPRM raised the threshold issue of whether the Commission has the statutory authority to regulate soft money. At the time, the Commission "reached the preliminary

[2] All "URL" citations were current as of February 1, 2000.

conclusion that it has the authority to issue new rules relating to soft money, at least insofar as it is used in connection with Federal elections." 63 FR at 37725 (July 13, 1998). However, the Commission also said that it did not regard this as a closed issue, and invited commenters to address the issue of whether the Commission has the authority to regulate soft money, and whether the proposed rules set out in the notice were within the scope of the Commission's authority.

1. Summary of Comments

a. Soft money limits exceed the Commission's statutory authority

Many of the commenters opposing soft money limits argued that the Commission lacks the statutory authority to limit soft money. In general, these commenters assert that the statute only limits federal election activity. It does not limit amounts spent to support state or local candidates, nor does it limit issue advocacy.

Two commenters discussed the Commission's authority in detail. One commenter said the Commission does not have general rulemaking authority, and may only fill gaps in the statute when it is vague or open-ended. This commenter said the proposed rules would effectively amend the FECA based on the quasi-legislative role of an independent agency.

The other commenter said the proposed rules would be invalid under the two-step analysis in Chevron v. Natural Resources Defense Council, 467 U.S. 837 (1984). In Chevron, the Supreme Court set out a two-step process for determining whether an agency rule is within its statutory authority. The Court said the first question is "whether Congress has directly spoken to the precise question at issue. If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress." Id. at 842-43. However, if Congress has not directly addressed the precise question at issue, the court "does not simply impose its own construction on the statute . . . . [T]he question is whether the agency's answer is based on a permissible construction of the statute." Id. at 843. "Such legislative regulations are given controlling weight unless they are arbitrary, capricious or manifestly contrary to the statute." Id. at 844. The commenter argued that the proposed rules would fail step one of the Chevron analysis because they do not fill a gap in the statute, and would fail step two because they burden First Amendment rights. Consequently, the commenter argued, the rules would not be entitled to deference from a reviewing court.

A number of commenters said the proposed rules are an attempt to limit issue advocacy by party committees, and therefore are beyond the Commission's statutory authority.[3] One commenter said that the definitions of "contribution" and "expenditure" are limited to funds given or spent to influence a federal election, which the Supreme Court has interpreted to mean "express advocacy." In this commenter's view, when this phrase is applied to funds spent for communications, it means that the communication must expressly

[3] These commenters also argued that the rules are unconstitutional for the same reason. The constitutional issues will be discussed in detail below.

advocate the election or defeat of a clearly identified federal candidate in order to be subject to the FECA. Thus, the FECA does not encompass soft money donations.

A few commenters cited language in the Supreme Court's opinion in Colorado Republican Federal Campaign Committee v. FEC, 518 U.S. 604 (1996) ("Colorado Republican"), as evidence that the Commission lacks the authority to limit soft money. In its opinion, the Supreme Court said "[w]e also recognize that FECA permits unregulated 'soft money' contributions to a party for certain activities, such as electing candidates for state office, see § 431(8)(A)(i), or for voter registration and 'get out the vote' drives, see § 431(8)(B)(xii)." 518 U.S. at 616. These commenters read this language as a limit on the Commission's authority to regulate soft money.

Several state party committees said the proposed rules would burden state and local committees. Furthermore, nonfederal donations are regulated by state law and are outside the Commission's statutory authority. These commenters also questioned the Commission's ability to regulate transfers of funds to be used for legitimate nonfederal purposes.

b. The Commission has the authority to limit soft money

Most the commenters that were in favor of soft money limits said that the rules are within the Commission's authority, since they merely build on the Commission's existing authority over party committees. One national party committee noted that in Common Cause v. FEC, 692 F. Supp. 1391 (D.D.C. 1987), the court said that the Commission could conclude that no allocation method would be adequate to ensure that soft money is not used to influence federal elections. Id. at 1396. Along those lines, the other commenters also argued that there is no legal basis for concluding that the a 65% federal allocation percentage is acceptable, but that a 100% federal allocation percentage is not. Several commenters also expressed the view that the Commission's authority extends equally to state party committees when they engage in activity that influences federal elections.

Several commenters included detailed legal arguments regarding the Commission's authority. One commenter said that the Commission's broad rulemaking authority under 2 U.S.C. § 438(a)(8), when combined with the substantive prohibitions and limitations in the Act, provides ample authority to limit soft money. The commenter went a step further, asserting that if the Commission did not limit soft money, this would be a failure to "administer, seek to obtain compliance with, and formulate policy with respect to" the FECA and the public financing statutes. 2 U.S.C. § 437c(b). Another commenter said that the Commission has the authority to regulate soft money in order to protect against evasion of the hard money limits, and can enact rules to prevent evasion even if those rules incidentally affect parties' nonfederal activities, since agencies have a "reasonable margin to insure effective enforcement," citing Mourning v. Family Publications Service, Inc., 411 U.S. 356, 374 (1973).

Several commenters said the Chevron decision would not limit the Commission's ability to regulate soft money. One commenter said that since the FECA does not require the

Commission to allow party committees to allocate, Chevron places limits on soft money squarely within the agency's discretion. Therefore, the question for a reviewing court would be whether limits on soft money are a permissible construction of statute. In this situation, the commenter asserts, the Commission's construction of the Act would be entitled to considerable deference.

Other commenters said that the Commission has an affirmative legal duty to limit soft money. One organization said current soft money practices are contrary to Congress' clear legislative intent to prevent corruption and the appearance of corruption and ensure that all contributions and expenditures that influence a federal election are subject to the FECA. This commenter argued that failure to limit soft money would be contrary to law under Chevron, since agencies have an obligation to adjust rules when they are inconsistent with legislative intent. Another commenter said it would be arbitrary and capricious for the FEC to not conclude that soft money is raised and spent for the purpose of influencing federal elections, that it facilitates massive evasions of the prohibitions and limitations, and that national party committee fundraising and state party committee mixed activities are central features of this system. Given this conclusion, the commenter believes that nothing less than a complete ban will keep soft money out of federal campaigns and meet the anti-corruption goals of the FECA. Adjusting the allocation ratios would be inadequate, because adjustments would not eliminate the use of soft money, and would do nothing to limit transfers of soft money.

2. Analysis

a. National party committees

The Office of General Counsel has analyzed the comments and the applicable law, and concluded that the Commission has the statutory authority to significantly limit the receipt and use of soft money by national party committees. The Act limits the amounts that individuals and political committees can contribute for the purpose of influencing federal elections, and also prohibits corporations, labor organizations and federal contractors from using their general treasury funds to make contributions in connection with federal elections. 2 U.S.C. §§ 441a, 441b, 441c. Section 438(a)(8) of the Act states that "[t]he Commission shall prescribe rules, regulations and forms to carry out the provisions of this Act. . . ." 2 U.S.C. § 438(a)(8).

As will be explained in detail below, the current allocation rules allow national party committees to raise significant amounts of money from prohibited sources and in excess of the contribution limits and to use those funds to finance activity that influences federal elections. The rules may also allow national party committees to transfer funds to state party committees with instructions to use those funds for a particular activity and pay the costs of that activity using the state party committee's more favorable allocation ratios. In our view, this system undermines the prohibitions and limitations in the FECA. The Commission has been assigned the task of "administer[ing], seek[ing] to obtain compliance with, and formulat[ing] policy with respect to" the FECA, 2 U.S.C. § 437c(b)(1). We believe that

promulgating rules designed to prohibit the national party committees from using soft money to influence federal elections is an appropriate exercise of that authority, and is also necessary to ensure fulfillment of the Commission's responsibilities.

The decision in Common Cause, discussed above, supports this conclusion. In Common Cause, the district court rejected the Commission's previous rules allowing party committees to allocate their expenses "on a reasonable basis," saying that the FECA required the Commission to promulgate more specific rules limiting the use of soft money for mixed activities. 692 F. Supp. at 1395. The court went on to say that, although not required to do so, the Commission could "conclude that no method of allocation will effectuate the Congressional goal that all monies spent by state political committees on those activities permitted in the 1979 amendments be 'hard money' under the FECA." Id. at 1396 (emphasis in original). Thus, the court concluded that, rather than limiting the Commission's authority to limit the use of soft money, the Act requires the Commission to promulgate rules that ensure that soft money is not used to finance activity that influences federal elections. It is worth noting that the Common Cause court reached this conclusion with regard to allocation by state party committees. Presumably, the Commission's authority to regulate allocation by national party committees, whose interests in federal elections are even greater, is at least as extensive.

Moreover, we agree with the Thompson Committee Report that the roots of the current soft money system lie in Commission advisory opinions, rather than in the FECA.

> Although the[] 1979 Amendments authorized a circumscribed realm of unlimited party expenditures, they did not sanction unlimited spending by party committees of unregulated (soft money) on activities designed to assist a particular candidate for federal office. The latter activity came into vogue as a result of FEC interpretations of the FECA. In Advisory Opinion 1978-10 the FEC declared that the Kansas Republican State Committee could use corporate and union money to finance a share of their voter drives, so long as it allocated its costs to reflect the federal and nonfederal shares of any costs incurred.

Thompson Committee Majority Report, Ch. 32 at 9. The Commission has the authority to revise or supersede policies articulated in past advisory opinions, if it determines that those policies no longer adequately ensure that soft money is not used to influence federal elections.

Other courts have also recognized that section 438(a)(8) of the Act gives the Commission broad rulemaking authority. "Congress provided the FEC with extensive rulemaking and enforcement powers and the FEC's interpretation of the statute it administers and its own regulations is entitled to substantial deference." Republican National Committee, et al v. Federal Election Commission, No. 98-1207 slip op. at 5 (D.D.C. June 25, 1998) (order denying preliminary injunction) (citing FEC v. Democratic Senatorial Campaign Committee, 454 U.S. 27 (1982) ("DSCC")).

> Normally an agency with rulemaking power has a measure of latitude where it is dealing with the regulated entity (here, corporations and unions) and where the rule is reasonably designed to achieve the statute's goal (here, to prohibit certain types of contributions). The FEC has such rulemaking power. 2 U.S.C. § 437d(a)(8). . . . Agencies often are allowed through rulemaking to regulate beyond the express substantive directives of the statute, so long as the statute is not contradicted.

Clifton v. Federal Election Commission, 114 F.3d 1309, 1312 (1st Cir. 1996) (citing Buckley v. Valeo, 424 U.S. 1, 110 (1976), Mourning v. Family Publications Service, Inc., 411 U.S. 356 (1973)). "The Supreme Court has held that the FEC is vested by Congress with primary and substantial responsibility for administering and enforcing FECA and that the Commission is provided with extensive rule making and adjudicative powers." FEC v. Ted Haley Congressional Committee, 852 F.2d 1111, 1114 (9th Cir. 1988) (citing DSCC).

The Office of General Counsel also believes that rules prohibiting the receipt and use of soft money by national party committees, with limited exceptions, would survive judicial review under Chevron. As discussed above, Chevron describes a two step process for reviewing agency regulations. The first question is "whether Congress has directly spoken to the precise question at issue. If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress." The FECA does not specifically address the allocation of expenses by national party committees. However, the Act clearly states that funds from prohibited sources and in excess of the contribution limits shall not be used to influence federal elections. Rules promulgated by the Commission to enforce these prohibitions and limitations would be consistent with this statutory purpose.

