FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

October 23, 2012

SENSITIVE

MEMORANDUM

TO: The Commission

FROM: Lisa J. Stevenson LJS
Deputy General Counsel - Law

Lorenzo Holloway LH/lp
Assistant General Counsel
For Public Finance and Audit Advice

Margaret J. Forman MJF
Attorney

SUBJECT: Request for Consideration of a Legal Question (LRA 917)

I. INTRODUCTION

On September 28, 2012, the Commission received a Request for Consideration of a Legal Question ("Request") from counsel on behalf of eight state party committees that the Commission voted to audit pursuant to 2 U.S.C. § 438(b).[1] Attachment.

The Request addresses a proposed audit finding for each of the Committees pertaining to the requirement in 11 C.F.R. § 106.7(d)(1) that state party committees maintain monthly payroll logs of the percentage of time each employee spends in connection with a federal election. The issue presented in the Request is whether the monthly time log requirement applies to employees

[1] The eight committees are: the Mississippi Democratic Party PAC, the Massachusetts Democratic State Committee – Fed. Fund, the State Democratic Executive Committee of Alabama, the Nebraska Democratic Party, the Vermont Democratic Party, the South Dakota Democratic Party, the Democratic Party of South Carolina, and the [redacted]. At least two Commissioners agreed to consider this Request pursuant to the Policy Statement Regarding a Program for Requesting Consideration of Legal Questions by the Commission, 76 *Fed. Reg.* 45798-45799 (Aug. 1 2011).

The Commission's action on this Request affects a total of 13 state party committees. The Commission has also received another request regarding this issue, which will be addressed in a separate memorandum from the Office of General Counsel.

who are paid with 100% federal funds. We conclude that under the literal language of the regulation, it does. But there is a separate question, as a prudential matter, of whether the Commission wishes to pursue recordkeeping findings in these circumstances. Where employees are paid with 100% federal funds, the soft money concerns underlying the regulations are absent. The only significance a log could have in these circumstances is verifying whether the disclosure of disbursements is on the correct line on the Detailed Summary Page of a committee's disclosure reports. The Audit Division submits that it needs the logs for this purpose and a recordkeeping finding is appropriate. Whether the Commission believes this purpose is sufficiently important to require a