The second step of the Chevron analysis states that if Congress has not "directly addressed the precise question at issue, . . . the question for the court is whether the agency's answer is based on a permissible construction of the statute." The Office of General Counsel believes that it would be permissible for Commission to construe the Act to limit the national party committees' ability raise soft money and require the committees to use hard dollars for virtually all of their activities, including activities that impact both federal and nonfederal elections. The record indicates that allowing national party committees to raise soft money and use it to pay for a portion of the costs of mixed activities results in the use of soft money to influence federal elections, thereby undermining the purposes of the Act. In our view, the Commission could reasonably conclude, as the Common Cause court suggested, 692 F. Supp. at 1396, that limiting the receipt of soft money by national party committees is the only way to ensure that they do not use soft money to influence federal elections. According to Chevron, this conclusion would be entitled to substantial deference, since, in the absence of any specific reference in the statute, "a court may not substitute its own construction of a statutory provision for a reasonable interpretation made by . . . an agency." 467 U.S. at 842-43 (footnotes omitted).

We recognize that two courts have said that the Commission's interpretations of the Act are entitled to less deference when they implicate First Amendment rights. Chamber of Commerce v. FEC, 600, 605 (D.C. Cir. 1995), petition for rehearing denied 76 F.3d 1234 (D.C. Cir. 1996) (concluding that the Commission is not entitled to Chevron deference when its interpretations raise significant constitutional issues); FEC v. Christian Coalition, 52 F. Supp. 2d 45, 82 n.40 (D.D.C. 1999) ("[T]he FEC's interpretation of the FECA is presumptively entitled to Chevron deference so long as its statutory interpretation does not run afoul of the First Amendment, as interpreted by the federal courts.").

However, as will be discussed in detail below, the Office of General Counsel believes that restrictions on the receipt of soft money by national party committees would be constitutionally permissible. Furthermore, in a subsequent case involving judicial review of a Commission interpretation of the Act, the D.C. Circuit cautioned that "our holding declining to apply Chevron in Chamber of Commerce does preclude its application in all First Amendment contexts." Bush-Quayle v. FEC, 104 F.3d. 448, 452 (D.C. Cir. 1997). "[T]he very nature of the FEC dictates that all Commission determinations will touch upon political speech. Courts are not, however, prohibited from applying Chevron to FEC determinations. . . . In fact, the Supreme Court has explicitly noted that the FEC 'is precisely the type of agency to which deference should presumptively be afforded.'" Id. (quoting DSCC, 454 U.S. at 37).[4]

The Office of General Counsel disagrees with those commenters who cited the Supreme Court's decision in Colorado Republican as a limit on the Commission's authority to promulgate rules regarding the use of soft money by national party committees. In its opinion, the Court said "[w]e also recognize that FECA permits unregulated 'soft money' contributions to a party for certain activities, such as electing candidates for state office, see § 431(8)(A)(i), or for voter registration and 'get out the vote' drives, see § 431(8)(B)(xii)." 518 U.S. at 616. Some of the commenters argued that this statement prevents the Commission from limiting the use of soft money by national party committees.

However, contrary to the commenters, we read the Court's statement as confirmation that the Act only allows party committees to receive and use soft money for very limited purposes. The Court emphasized this later in its opinion. "Unregulated 'soft money' contributions may not be used to influence a federal campaign, except when used in the limited, party-building activities specifically designated in the statute." See § 431(8)(B) Id. The exceptions for party-building activities listed in section 431(8)(B) only apply to state and

[4] The facts of Chamber of Commerce also suggest that it would not control the level of deference that would be afforded the draft final rules set out below. The statutory interpretation of the term "member" that was at issue in Chamber of Commerce "would have prevented the organization from communicating on political subjects with thousands of persons and would have burdened the organizations' First Amendment rights." Bush-Quayle v. FEC, 104 F.3d. 448, 452 (D.C. Cir. 1997) (citing Chamber of Commerce, 69 F.3d at 605). In contrast, limiting the receipt of soft money by national party committees would not limit a national party committee's ability to engage in any type of communication, nor would such a rule place a ceiling on how much the committee could spend on that communication. Thus, although such a rule, like other Commission rules, may "touch upon political speech," it may not raise the type of constitutional issues that were at issue in Chamber of Commerce. Consequently, such a rule would be entitled to Chevron deference. Bush-Quayle, 104 F.3d at 452.

local party committees. See section 431(8)(B)(v), (x) and (xii). Thus, we believe that Colorado Republican confirms the Commission's authority to promulgate rules directed at national party committees.

Moreover, we note that even if the Court's statement is read as interpreting FECA to allow soft money donations to national party committees for the purpose of electing candidates to state or local office, the draft final rules follow that interpretation by allowing donations to national party committees for this purpose. Section 102.5(c)(2)(ii) of the draft final rules would allow national party committees to receive soft money for the purpose of making direct donations to candidates for nonfederal office or direct disbursements on behalf of candidates for nonfederal office. Thus, we do not believe Colorado Republican limits the Commission's authority to promulgate the draft final rules set out below.

We disagree with those commenters who argued that the Commission can only regulate funds donated to party committees for use in express advocacy, and thus, limits on the receipt of soft money by the national party committees are beyond the Commission's statutory authority. As will be discussed further below, the court decisions applying the "express advocacy" standard involved direct restrictions on independent expenditures. The draft final rules would not limit party committee independent expenditures. Thus, these cases are inapplicable. See Orloski v. FEC, 795 F.2d 156 (D.C. Cir. 1986), discussed below.

Based on the foregoing, we believe the Commission has the statutory authority to promulgate new regulations limiting the receipt and use of soft money by the national party committees.

b. State and local party committees

As discussed above, the second and third variations on the core proposal in the proposed rules were directed at the use of soft money by state and local party committees. Variation two would require the national committee to earmark transferred funds for a particular activity, and would require the recipient committee to finance the identified activity entirely with hard dollars. Variation three would require state and local party committees to finance their mixed activities entirely with hard dollars.

Two commenters objected to these proposals, saying that national party committees should be able to freely transfer hard dollars to state party committees, and questioning whether these limits would be lawful. In contrast, three commenters urged the Commission to adopt variation three, implicitly arguing that the Commission has the statutory authority to promulgate these rules. A national party committee largely agreed, saying that the Commission should adopt variation three, but with a modification that would allow state party committees to continue allocating their administrative expenses. This commenter said that the Commission could conclude that all other state party committee mixed activities have an impact on federal elections.

The Office of General Counsel has examined the Commission's statutory authority to limit the receipt and use of soft money by state and local party committees. We conclude that, in general, the Commission has the authority to limit the receipt and use of soft money by state and local party committees when that money is used to influence a federal election. We also believe that the Commission's broad rulemaking authority includes the authority to promulgate new rules to prevent evasion of the existing rules. Thus, in our view, the Commission has the authority to promulgate variation two of the core proposal, since this variation seeks to limit the national party committees' practice of transferring soft money to state and local party committees in order to take advantage of the recipient committee's more favorable allocation ratio.

However, the Commission's authority to implement variation three, which would require state and local party committees to finance their mixed activities entirely with hard dollars, is a closer question. The House Report accompanying the 1979 amendments contains language suggesting that Congress intended to allow state and local party committees to allocate the costs of two types of expenses: (1) slate cards; and (2) campaign materials produced in connection with volunteer activities.[5] H.R. Rep. No. 96-422 (1979). With regard to slate cards, the House Report says that

> [i]f a state or local party organization prepares a slate card which includes both Federal and State candidates, the party organization may allocate or apportion the costs attributable to all the Federal candidates and the costs attributable to all the State candidates. The portion of the costs attributable to Federal candidates must be paid with funds subject to the prohibitions and limitations of the Act.

Id. at 8. With regard to campaign materials produced in connection with volunteer activities, the House Report says that "if the campaign materials contain reference to both State and Federal candidates, the party organization may allocate the costs between the State and Federal candidates. The money used to pay the cost attributable to State candidates would be subject to State, not Federal law." Id. at 9.

Thus, the scope of the Commission's authority to limit allocation by state and local party committees is not as clear as it is for national party committees. For this reason, and for other reasons that will be discussed in detail below, we recommend that the Commission make no substantive changes to the current allocation rules for state and local party committees.

B. Constitutionality

[5] Costs incurred in producing slate cards are exempt from the definition of "contribution" under section 431(8)(B)(v) of the FECA. See also 11 CFR 100.7(b)(9). Similarly, the costs of campaign materials used by a state or local party committee in connection with volunteer activities are exempt from the definition of contribution under section 431(8)(B)(x). See also 11 CFR 100.7(b)(15). The current rules require state and local party committees to allocate these costs when they involve both federal and nonfederal candidates. 11 CFR 106.5(a)(2)(iii), 106.5(e).

1. Comments

a. Soft money limits are unconstitutional

Some commenters based their opposition to the proposed rules on constitutional grounds. Some said that any Commission regulation of soft money would be unconstitutional. Others said the proposed limits on the receipt and use of soft money would be unconstitutional. These commenters said that limits on soft money must be narrowly tailored to serve the compelling government interest in preventing corruption or the appearance of corruption, and said that the Commission must present evidence that limitations actually prevent corruption or the appearance of corruption in order for the limits to be constitutional. Most of these commenters believe that no such evidence exists.

One national party committee said that increases in the receipt and use of nonfederal funds for legitimate nonfederal activities are not proof of abuse. Other commenters argued that there is no evidence of actual, quid pro quo corruption, nor is there evidence of an appearance of corruption. These commenters said it is unclear whether the level of corruption perceived by the public has increased. Furthermore, they say that voter cynicism cannot be treated as an indicator of the appearance of corruption, and that even if it were, there is no way to attribute this appearance of corruption to soft money.

A national party committee argued that the proposed rules eliminate nonfederal accounts in order to prohibit disbursements of nonfederal funds, and therefore, the rules act as an expenditure limit. This commenter argued that Buckley held that expenditure limits are unconstitutional because they do not directly prevent corruption or the appearance of corruption. If limits on federal expenditures are unconstitutional, this commenter claimed, then limits on nonfederal disbursements are also unconstitutional.

Some of these commenters also argued that the rules are an unconstitutional attempt to limit issue advocacy by party committees. A national party committee argued that Buckley requires express advocacy to avoid vagueness concerns, and also said that Citizens Against Rent Control v. Berkeley, 454 U.S. 290 (1981) ("Berkeley"), struck down limits on contributions and expenditures for issue advocacy by political associations. Other commenters said that under Colorado Republican, party committees have the same rights as individuals to engage in issue advocacy. Therefore, the Commission cannot regulate party committee issue advocacy simply because the speaker is a party committee. An individual commenter argued that under First National Bank of Boston v. Bellotti, 435 U.S. 765 (1978) ("Bellotti") and Berkeley, the Commission cannot limit the size or source of contributions to be used for issue advocacy.

Some commenters also stated other constitutional objections to limits on soft money. One national party committee argued that the proposed rules violate its First Amendment associational rights by effectively prohibiting it from associating with its state and local candidates. Two commenters argued that the proposed rules would violate the Tenth

Amendment, which reserves powers not delegated to the United States by the Constitution for the states, because they would interfere with states' rights to regulate their own elections, and would also limit party committees' ability to participant in state and local elections. An individual commenter said that the rules would regulate state party committee spending on state races and ballot initiative drives, which is not within Congress' authority under the Commerce clause. A national party committee said that the Commission cannot preempt state laws allowing the use of soft money in public debates without a clear statement from Congress.

b. Limits on soft money are not unconstitutional

Several commenters analyzed the constitutionality of limits on soft money, and concluded that limits, and the proposed rules, would be constitutionally permissible. Most of these commenters argued that the government has a compelling interest in preventing both actual corruption, where large donations are given to secure a quid pro quo from current or potential officeholders, and also the appearance of corruption, which results from public awareness of the opportunities for abuse inherent in large financial donations. Citing the Buckley decision, these commenters argued that this compelling interest justifies limiting the source and amounts of contributions made to federal candidates. The commenters also pointed out that Buckley concluded that party committees are political committees whose activities and expenditures are, by definition, campaign related. Consequently, the commenters said, Congress and the Commission can constitutionally regulate the means by which party committees raise funds to pay for those activities.

Many commenters said that the record shows that soft money creates both actual corruption and the appearance of corruption in the political process. Soft money creates actual corruption, because soft money donors receive preferred access to and special influence with candidates and elected officials. A Congressman said that Members of Congress look for new ways to provide access to big money donors in order to increase fundraising receipts. Some commenters alleged that soft money leads to legislative concessions. Others said that merely providing preferred access is a significant quid pro quo, because it provides large donors with an greater opportunity to influence candidates and elected officials. The Congressman also said that soft money influences the legislative process by limiting Congress' ability to address significant issues. Another commenter said that there is proof of actual corruption in the Thompson Committee Reports, which, the commenter argued, show that soft money was at the root of virtually all of the 1996 campaign controversies.

The comments also said that soft money creates the appearance of corruption by creating the perception that the political system is dominated by the wealthiest and most powerful, rather than the American people. One national party committee specifically endorsed this view. Several individual commenters stated their belief that soft money gives donors undue influence that drowns out ordinary people, causing voter apathy and cynicism.

Some commenters specifically rejected arguments that limits on soft money act as an expenditure limit or unconstitutionally limit issue advocacy. An organization noted that soft money limits would not regulate either the form or quantity of party committee speech, because they focus on donations of soft money, not on the use to which the money is put. In this commenter's view, having the right to engage in issue advocacy does not mean that party committees have a right to raise soft money to pay for it. This commenter noted that if limits on soft money donations to party committees were an unconstitutional expenditure limit, then the limits on direct contributions to candidates would also be an unconstitutional expenditure limit. This conclusion would allow candidates to raise soft money and engage in issue advocacy, a result that the commenter said would clearly negate the law. Another commenter agreed, saying that under Buckley, the government can regulate party committee activities, even if those activities do not involve express advocacy. This commenter emphasized that no court has ever applied the express advocacy test to activities conducted by political parties.

These commenters said that Colorado Republican is irrelevant, for two reasons. First, several noted that the language quoted from the opinion regarding soft money is dicta, and asserted that the permissive reference was to state party committee use of soft money for state and local election activity. In addition, the commenters said the case is irrelevant because it dealt with expenditures of hard money. Consequently, the Supreme Court presupposed that the money at issue created no risk of corruption. Thus, the case did not address the constitutionality of a soft money ban.

Two commenters responded directly to the assertion that donations to party committees' soft money accounts pose no risk of corruption. A Congressman said that donors expect the same thing no matter whether their donations are considered hard money or soft money, and noted that it is often easier for donors to make soft money donations than it would be to gather hard dollar contributions. The Congressman also rejected the argument that political party committees provide a buffer between donors and candidates or officeholders, saying that candidates and officeholders find out who has donated money to the party and later solicit these donors for direct contributions. An organization agreed, saying that federal candidates find out who has contributed even when they are excluded from the fundraising process. Regarding the impact of inflation on the hard dollar limits, the Congressman noted that even with the outdated hard dollar limits, new hard dollar records are set in every election cycle. Thus, the notion that these limits are unconstitutionally small or that proposed rules would reduce the overall amount of speech are not persuasive.

One commenter noted that several Supreme Court cases have upheld restrictions designed to prevent evasion of the size and source limits in the FECA. Other commenters said that transfers from national party committees to state party committees undermine the FECA by allowing party committees to pay for mixed activities with a larger percentage of soft dollars, and by transforming soft dollars into hard dollars that can be used by the national party committee to influence federal elections.

2. Analysis

The Office of General Counsel has analyzed the constitutional issues raised in the comments, and believes that limits on the receipt of soft money by national party committees would be constitutionally permissible. As explained in detail below, we believe the record shows that the national party committees are using funds from prohibited sources and in excess of the individual contribution limits to influence federal elections. Limits on soft money donations to the national party committees would implement the contribution limitations and prohibitions in the FECA by ensuring that soft money is not used for this purpose. In Buckley, the Supreme Court held that the contribution prohibitions and limitations serve the compelling government interest in preventing corruption and the appearance of corruption in the political process. 424 U.S. at 26-27. The Supreme Court recently reaffirmed its conclusion that contribution limits serve a compelling governmental interest. Nixon v. Shrink Missouri Government PAC, No. 98-963, 2000 WL 48424 (U.S. Jan. 24, 2000) ("Shrink Missouri"). Therefore, we believe that limits on the receipt of soft money by the national party committees would be constitutionally permissible.

We disagree with the commenters who argued that the proposed rules would be an unconstitutional limit on party committee expenditures. Nothing in the draft final rules would limit the amount that a national party committee could spend on any activity. Party committees could continue to engage in the activities that they currently allocate, and could continue to make unlimited transfers to state and local party committees. The rules would merely require them to use hard dollars for these activities. Thus, the national committees' ability to make expenditures would be limited only by their ability to raise funds subject to the contributions limits. As Buckley recognized in upholding the contribution limits,

> [t]he overall effect of the Act's contribution ceilings is merely to require candidates and political committees to raise funds from a greater number of persons and to compel people who would otherwise contribute amounts greater than the statutory limits to expend such funds on direct political expression, rather than to reduce the total amount of money potentially available to promote political expression.

Id. at 22. One district court reached the same conclusion regarding section 106.5 of the current allocation rules.

> With this regulation, the FEC is not seeking a spending cap on advertisements that influence federal campaigns, but rather is attempting to ensure that political parties do not facilitate any impression that wealth can buy access to our important federal decision makers. This regulation simply requires political parties to reach out to a greater number of constituents in order to increase their hard money reserve.

Ohio Democratic Party, et al, v. FEC, No. 98-0991, slip op. at 3 (D.D.C. Jun. 25, 1998).

Furthermore, we believe that the Commission can regulate funds donated to party committees regardless of whether those funds are used for activity that involves express advocacy. The court decisions applying the "express advocacy" standard involved direct restrictions on independent expenditures. As explained above, nothing in the draft final rules would limit independent expenditures by national party committees. Thus, these cases are inapplicable. "[T]he [Buckley] Court limited [the express advocacy requirement] to those provisions curtailing or prohibiting independent expenditures. This definition is not constitutionally required for those statutory provisions limiting contributions." Orloski v. FEC, 795 F.2d 156, 167 (D.C. Cir. 1986). The Supreme Court has "consistently held that restrictions on contributions require less compelling justification than restrictions on independent spending." FEC v. Massachusetts Citizens for Life, Inc., 479 U.S. 238, 259-60 (1986). See also Shrink Missouri, 2000 WL 48424 at *5 ("While [Buckley] did not then say in so many words that different standards might govern expenditure and contribution limits affecting associational rights, we have since said so explicitly in [FEC v. Massachusetts Citizens for Life].").

Several comments argued that there is no evidence of corruption or the appearance of corruption in the current system, and therefore the rules are not justified by a compelling governmental interest. In support of this argument, one national party committee asserted that, according to public opinion polls, campaign finance reform is not an important issue to the American public. The committee also asserted that Congress' high approval rating rebuts any suggestion that the public perceives Congress to be corrupt. In further support of its position, the committee submitted a memorandum prepared by The Tarrance Group summarizing the findings of a survey of voter attitudes on campaign finance reform. The memorandum states that

> [c]ampaign reform is simply not on the radar screen with voters at this time. Just one person out of one thousand - one tenth of one percent - volunteers the issue as the biggest problem facing the country. . . [t]he relative low importance of campaign finance reform is substantiated further in the fact that it rates extremely low again even when the issue is listed in a short recitation of prominent concerns. . . . Even in the context of political reforms, campaign finance reform ranks fourth of seven reforms among the voters. Only 7% think campaign finance reform is the most important reform that Congress should deal with right now. . . ."

Tarrance Group Memorandum at 1-2 (emphasis in original).

The Office of General Counsel believes that there is a wealth of evidence of corruption and the appearance of corruption in the current system. For example, although the Tarrance Group Memorandum concludes that campaign finance reform is not the highest priority issue among voters, it also acknowledges that "46 % of the electorate asserts that it is extremely or very important to them personally that their Member of Congress support campaign finance reform. As with many issues, campaign finance reform is important to voters as a singular issue, but in the context of all the issues, it simply is not going to be the

vote-motivating issue for the vast majority of American voters." Tarrance Group Memorandum at 3. Thus, if the public's views on campaign finance reform are to be treated as an indicator of the extent to which the current system creates an appearance of corruption, these poll results suggest that some appearance of corruption exists, regardless whether a candidate's position on the issue of campaign finance reform would affect the outcome of an election.

A survey of money and politics conducted by the Princeton Survey Research Associates supports this interpretation. The survey concludes that "[A]mericans may not understand the basics of the campaign finance system, but they are clearly troubled by the role that money plays in contemporary politics." Money and Politics Survey, Princeton Survey Research Associates for the Center for Responsive Politics, at 1 <http://www.opensecrets.org/pubs/survey/s2.htm> ("Princeton Survey"). Princeton surveyed 1404 adults aged 18 or older in April of 1997. About 65% of those surveyed believe "excessive influence of political contributions on elections and government policy is a major problem with the system," and that "the conflicts of interest created when elected officials solicit or accept political contributions while they are making policy decisions" is also a major problem. Id. More than 7 in 10 believe that money in politics is a systemic problem, and assume that it "give[s] the rich and powerful special access to members of Congress." Id. at 2. The Princeton report acknowledged that

> only 15% of Americans think campaign finance reform should be Washington's top priority. And people overwhelmingly believe that . . . major social and economic problems, such as improving education, fighting crime, reforming Medicare, and balancing the federal budget, should take precedence. . . Such greater concern about other national problems, however, does not mean that Americans have been unaffected by news reports about questionable fundraising. History suggests that political reform will never rank first on the public's agenda.

Id. (emphasis in original).

The Thompson Committee Report revealed significant evidence of real or apparent corruption resulting from the use of soft money in the 1995-96 Presidential election. The Senate Committee investigated national party committee campaign funding practices during the election, and concluded that, in spite of the prohibitions and limitations in the FECA, soft money played a significant role.

> During the 1996 federal election cycle, the[] restrictions on the use of "soft" money were ignored; the DNC became a shadow re-election campaign, allowing the President to spend more than the federal limits to which he had agreed in accepting partial public financing for his campaign. In short, the President used the DNC for an end-run around restrictive federal campaign laws.

Thompson Committee Majority Report, Ch.4 at 10-11 (footnotes omitted). The Committee's report contains bipartisan criticism of the use of soft money. The Minority Report states that

> **(1) The most insidious problem with the campaign finance system involved soft (unrestricted) money raised by both parties.** The soft money loophole, though legal, led to a meltdown of the campaign finance system that was designed to keep corporate, union and large individual contributions from influencing the electoral process. . . . **(3) Both parties went to significant lengths to raise soft money, including offering access to party leaders, elected officials, and exclusive locations on federal property in exchange for large contributions. Both parties used issue ads, which were effectively indistinguishable from candidate ads and which -- unlike candidate ads -- can be paid for in part with soft (unrestricted) money, to support their candidates."**

Thompson Committee Minority Report, Findings at 19 (emphasis in original). The Minority Report described soft money as a "fundamental flaw[] in the existing legal and regulatory system," Id., Executive Summary at 4, and also said "[t]he appearance of corruption, in which large contributions appear to be traded for access to government officials or favored treatment, and the resulting loss of public confidence in government are two of the most serious consequences of the soft money system." Id., Ch. 23 at 5.

As indicated above, a current Member of Congress testified that soft money has a corrupting influence because soft money donations buy access to members of Congress. He specifically rejected assertions that smaller donors have as much access to members as large donors, and noted that Members of Congress look for innovative ways to provide access in order to increase receipts. Hearing Transcript at 324.

A group of business and academic leaders issued a report that reaches similar conclusions, and strongly criticizes the current soft money system. The Committee for Economic Development ("CED"), a nonprofit, nonpartisan, and nonpolitical independent research and policy organization of 250 business leaders and educators, recently published a report entitled Investing in the People's Business: A Business Proposal for Campaign Finance Reform, Committee for Economic Development (1999) ("CED Report"). CED's report concludes that, among other things, national party committees "rely in large part on the access they can provide to federal officials, or on the more direct influence of federal officeholders and candidates, to solicit large sums from corporations, labor unions, and other donors that provide most of their soft money." Id. at 22.

> In recent years, both major parties have offered soft money donors access to elected leaders in exchange for contributions. White House officials and congressional leaders have been asked to appear at fundraisers, participate in party-sponsored policy briefings, attend weekend retreats with donors, and play a role in other small group meetings. Elected officials have even been recruited by the party committees to solicit soft money donations from

> potential contributors, especially from their own financial supporters and others with whom they have a relationship. Federal officeholders have thus assisted their parties in raising funds for issue advocacy advertising, voter registration, election day turnout drives, and other activities that directly benefit their own campaigns for office.

Id. at 27. The report notes that the largest soft money donors tend to be "companies or industries that are heavily regulated by the federal government," and lists a number of examples. "These examples, which are not atypical, demonstrate how ineffective the party contribution limits established by FECA have become in practice." Id. The CED report also concludes that the appearance of corruption in federal elections has a significant effect on public attitudes. "Given the size and source of most soft money contributions, the public cannot help but believe that these donors enjoy special influence and receive special favors. The suspicion of corruption deepens public cynicism and diminishes public confidence in government." Id.

It is true that one district court has said that providing access to candidates or officeholders is not corruption or the appearance of corruption.

> "The hallmark of corruption is the financial quid pro quo: dollars for political favors." [FEC v. National Conservative Political Action Committee], 470 U.S. at 497. The FEC's attempt to broaden the definition of corruption to include mere access is unsupported by precedent.

Colorado Republican, 41 F. Supp. 2d 1197, 1209 (D. Colo. 1999) (opinion on remand).

However, the Office of General Counsel believes this court's conclusion is inconsistent with Buckley and Shrink Missouri. To the extent this court is saying that no corruption exists absent an exchange of money for a discreet, identifiable legislative action, the court effectively equates the concept of corruption with bribery. The Buckley Court recognized that some quid pro quo arrangements that fall short of criminal bribery can also be corruptive, and concluded that Congress could enact contribution limits to address this concern.

> Appellants contend that the contribution limitations must be invalidated because bribery laws and narrowly drawn disclosure requirements constitute a less restrictive means of dealing with "proven and suspected quid pro quo arrangements." But laws making criminal the giving and taking of bribes deal with only the most blatant and specific attempts of those with money to influence governmental action. . . . Congress was surely entitled to conclude that disclosure was only a partial measure, and that contribution ceilings were a necessary legislative concomitant to deal with the reality or appearance of corruption inherent in a system permitting unlimited financial contributions, even when the identities of the contributors and the amounts of their contributions are fully disclosed.

Buckley, 424 U.S. at 27-28 (footnote omitted). The Supreme Court recently reaffirmed this conclusion in Shrink Missouri.

> In defending its own statute, Missouri espouses those same interests of preventing corruption and the appearance of it that flows from munificent campaign contributions. Even without the authority of Buckley, there would be no serious question about the legitimacy of the interests claimed, which, after all, underlie bribery and anti-gratuity statutes. While neither law nor morals equate all political contributions, without more, with bribes, we spoke in Buckley of the perception of corruption 'inherent in a regime of large individual financial contributions' to candidates for public office . . . as a source of concern 'almost equal' to quid pro quo improbity. . . . Leave the perception of impropriety unanswered, and the cynical assumption that large donors call the tune could jeopardize the willingness of voters to take part in democratic governance.

2000 WL 48424 at *6 (quoting Buckley, 424 U.S. at 27).

The Supreme Court and Court of Appeals decisions in Buckley also recognized that the provision of access in exchange for donations of soft money is a quid pro quo in the sense that it provides a donor with an opportunity to influence a candidate or officeholder that is not available to those who have not made a similar donation. In upholding contribution limits, the D.C. Circuit cited testimony by oil and airline industry executives "that they were motivated [to make corporate contributions] by the perception that this was necessary as a 'calling card, something that would get us in the door and make our point of view heard' . . . or 'in response to pressure for fear of a competitive disadvantage that might result.'" Buckley v. Valeo, 519 F.2d 821, 839 n.37 (D.C. Cir. 1975) (citations omitted). The Court of Appeals also said "[t]he quality of political contributions as denotive of freedom of thought and association must be reappraised realistically, so far as large contributions are concerned, in the light of the common practice of many large donors of contributing to both candidates for the same office . . . Large contributions are intended to, and do, gain access to the elected official after the campaign for consideration of the contributor's particular concerns." Id. at 838 (footnotes omitted).

On appeal, the Supreme Court cited these "deeply disturbing examples" as evidence that "the problem [of large contributions being given to secure political quid pro quos from current and potential office holders] is not an illusory one." 424 U.S. at 26-27 & n.28. The Supreme Court also cited this evidence approvingly in Shrink Missouri. In reviewing its own opinion in Buckley, the Shrink Missouri Supreme Court said

> Although we did not ourselves marshal the evidence in support of the congressional concern, we referred to "a number of the abuses" detailed in the Court of Appeals's decision . . . The evidence before the Court of Appeals described public revelations by the parties in question more than sufficient to

show why voters would tend to identify a big donation with a corrupt purpose . . . [and] exemplifies a sufficient justification for contribution limits.

2000 WL 48424 at *6 (citing Buckley v. Valeo, 424 U.S. at 27, and n.28, and 519 F.2d at 839-840, and nn. 36-38). According to the Thompson Committee Report, the national party committees provide donors with access to federal officeholders in exchange for soft money donations.[6] On the basis of the Buckley and Shrink Missouri opinions, we believe these practices result in actual or apparent corruption, and that rules written to limit these practices would be justified by a compelling governmental interest.

Some commenters urged the Commission to reject the proposed rules because inflation has reduced the value of permissible hard dollar contributions. However, in Shrink Missouri, the Supreme Court rejected a similar argument, saying that Buckley did not set a minimum constitutional threshold for contribution limits. 2000 WL 48424 at *8. Therefore, the reduction in value resulting from inflation would not, by itself, render previously constitutional limits unconstitutional. Furthermore, the Office of General Counsel believes that rejecting the proposed rules in order to compensate for the effects of inflation would be inconsistent with the FECA. Congress wrote specific dollar limits into section 441a(a) without indicating any intent to index those limits for inflation. In contrast, the dollar limits on expenditures by Presidential candidates in section 441a(b) are adjusted for changes in the Consumer Price Index. 2 U.S.C. § 441a(c). We believe this indicates that Congress specifically chose not to index the contribution limits in section 441a. Allowing the national party committees to use soft money to offset the reduced value of hard dollar contributions would be inconsistent with this legislative decision. Congress can always amend the FECA to raise the contribution limits or index the limits for inflation, or both, if it believes such a legislative change is necessary.

With regard to the associational rights of the national party committees, the Office of General Counsel believes the draft final rules set out below would be constitutionally permissible. The rules would not limit a national party committee's ability to confer with or engage in joint activities with its state and local affiliates in any way. For example, the national committees could continue to engage in joint fundraising activities with their state and local affiliates, so long as the rules regarding the receipt of contributions are observed. See section 102.5 of the draft final rules. Furthermore, the national party committees could continue to make and receive unlimited hard dollar transfers to and from their state and local affiliates. 2 U.S.C. § 441a(a)(4), 11 CFR 110.3(c). In short, the draft final rules would not alter the national party committees' ability to participate in state election activity in any way. They would merely require the national committees to use hard dollars to pay for activities that they currently finance with a mixture of federal and nonfederal funds.

Nor do we believe that the draft final rules would raise significant Tenth Amendment issues. The rules do not require the states to promulgate regulations directed at private parties, nor do they impose regulatory requirements on the states themselves. In Blount v.

[6] See e.g., Thompson Committee Majority Report, Ch. 3, Summary of Findings, and Thompson Committee Minority Report, Executive Summary.

SEC, 61 F.3d 938 (D.C. Cir. 1995), the D.C. Circuit rejected a Tenth Amendment challenge to the Securities and Exchange Commission's "pay-to-play" rule, which states that a municipal securities professional that has made a contribution of $250 or more to an official of any "issuer," i.e. state or local government, is prohibited from doing business with that issuer for a period of two years after the contribution. Id. at 940-41. The court analogized the pay-to-play rule to the contribution limits in the FECA that were upheld in Buckley, saying

> the object in Buckley and the other campaign finance cases was not only, as here, to prevent direct quid pro quos (and the appearance thereof) but more broadly to reduce the indirect impact of wealth on the electoral process, including the pervasive impact on both candidates and the public at large of messages communicated by the wealthy in that process.

61 F.3d at 943 (emphasis added). With regard to claims that the pay-to-play rule is "an effort to regulate state election campaigns and, as such, usurps the states' power to control their own elections," the court said

> [t]his contention is meritless. [The rule] neither compels the states to regulate private parties, as the Tenth Amendment prohibits . . . nor regulates the states directly. . . . Further, the rule does not have anything resembling the kind of preemptive effect on states' ability to control their own election processes that might be perceived as "destructive of state sovereignty."

Id. at 949 (quoting New York v. United States, 505 U.S. 144, 160, (1992), Garcia v. San Antonio Metropolitan Transit Authority, 469 U.S. 528, 554 (1985). Thus, the court concluded that federal agency rules that prohibit certain individuals from making contributions directly to state and local candidates do not violate the Tenth Amendment.

The draft final rules set out below are less intrusive than the pay-to-play rule. They would allow the national party committees' to donate soft money directly to nonfederal candidates, and would also allow the national committees to make direct disbursements expressly advocating the election or defeat of these candidates. For these reasons, we believe they would not violate the Tenth Amendment.

With regard to the issue of preemption, section 453 of the FECA states that "[t]he provisions of this Act, and of rules prescribed under this Act, supersede and preempt any provision of State law with respect to election for Federal office." The draft final rules would only preempt state law to the extent that those laws specifically allow national party committees to use soft money to engage in generic activity related to state and local elections. We believe that the Act's broad preemption provision encompasses this modest encroachment. The draft final rules seek to implement the prohibitions and limitations in the Act by minimize the use and influence of soft money in federal elections. In Weber v. Heaney, 955 F.2d. 872 (8th Cir. 1993), the U.S. Court of Appeals for the Eighth Circuit concluded that, with regard to the contribution and expenditure limits, "Congress explicitly

stated in 2 U.S.C. § 453 its intent that FECA preempt state law." Id. at 875. Therefore, we do not believe the draft final rules would exceed the Commission's preemption authority.[7]

3. Conclusion

For these reasons, the Office of General Counsel believes that a prohibition on the receipt of soft money by national party committees, with the limited exceptions provided for in these rules, would be constitutionally permissible.

C. The Impact of Soft Money

1. Comments

a. Minimal impact

Some commenters argued that the impact of soft money under the current system is overstated. One national party committee claimed that soft money represents only 34% of its receipts, and that a $100,000 soft money donation is only 0.1% of its receipts, which is not enough to influence a candidate or officeholder. This commenter also argued that the real crisis is in hard money, since inflation has reduced the value of hard dollar contributions. The commenter said that if the contribution limits were adjusted for inflation, about two thirds of the soft money donations would be permissible contributions. At same time, campaign and fundraising costs have increased even faster than the rate of inflation. The commenter also said that large soft money donors do not receive greater access than small donors.

This commenter and others said there is no solid evidence that soft money is being used to influence federal elections, and that there is no evidence that soft money leads to corruption or the appearance of corruption. They argue that soft money is used for legitimate nonfederal election activity. Another national party committee said that increases in the receipt and use of nonfederal funds for legitimate nonfederal activities are not proof of abuse, particularly where those funds are regulated by state law.

b. Significant impact

In contrast, several commenters said that soft money has a significant impact on federal elections. These commenters said that party committees are using soft money to influence federal elections, thereby evading the prohibitions and limitations in the Act. They claim that the system allows party committees to use large donations from individuals and corporate and labor organization general treasury funds to support federal candidates. These commenters argue that this is exactly what the FECA was designed to eliminate.

[7] We note that while the Commission is not subject to Executive Order 13132 on Federalism, 64 FR 43255 (Aug. 10, 1999), we believe the draft final rules would not conflict with this Executive Order.

Several commenters also said that transfers from national party committees to state party committees further undermine the FECA. One commenter said that these transfers effectively obliterate the distinction between hard and soft money. In some situations, the national party committee continues to control the transferred funds, but the state party spends the funds using its own allocation ratios, which results in the use of a larger percentage of soft money. In other situations, the state party returns an equal or similar amount of its hard money to the national committee. Thus, from the national party committee's standpoint, the transfer effectively transforms soft dollars into hard dollars that can permissibly be used to influence federal elections.

2. Analysis

a. Increases in the receipt and use of soft money

The Commission promulgated the allocation rules in 1990 in response to the District Court's decision in Common Cause. As explained above, the Common Cause court concluded that the Commission's previous rules allowing state and local party committees to allocate the costs of campaign materials used for volunteer activities, voter registration and get-out-the-vote drives "on a reasonable basis" were contrary to law because the FECA clearly states that state party committee expenditures for these activities vis-à-vis federal elections "must be paid for 'from contributions subject to the limitations and prohibitions of this Act'. . . . That is, with respect to federal elections, 'soft money' cannot properly be used for these activities under the FECA." Id. at 1395 (quoting 2 U.S.C. §§ 431(8)(B)(x)(2) and (xii)(2), 431(9)(B)(viii)(2) and (ix)(2)). The court directed the Commission to promulgate more specific rules to ensure the proper allocation of the costs incurred by state party committees. "The plain meaning of the FECA is that any improper allocation of nonfederal funds by a state committee would be a violation of the FECA." Id. at 1396.

At the time the rules were promulgated, it was difficult to determine the extent to which the national party committees were raising and spending soft money, since there was no systematic disclosure of soft money activity, and no uniform guideline for allocating expenses. Consequently, the Commission declined the Common Cause court's invitation to require 100% federal allocation, under which national party committees would be required to finance their mixed activities entirely with hard dollars. Instead, the Commission established specific allocation methods and required additional disclosure by the national committees. The Commission believed this approach would adequately ensure that the national party committees would not use significant amounts of soft money to influence federal elections.

However, circumstances have changed since promulgation of the allocation rules in 1990. Many recent developments raise questions as to whether the allocation rules have allowed the national party committees to use large contributions from prohibited sources and in excess of the hard dollar limits in ways that, in fact, influence federal elections, even though they are ostensibly being used for nonfederal election activity.

One significant development is the dramatic increase in the amount of soft money raised and spent by the national party committees. As indicated in the NPRM, the national party committees raised $86 million in soft money in the 1991-92 presidential election cycle. This amount increased to $262.1 million in soft money during the 1995-96 election cycle. Similarly, soft money disbursements, which were $79.1 million in the 1992 election cycle, increased to $271.5 million in the 1996 election cycle. National Party Committee Nonfederal Activity, <http://www.fec.gov/press/sftlong.htm> ("Nonfederal Summary"). The disclosure reports submitted by the parties also show that the soft money receipts of the national party committees continued to increase in the 1997-98 election cycle. The committees raised $101.6 in soft money during the 1993-94 mid-term election cycle. This amount increased to $224.4 million in soft money during the 1997-98 election cycle. Id. These increases have continued through the first six months on the 1999-2000 election cycle. The national party committees collected $57.2 million in soft money during that period, up from the $27.2 million collected during the same portion of the 1995-96 election cycle. Id.

Furthermore, the percentage of all national party committee receipts that are soft dollars is steadily increasing. Soft money represented 36% of the receipts of the Democratic national party committees in the 1994 election cycle, and 42% in the 1998 cycle. The Republican national party committees receipts were 23% in the 1994 cycle and 36% in the 1998 cycle. Compare Nonfederal Summary, Id., with Democratic Party Financial Activity, <http://www.fec.gov/press/demhrd98.htm> and Republican Party Financial Activity, <http://www.fec.gov/press/rephrd98.htm>. A recent study that examined the impact of soft money spent in the 1997-98 election cycle noted that the increases in soft money donations, when compared to the more modest increases in hard money contributions, may reflect an increased reliance on the use of soft money to influence federal elections.

> Both parties in the aggregate gave at least 56 percent less money to candidates in hard money contributions in 1998 that they did in 1994, the previous mid-term election. Party coordinated expenditures also fell by at least 58 percent in both parties. This reversed the trend for increased hard money spending that persisted in pervious [sic] election cycles, suggesting that both parties focused their fundraising on soft money rather than hard money in 1998.

Outside Money: Soft Money & Issue Ads in Competitive 1998 Congressional Elections, David Magleby & Marianne Holt (1999) at 12 ("Outside Money").

There is also evidence that an increasing number of donors are using the national party committees' nonfederal accounts as an avenue through which they can make contributions that would be prohibited under sections 441b or 441c or would be excessive under section 441a. Some individual contributors may also be using these accounts to make contributions that would otherwise exceed their $25,000 overall contribution limit. The NPRM noted that, in the 1991-92 election cycle, national party committee nonfederal accounts received 381 donations from individuals that exceeded $20,000, and 11,000 donations from sources such as corporations and labor organizations that are prohibited from making contributions in connection with federal elections. In the 1995-96 election cycle,

these numbers increased to 1000 individual donations exceeding $20,000 and approximately 27,000 donations from corporations and labor organizations. 63 FR at 37227. This trend continued in the 1997-98 election cycle, when compared to the previous midterm election cycle. In the 1993-94 cycle, national party committee nonfederal accounts received 353 individual donations in excess of $20,000 and 9605 donations from corporations, labor organizations and federal contractors. In 1997-98, the national parties' nonfederal accounts received 834 individual donations of more than $20,000, and 22,984 donations from corporations and labor organizations. Thus, the number of each type of donation has more than doubled in four years.

Not surprisingly, the amount of soft money spent by the national party committees on allocable activities has also increased significantly. In the 1991-92 presidential election cycle, the national party committees reported spending a total of $44.1 million on the nonfederal share of mixed activities. In the 1995-96 cycle, the amount doubled to $90.5 million. Similarly, the 1993-94 amount, $43.3 million, increased to $94.8 million in the 1997-98 cycle.[8] Thus, there has been a rapid increase in the amount of soft money spent by the national party committees on mixed activities since promulgation of the allocation rules. It is also worth noting that the amount spent in the most recent cycle, a mid-term election in which there were no presidential candidates on the ballot, was larger than the amount spent in the presidential election two years before.

The national party committees spent additional amounts of soft money on mixed activities that are not reflected in these totals. The Thompson Committee Report indicates that

> to take advantage of the current system, national party committees have begun transferring soft money to state party committees to utilize the various states' higher soft money allowance. Substantial amounts of such transfers are made to state and local political parties for "generic voter activities" that in fact ultimately benefit federal candidates because the funds for all practical purposes remain under the control of the national committees. The use of such soft money thus allows more corporate, union treasury, and large contributions from wealthy individuals into the system. . . . Recent history is replete with evidence that these different state and national allocation formulas are being utilized to circumvent the FECA.

Thompson Committee Majority Report, Ch. 32 at 14-16. As with receipts and disbursements, the disclosure reports filed by the national party committees show a dramatic increase in the amount of soft money transferred to state and local party committees since the promulgation of the allocation rules. In the 1991-92 presidential election cycle, the national party committees transferred a total of $33 million to state and local party committees. In the 1995-96 cycle, the national committees transferred $217.3 million, more than six times the amount transferred in 1991-92. The amounts transferred during successive midterm election

[8] These figures are drawn from the disclosure reports submitted by the party committees. See FEC Form 3X, Detailed Summary page, Line 18.

cycles also increased. In the 1993-94 cycle, the parties transferred $37.8 million. In the 1997-98 cycle, the amount transferred increased to $69 million. Thus, it is likely that the national parties are spending large of amounts of soft money on mixed activities indirectly, by first transferring this money to the state and local party committees.

b. The impact of soft money on federal elections

There is strong evidence that the increased used of soft money by the national party committees, both directly and through transfers to state and local party committees, is having a significant impact on federal elections. The Thompson Committee Report concluded that the DNC

> illegally utilize[d] approximately $44 million in national committee soft money to their candidate's advantage through electioneering messages that they claim to be pure issue advertisements. These advertisements carefully avoided expressly advocating the election of President Clinton, but these party committee expenditures were clearly made for the purpose of influencing the Presidential election.

Thompson Committee Majority Report, Ch. 32 at 13-14. The Minority Report said

> Soft money . . . is not supposed to be spent on behalf of individual candidates. And yet it is: Tens of millions of soft dollars are raised by the parties and spent, through such devices as "issue advocacy" ads, for the benefit of candidates. The soft money loophole undermines the campaign finance laws by enabling wealthy private interests to channel enormous amounts of money into political campaigns.

Thompson Committee Minority Report, Executive Summary at 13.

Several research studies of recent political campaigns also concluded that the increased used of soft money by party committees is having a significant impact on federal elections. In the Outside Money study referred to above, researchers examined the impact of money spent by political parties and interest groups on sixteen federal races in the 1997-98 election cycle. The first of the study's three findings is that

> soft money contributors, especially the large donors, have become much more important to competitive congressional elections. The congressional party committees are now much more important because of the large amounts of money they spend in competitive races.

Outside Money at 1. The report also states that "[t]he close margin of party control in the U.S. House and the frequent shift of party control in the U.S. Senate in recent decades has strengthened the power of the congressional campaign committees in allocating money, especially soft money, to the most competitive races." Outside Money at 20.

The CED report contains four recommendations for changing the current campaign finance system. CED's first recommendation for change is to eliminate soft money.

> As a general principle, funds used to promote political candidacies should be subject to the requirements and restrictions of federal campaign finance law. Soft money is the most egregious example of campaign financing that violates this principle. No reform is more urgently needed than a ban on national party "soft money" financing.

Id. at 4 (emphasis in original).

The CED Report also discusses the national party committees' practice of transferring soft money to state and local party committees. The Report notes that the national committees provide access to federal officials in exchange for large soft money donations, and "then distribute a share of these monies to state party committees, who usually spend these funds in accordance with national party directives." CED Report at 22. The allocation rules allow the state party committee to pay a larger portion of the costs of a mixed activity with soft dollars than the national party would be able to if it financed the same activity directly. Thus, these transfers enable the national party committee to conserve a significant amount of hard dollars. By controlling the state party committee's use of the funds, the national committee is, in effect, conducting the activity itself, but paying for the activity using the state committee's allocation ratios.[9]

According to the Outside Money report, national party committees also transfer soft money to state and local party committees in order to transform those funds into hard dollars.

> [s]ome state parties serve as laundering stations where national parties can contribute soft money and in return receive hard money contributions from state parties. This enables the state party to keep a bit "off the top" and allows the national party committee to receive hard money, which can be used for more things than soft money.

Outside Money at 14. The national committee then uses the hard dollars received from the state or local committee to directly assist candidates for federal offices.

The CED Report also said that one of the primary ways in which party committees use soft money to influence federal elections is by financing issue advocacy advertisements. "Party committees were the biggest issue advocacy spenders because they could then finance advertising that directly benefited their candidates with soft money. Each of the major parties

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[9] See, e.g., Thompson Committee Majority Report, Ch. 32 at 16-18 ("Recent history is replete with evidence that these different state and national allocation formulas are being utilized to circumvent the FECA." Id. at 16. "Th[ese] scheme[s] to avoid FEC mandated allocation is especially odious in that it allows national party committees to continue to control the content and placement of advertisements, and at that same time avoid adherence of the FEC's specific regulations." Id. at 18.). See also Thompson Committee Minority Report, Executive Summary.

spent tens of millions of dollars on ads designed to support its presidential candidate. Both parties also sponsored ads that sought to influence the voting in marginal congressional races." Id. at 29.

The Annenberg Public Policy Center studied issue advocacy during the 1997-98 election cycle. Issue Advocacy Advertising During the 1997-1998 Election Cycle, Jeffrey D. Stranger & Douglas G. Rivlin, Annenberg Public Policy Center (1999) <http://www.appcpenn.org/issueads/> ("Annenberg Study"). The study defined three categories of issue advocacy advertisements:

> Issue advertisements are either legislatively-focused, general policy or candidate-centered. Legislative issue ads seek to mobilize constituents or policy makers in support of or in opposition to pending legislation or regulatory policy. General policy issue ads are more broadly gauged to enhance the visibility of an organization or its issue positions, but are not tied directly to a pending legislative or regulatory issue. Finally, candidate-centered issue ads couch their arguments in terms of candidates for office that either support or oppose the advocacy organization's or party's policy stance. Because they do not explicitly call for the election or defeat of the candidate . . . they are not considered election activity, and therefore fall outside the regulatory jurisdiction of federal election law.

Annenberg Study at 4. The Center's report shows that the party committees concentrated their issue advocacy activities in the two months just before the election. The parties committees were responsible for just 10% of the issue ads that ran from January 1997 through August of 1998, but were responsible for more than 70% of the issue ads that ran after September 1, 1998. The study also revealed a shift from legislative to candidate-centered issue advocacy advertisements during the two months prior to the 1998 election. Prior to September 1, 1998, only 35% of the issue ads mentioned candidates. In contrast, 80% of those that appeared after September 1, 1998 mentioned candidates. "Clearly, candidate-centered became the dominant form of issue advocacy as Election Day approached." Annenberg Study at 4.

The study also examined the extent to which issue advocacy advertisements were "attack-oriented,"[10] and compared issue ads that ran after September 1 to advertisements run by candidates during the same period. The report indicates that, prior to September 1, one-third of the issue ads were attack ads, but after September 1, more than half of the issue ads were attack ads. The report attributes this increase "primarily to the entry of party issue ads, of which 59.5% were pure attack ads." Id. at 8. This is in contrast to non-party issue ads that aired after September 1, which only attacked 32.0% of the time. It also stands in contrast to candidate sponsored ads run in the same period, of which only 24% were attack ads.

[10] A prior Annenberg study defined "pure attack" as "a case made only against the opposing position." *Issue Advocacy Advertising During the 1996 Campaign*, Deborah Beck, *et al*, Annenberg Public Policy Center (1997) <http://appcpenn.org/issueads/past_research.htm>.

Thus, the study showed increased party committee issue advocacy after September 1, increased overall use of candidate-centered issue ads after September 1, and increased use of attack-oriented ads after September 1. This suggests that the party committees run issue ads to indirectly attack their candidates' opponents just before the election. "The data show that party issue ads were used in the final phases of the campaign to attack, leaving candidates to take the higher road of self-advocacy and comparison." Id.

Based on the foregoing, the Office of General Counsel believes that the increased use of soft money by the national party committees is having a significant influence on federal elections.

D. CONCLUSION

1. National party committees

Because of the developments described above, the Office of General Counsel believes that, with regard to the national party committees, the allocation rules are no longer adequately serving the purpose for which they were promulgated. The rules are allowing national party committees to channel significant amounts of soft money into activities that influence federal elections. "Under the FECA's current system of contribution limitations . . . soft money spending by political party committees eviscerates the ability of the FECA to limit the funds contributed by individuals, corporations, or unions for the defeat or benefit of specific candidates." Thompson Committee Majority Report, Ch. 32 at 18. "The massive use of soft, or unrestricted, money is a relatively new phenomenon in the campaign financing system. Since 1988 it has become the crux of many of the problems examined by the Committee, including the offers of access for large contributions and the use of party-run issue ads on behalf of candidates." Thompson Committee Minority Report, Findings at 19.

Therefore, the Office of General Counsel recommends that the Commission promulgate new rules to limit the receipt and use of soft money by the national party committees. We have prepared draft final rules for the Commission's consideration. These rules are set out in Part V., below.

2. State and local party committees

The second and third variations on the core proposal in the proposed rules were directed at the use of soft money by state and local party committees. Both of these variations would revise section 106.5 in an effort to ensure that hard money transferred from a national to a state or local party committee is spent by the recipient committee using the rules applicable to the national committee, rather than the state or local committee's more favorable allocation ratios. Variation two would require the national committee to earmark transferred funds for a particular activity, and would require the recipient committee to finance the identified activity entirely with hard dollars. Variation three would require state and local party committees to finance their mixed activities entirely with hard dollars.

The Commission received several comments directed specifically at these two variations. Two commenters opposed variation two, saying that the Commission should not limit transfers from national to state and local party committees, and questioning whether it would be lawful for the Commission to do so. In contrast, three commenters urged the Commission to reject variation two because it would allow state party committees to continue to allocate the costs of mixed activities. This would undermine the core proposal's limits on the receipt of soft money by the national party committees, these commenters said, because the national committees would simply divert soft money donors to state party committees, thereby shifting the soft money problem to the state and local level. These three commenters preferred variation three.

Four commenters specifically addressed variation three. Three commenters supported this alternative. One of these commenters said variation three is the only option that is consistent with the finding that soft money influences federal elections. Another of these commenters urged approval of this limit, saying that the party committees will exploit any opportunity to use soft money to influence elections. The fourth commenter, a national party committee, urged the Commission to adopt variation three, but modify it slightly to allow state party committees to allocate their administrative expenses.

The Office of General Counsel recognizes that imposing limits on the receipt of soft money by the national party committees without also limiting allocation by state and local party committees may simply redirect the flow of soft money to state and local committees, and may not eliminate the use of soft money to influence federal elections.

However, as discussed above, the House Report accompanying the 1979 amendments contains language suggesting that Congress intended to allow state and local party committees to allocate the costs of slate cards and volunteer activities. H.R. Rep. No. 96-422 at 8, 9 (1979). This raises questions as to whether the Commission has the authority to require state and local party committees to pay the costs of these activities entirely with hard dollars.

Furthermore, we are reluctant to recommend changes to the state and local party committee allocation rules without more evidence of abuse by these committees. Although state and local party committees spent significant and increasing amounts of soft money on allocable activities during the last four election cycles,[11] a portion of this soft money was transferred from national party committees.[12] The draft final rules would eliminate these transfers. If these rules are implemented, the amount of soft money spent by the state and local party committees on allocable activities may be much less significant.

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[11] In the 1991-92 presidential election cycle, state and local party committees spent a combined total of $70.5 million in soft money on the nonfederal share of the costs of allocable activities. In the 1995-96 election cycle, this amount increased to $167.1 million. In the 1993-94 election cycle, state and local party committees spent $88.4 million, compared to $162.5 million in 1997-98.

[12] For statistics on transfers from national to state and local party committees, see p. 34, supra.

For these reasons, the Office of General Counsel concludes that it is premature to recommend changes to the allocation rules applicable to state and local party committees. We think it would be more appropriate to adopt a step-by-step approach, and defer any revisions to the state and local party committee allocation rules until the impact of the draft rules regarding national party committees can be determined. Instead of promulgating new rules applicable to state party committees, we believe the Commission should monitor the soft money activities of these committees, and take appropriate regulatory action as it becomes necessary.

Therefore, the Office of General Counsel recommends that the Commission make no substantive changes to the allocation rules for state and local party committees at this time.

V. EXPLANATION OF THE DRAFT FINAL RULES

A. National party committees, including the Senate and House campaign committees of the national parties

The draft final rules would prohibit the national party committees from operating nonfederal accounts, and require them to make all disbursements from funds that are permissible under the FECA, subject to two limited exceptions. First, the rules would allow national party committees, including the Senate and House campaign committees, to maintain building fund accounts, as provided for by the FECA. Second, the rules would allow national party committees other than the Senate and House campaign committees to maintain a second nonfederal account to be used exclusively for the purpose of supporting nonfederal candidates. This support could only take the form of direct donations to nonfederal candidates, or direct disbursements solely for the purpose of expressly advocating the election or defeat of clearly identified nonfederal candidates.

These changes would be incorporated into sections 102.5, 106.5 and 106.1. A new paragraph (c) entitled "permissible national party committee nonfederal accounts" would be added to section 102.5 to limit the national party committees, including the Senate and House campaign committees, to the building fund accounts and nonfederal candidate support accounts referred to above. Paragraph (c)(2) would describe these accounts in detail.

Under paragraph (c)(2)(i), national party committees, including the Senate and House campaign committees of a national party, could establish a building fund account to be used exclusively for the purpose of receiving gifts, subscriptions, loans, advances or deposits of money or anything of value described in 11 CFR 100.7(b)(12) or 11 CFR 100.8(b)(13).

Under paragraph (c)(2)(ii), national party committees other than the Senate and House campaign committees could establish nonfederal accounts to make direct donations to candidates for nonfederal office (see paragraph (c)(2)(ii)(A)), or to make direct disbursements on behalf of candidates for nonfederal office (see paragraph (c)(2)(ii)(B)). Funds spent from this account must be either directly donated to or directly disbursed on behalf of specific nonfederal candidates. They may not pass through any state or local party committee. This

ensures that these disbursements are not de facto transfers to a state or local party committee. Direct disbursements on behalf of candidates for nonfederal office are disbursements that expressly advocate the election or defeat of a nonfederal candidate, whether or not they are coordinated with the candidate. Paragraph (c)(2)(ii)(B)(1). In addition, these disbursements may not make reference to any federal candidate or officeholder. Paragraph (c)(2)(ii)(B)(2).

The draft final rules would make related changes to section 106.1.[13] Draft section 106.1(a) contains the rules applicable to national party committees, including the senate and house campaign committees. Under paragraph (a)(1), expenditures made by a national party committee on behalf of more than one clearly identified federal candidate, and payments by a national party committee that involve both expenditures on behalf of one or more clearly identified federal candidates and disbursements on behalf of one or more clearly identified nonfederal candidates, must be made entirely from the committee's federal account(s), i.e., with funds subject to the prohibitions and limitations of the Act. This would include the costs of fundraising programs conducted on behalf of a combination of federal and nonfederal candidates.

Section 106.1(a) would apply to all of the national party committees, including the Senate and House campaign committees. With regard to attribution of expenditures and disbursements to specific candidates, the national committees would continue to attribute the respective portions of these expenses to the various candidates according to the benefit reasonably expected to be derived. Paragraph (a)(1)(ii). For disbursements that benefit a nonfederal candidate, the committees would identify the candidate in their reports by including a the candidate's name in a memo entry on their schedule of itemized disbursements.

The draft rules would also make related changes to those portions of section 106.5 that apply to the national party committees. The section's heading would be revised to reflect its operative provisions. Paragraph (a)(1) would be renumbered as paragraph (a) and its description of the scope of section 106.5 would be modified slightly, also to reflect the section's operative provisions. Finally, paragraphs (b) and (c) of the current rules would be replaced by a new paragraph (b). Paragraph (b) would require national party committees, including the Senate and House campaign committees, to defray their expenses entirely from hard dollars, subject to exceptions for the building fund and nonfederal candidate support accounts described above. This would include the costs of combined federal and non-federal fundraising programs currently allocated using the funds received method in section 106.5(f). It would also include costs incurred in fundraising for the committees' building funds and nonfederal candidate support funds, in order to ensure that fundraising for these funds does not become an avenue for spending soft money to influence federal elections, such as by soliciting donations with communications that expressly advocate the election or defeat of federal candidates.

[13] In addition to the substantive changes made relating to national party committees, section 106.1 has been completely reorganized for the purposes of clarification. However, those aspects of the current rule that are applicable to state and local party committees, separated segregated funds, and nonconnected committees have been preserved. Thus, we intend no substantive change in the application of section 106.1 to these entities.

B. State and local party committees

The draft final rules make no substantive changes to the allocation rules for state and local party committee rules. However, the rules contain several conforming amendments. The introductory language of section 102.5(a) and the language of paragraph (a)(1) of that section have been revised to exclude national party committees, since, under the draft final rules, national party committees would no longer be able to establish separate federal and nonfederal accounts other than those described in section 102.5(c).

As indicated above, section 106.1 has been reorganized. The provisions of current section 106.5 that remain applicable to state and local party committees have been collected in section 106.5(b) of the draft final rules. No substantive change is intended in this reorganization.

Similarly, the draft final rules would reorganize some aspects of section 106.5 relating to state and local party committees. The descriptions of the four categories of allocable activities in current paragraph (a)(2) would be moved to paragraph (c)(2), and new paragraph (c)(1) would state the general rule that state and local party committees must allocate the costs of these activities in accordance with paragraphs (d) through (f).[14] In addition, all references to paragraph (a)(2) in paragraphs (d) through (f) would be replaced with citations to (c)(2). Finally, the heading of paragraph (f) would be revised to indicate that it applies only to state and local party committees.

The draft final rules would clarify current paragraphs (a)(2)(ii) and (a)(2)(iv) to address allegations made by some of the commenters that the rules allow party committees to transfer funds to nonprofit organizations in order to avoid the allocation requirements. The revised versions, numbered (c)(2)(ii) and (c)(2)(iv), would clarify that state and local party committees must allocate the costs of fundraising activities and generic voter drives, whether the party committee conducts the drive itself or in conjunction with another entity. See Federal Election Commission v. California Democratic Party, No. S-97-0891, (E.D. Cal. October 13, 1999).

C. Party committee solicitations by federal candidates and officeholders

The draft final rules would also amend section 102.5(a)(3) and add section 102.5(c)(3) to make it clear that when a federal candidate or officeholder solicits contributions on behalf of a party committee, the resulting contributions are subject to the prohibitions and limitations of the Act. However, in the case of a solicitation for a national party committee, this presumption could be rebutted if the donor expressly designates the donation for an otherwise permissible nonfederal account, i.e., a building fund account or nonfederal candidate support account described in section 102.5(c)(2). See section

[14] Current paragraph (c) relates to the Senate and House campaign committees. Under the draft final rules, these entities would be covered by paragraph (b). The current version of paragraph (c) would be completely replaced with provisions applicable to state and local party committees.

102.5(c)(3). In the case of a solicitation for a state party committee, this presumption could be rebutted if the donor expressly designates the donation for the committee's building fund account, or for another nonfederal account described in section 102.5(a)(1)(i). See section 102.5(a)(3). Donors to a local party committee could also designate their contributions for a nonfederal account.

The draft final rules also contain a conforming amendment to current section 102.5(a)(2), which would add to the list of contributions that may be deposited in a federal account those contributions that, due to the operation of paragraphs (a)(3), would be presumed to be for the purpose of influencing an election.

VI. RECOMMENDATIONS

The Office of General Counsel recommends that the Commission take the following actions:

1. Approve the draft final rules set out below.

2. Direct the Office of General Counsel to prepare a draft Explanation and Justification for the final rules, and submit that document to the Commission for its review.

VII. DRAFT FINAL RULES[15]

PART 102 -- REGISTRATION, ORGANIZATION, AND RECORDKEEPING BY POLITICAL COMMITTEES (2 U.S.C. 433)

1. The authority citation for part 102 continues to read as follows:

Authority: 2 U.S.C. 432, 433, 438(a)(8), 441d.

2. Section 102.5 is amended by revising paragraph (a) heading, paragraph (a)(1) introductory text, paragraphs (a)(2) and (a)(3), and by adding paragraph (c), to read as follows:

[15] The NPRM sought comments on proposed changes to section 103.3 of the current rules. The Office of General Counsel now believes it would be more appropriate to address these proposals in another rulemaking. If the Commission approves the draft final rules set out below, the Explanation and Justification will indicate that the Commission will consider the proposed changes to section 103.3 at a later date.

§ 102.5 Organizations financing political activity in connection with Federal and non-Federal elections, other than through transfers and joint fundraisers.

(a) Organizations, other than national party committees, that are political committees under the Act.

(1) Except as provided in paragraph (c) of this section, any organization that finances political activity in connection with both federal and nonfederal elections and that qualifies as a political committee under 11 CFR 100.5 shall either:

* * * * *

(2) Permissible deposits. Only contributions described in paragraphs (a)(2)(i), (ii), (iii) or (iv) of this section may be deposited in a federal account established under paragraph (a)(1)(i) of this section or may be received by a political committee established under paragraph (a)(1)(ii) of this section:

(i) Contributions designated for the federal account;

(ii) Contributions that result from a solicitation which expressly states that the contribution will be used in connection with a federal election;

(iii) Contributions from contributors who are informed that all contributions are subject to the prohibitions and limitations of the Act; or

(iv) Contributions that, due to the operation of paragraph (a)(3) of this section, are presumed to be for the purpose of influencing a federal election.

(3) Solicitations by federal candidates and officeholders. A state or local party committee solicitation that is made by a federal candidate or federal officeholder or that makes reference to a federal candidate or a federal election shall be presumed to be for the purpose of influencing a federal election. The full amount of any funds received as a result of that solicitation shall be presumed to be a contribution under 11 CFR 100.7(a) that is subject to the prohibitions and limitations in 11 CFR parts 110 and 114. However, this paragraph does not apply to a donation that is expressly designated for an otherwise permissible nonfederal account, or for a state party building fund account described in 11 CFR 100.7(b)(12) or 11 CFR 100.8(b)(13).

* * * * *

(c) National party committees.

(1) General rule. National party committees, including the Senate and House campaign committees of a national party, shall establish one or more federal account(s) in accordance with 11 CFR part 103. The federal account(s) shall receive only contributions subject to the prohibitions and limitations of the Act. Except as provided in paragraph (c)(2) of this section, national party committees, including the Senate and House campaign committees of a national party, shall not establish any nonfederal account or receive any contribution or donation of anything of value that is not subject to the prohibitions and limitations of the Act.

(2) Building funds; other permissible national party committee nonfederal accounts.

(i) National party committees, including the Senate and House campaign committees of a national party, may establish a building fund account to be used exclusively for the purpose of receiving gifts, subscriptions, loans, advances or deposits of money or anything of value described in 11 CFR 100.7(b)(12) or 11 CFR 100.8(b)(13).

(ii) National party committees, other than the Senate and House campaign committees of a national party, may establish one or more nonfederal accounts to be used exclusively for the following purposes:

(A) To make direct donations to candidate(s) for nonfederal office that are not made through a state or local party committee;

(B) To make direct disbursements on behalf of candidate(s) for nonfederal office. Direct disbursements on behalf of candidate(s) for nonfederal office are disbursements:

(1) Expressly advocating the election or defeat of one or more clearly identified candidate(s) for nonfederal office, whether or not they are made in cooperation or consultation with, in concert with, or at the request or suggestion of, any nonfederal candidate;

(2) That make no reference to any federal candidate or officeholder; and

(3) That are not made through a state or local party committee.

(3) Solicitations by federal candidates and officeholders. A national party committee solicitation that is made by a federal candidate or federal officeholder or that makes reference to a federal candidate or a federal election shall be presumed to be for the purpose of influencing a federal election. The full amount of any funds received as a result of that solicitation shall be presumed to be a contribution under 11 CFR 100.7(a) that is subject to the prohibitions and limitations in 11 CFR parts 110 and 114. However, this paragraph does not apply to a donation that is expressly designated for a nonfederal account described in paragraph (c)(2) of this section.

PART 106 -- ALLOCATIONS OF CANDIDATE AND COMMITTEE ACTIVITIES

3. The authority citation for part 106 continues to read as follows:

Authority: 2 U.S.C. 438(a)(8), 441a(b), 441a(g)

4. Section 106.1 is revised to read as follows:

§ 106.1 Allocation of expenses between candidates.

(a) National party committees, including the Senate and House campaign committees of the national party committees.

(1) General rule. Expenditures, including in-kind contributions, independent expenditures and coordinated expenditures, made by a national party committee on behalf of more than one clearly identified federal candidate, and payments by a national party committee that involve both expenditures on

behalf of one or more clearly identified federal candidates and disbursements on behalf of one or more clearly identified nonfederal candidates, shall be:

(i) Made entirely from the committee's federal account(s), i.e., with funds subject to the prohibitions and limitations of the Act; and

(ii) Except as provided in paragraphs (a)(1)(ii)(A) and (B) of this section, attributed to each such candidate according to the benefit reasonably expected to be derived,. For example, in the case of a publication or broadcast communication, the attribution shall be determined by the proportion of space or time devoted to each candidate as compared to the total space or time devoted to all candidates. In the case of a fundraising program or event where funds are collected by one committee for more than one clearly identified candidate, the attribution shall be determined by the proportion of funds received by each candidate as compared to the total receipts by all candidates.

(A) Expenditures for rent, personnel, overhead, general administrative, fund-raising, and other day-to-day costs of political committees need not be attributed to individual candidates, unless these expenditures are made on behalf of a clearly identified candidate and the expenditure can be directly attributed to that candidate; and

(B) Expenditures for educational campaign seminars, for training of campaign workers, and for registration or get-out-the-vote drives of committees need not be attributed to individual

candidates unless these expenditures are made on behalf of a clearly identified candidate, and the expenditure can be directly attributed to that candidate.

(2) Reporting. Expenditures and other disbursements made by a national party committee on behalf of more than one clearly identified candidate shall be reported pursuant to 11 CFR 104.10(a). An authorized expenditure made by a candidate or political committee on behalf of another candidate shall be reported as a contribution in-kind to the candidate on whose behalf the expenditure was made, except that expenditures made by party committees pursuant to 11 CFR 110.7 need only be reported as an expenditure.

(b) State and local party committees.

(1) General rule. Expenditures, including in-kind contributions, independent expenditures, and coordinated expenditures made on behalf of more than one clearly identified federal candidate shall be attributed to each such candidate according to the benefit reasonably expected to be derived. For example, in the case of a publication or broadcast communication, the attribution shall be determined by the proportion of space or time devoted to each candidate as compared to the total space or time devoted to all candidates. In the case of a fundraising program or event where funds are collected by one committee for more than one clearly identified candidate, the attribution shall be determined by the proportion of funds received by each candidate as compared to the total receipts by all candidates.

(2) Allocation between federal and nonfederal candidates.

(i) Except as provided in paragraph (b)(2)(ii) of this section, the methods described in paragraph (b)(1) of this section shall also be used to allocate payments involving both expenditures on behalf of one or more clearly identified federal candidates and disbursements on behalf of one or more clearly identified nonfederal candidates. When such a payment is made by a political committee with separate federal and nonfederal accounts, the payment shall be made according to the procedures set forth in 11 CFR 106.5(g).

(ii) State and local party committees that make disbursements for administrative expenses, fundraising, or generic voter drives in connection with both federal and nonfederal elections shall allocate their expenses in accordance with § 106.5. For the purposes of this section:

(A) Expenditures for rent, personnel, overhead, general administrative, fund-raising, and other day-to-day costs of political committees need not be attributed to individual candidates, unless these expenditures are made on behalf of a clearly identified candidate and the expenditure can be directly attributed to that candidate.

(B) Expenditures for educational campaign seminars, for training of campaign workers, and for registration or get-out-the-vote drives of committees need not be attributed to individual

candidates unless these expenditures are made on behalf of a clearly identified candidate, and the expenditure can be directly attributed to that candidate.

(C) Payments made for the cost of certain voter registration and get-out-the-vote activities conducted by State or local party organizations on behalf of any Presidential or Vice-Presidential candidate(s) are exempt from the definition of a contribution or an expenditure under 11 CFR 100.7(b)(17) and 100.8(b)(18). If the State or local party organization includes references to any candidate(s) seeking nomination or election to the House of Representatives or Senate of the United States the portion of the cost of such activities allocable to such candidate(s) shall be considered a contribution to or an expenditure on behalf of such candidate(s), unless such reference is incidental to the overall activity. If such reference is incidental to the overall activity, such costs shall not be considered a contribution to or expenditure on behalf of any candidate(s).

(3) Reporting. An expenditure made by a state or local party committee on behalf of more than one clearly identified federal candidate shall be reported pursuant to 11 CFR 104.10(a). A payment that also includes amounts attributable to one or more nonfederal candidates, and that is made by a state or local party committee with separate federal and nonfederal accounts, shall be made according to the procedures set for in 11 CFR 106.5(g), and shall also be

reported pursuant to 11 CFR 104.10(a). An authorized expenditure made by a candidate or political committee on behalf of another candidate shall be reported as a contribution in-kind to the candidate on whose behalf the expenditure was made, except that expenditures made by party committees pursuant to 11 CFR 110.7 need only be reported as an expenditure.

(c) Separate segregated funds and non-connected committees.

(1) General rule. Expenditures, including in-kind contributions and independent expenditures, made by a separate segregated fund or non-connected committee on behalf of more than one clearly identified federal candidate shall be attributed to each such candidate according to the benefit reasonably expected to be derived. For example, in the case of a publication or broadcast communication, the attribution shall be determined by the proportion of space or time devoted to each candidate as compared to the total space or time devoted to all candidates. In the case of a fundraising program or event where funds are collected by one committee for more than one clearly identified candidate, the attribution shall be determined by the proportion of funds received by each candidate as compared to the total receipts by all candidates.

(2) Allocation between federal and nonfederal candidates.

(i) Except as provided in paragraph (c)(2)(ii) of this section, the methods described in paragraph (c)(1) of this section shall also be used by a separate segregated fund or non-connected committee to allocate payments involving both expenditures on behalf of one or more clearly

identified federal candidates and disbursements on behalf of one or more clearly identified nonfederal candidates.

(ii) Separate segregated funds and nonconnected committees that make disbursements for administrative expenses, fundraising, or generic voter drives in connection with both federal and nonfederal elections shall allocate their expenses in accordance with § 106.6. For the purposes of this section:

(A) Expenditures by a separate segregated fund or non-connected committee for rent, personnel, overhead, general administrative, fund-raising, and other day-to-day costs of political committees need not be attributed to individual candidates, unless these expenditures are made on behalf of a clearly identified candidate and the expenditure can be directly attributed to that candidate; and

(B) Expenditures by a separate segregated fund or non-connected committee for educational campaign seminars, for training of campaign workers, and for registration or get-out-the-vote drives of committees need not be attributed to individual candidates unless these expenditures are made on behalf of a clearly identified candidate, and the expenditure can be directly attributed to that candidate.

(3) Reporting. An expenditure made by a separate segregated fund or non-connected committee on behalf of more than one clearly identified federal

candidate shall be reported pursuant to 11 CFR 104.10(a). A payment that also includes amounts attributable to one or more nonfederal candidates, and that is made by a separate segregated fund or nonconnected committee with separate federal and nonfederal accounts, shall be made according to the procedures set forth in 106.6(e), as appropriate, but shall be reported pursuant to 11 CFR 104.10(a).

(d) Definitions. For purposes of this section --

(1) National party committee includes the Senate and House campaign committees of the national party committees.

(2) Clearly identified shall have the same meaning as set forth at 11 CFR 100.17.

5. Section 106.5 is amended by revising the section heading, paragraph (a), (b), (c), (d)(1), the first sentence of paragraph (e), the heading of paragraph (f), and the first sentence of paragraph (f)(1), to read as follows:

§ 106.5 Party committee federal and nonfederal activities; payments by national party committees; allocation by state and local party committees.

(a) General rules. Party committees that make disbursements in connection with federal and nonfederal elections shall make those disbursements entirely from funds subject to the prohibitions and limitations of the Act, or from accounts established pursuant to 11 CFR 102.5. Political committees that have established separate federal and nonfederal accounts under 11 CFR 102.5(a)(1)(i) shall allocate expenses between those accounts according to this section. Organizations that are not political committees but have established separate federal and nonfederal accounts under 11 CFR 102.5(b)(1)(i), or that make federal and nonfederal disbursements from a single account under 11 CFR 102.5(b)(1)(ii) shall also allocate their

federal and nonfederal expenses according to this section. This section covers (i) general rules regarding allocation of federal and nonfederal expenses by party committees, (ii) methods for allocation of administrative expenses, costs of generic voter drives, exempt activities, and fundraising costs by state and local party committees, and (iii) procedures for payment of allocable expenses. Requirements for reporting of allocated disbursements are set forth in 11 CFR 104.10.

(b) National party committees.

(1) Except as provided in paragraph (b)(2) and (b)(3) of this section, national party committees, including the Senate and House campaign committees of a national party, shall defray their expenses entirely from funds subject to the prohibitions and limitations of the Act.

(2) National party committees, including the Senate and House campaign committees of a national party, may defray the expenses described in 11 CFR 100.7(b)(12) and 11 CFR 100.8(b)(13) with funds from an account established in accordance with 11 CFR 102.5(c)(2)(i).

(3) National party committees, other than the Senate and House campaign committees of a national party, may make direct donations to candidate(s) for nonfederal office, and direct disbursements on behalf of candidate(s) for nonfederal office, in accordance with 11 CFR 102.5(c)(ii).

(c) State and local party committees; general rule.

(1) General rule. State and local party committees shall allocate the costs described in paragraph (c)(2) of this section in accordance with paragraphs (d) through (f) of this section.

(2) Costs to be allocated. Committees that make disbursements in connection with federal and nonfederal elections shall allocate expenses according to this section for the following categories of activity:

(i) Administrative expenses including rent, utilities, office supplies, and salaries, except for such expenses directly attributable to a clearly identified candidate;

(ii) The direct costs of a fundraising program or event, including disbursements for solicitation of funds and for planning and administration of actual fundraising events, through which a committee collects both federal and nonfederal funds, whether the committee conducts the program or event individually or in conjunction with another committee;

(iii) State and local party activities exempt from the definitions of contribution and expenditure under 11 CFR 100.7(b) (9), (15) or (17), and 100.8(b) (10), (16) or (18) (exempt activities) including the production and distribution of slate cards and sample ballots, campaign materials distributed by volunteers, and voter registration and get-out-the-vote drives on behalf of the party's presidential and vice-

presidential nominees, where such activities are conducted in conjunction with nonfederal election activities; and

(iv) Generic voter drives either conducted by the committee itself or paid for by the committee and conducted by another entity, including voter identification, voter registration, and get-out-the-vote drives, or any other activities that urge the general public to register, vote or support candidates of a particular party or associated with a particular issue, without mentioning a specific candidate.

(d) * * *

(1) General rule. All state and local party committees except those covered by paragraph (d)(2) of this section shall allocate their administrative expenses and costs of generic voter drives, as described in paragraph (c)(2) of this section, according to the ballot composition method, described in paragraphs (d)(1)(i) and (ii) of this section as follows:

* * * * *

(e) State and local party committees; method for allocating costs of exempt activities. Each state or local party committee shall allocate its expenses for activities exempt from the definitions of contribution and expenditure under 11 CFR 100.7(b) (9), (15) or (17), and 100.8(b) (10), (16) or (18), when conducted in conjunction with nonfederal election activities, as described in paragraph (c)(2) of this section, according to the proportion of time or space devoted in a communication. * * *

(f) State and local party committees; method for allocating direct costs of fundraising.

(1) If federal and nonfederal funds are collected by one committee through a joint activity, that committee shall allocate its direct costs of fundraising, as described in paragraph (c)(2) of this section, according to the funds received method. * * *

* * * * *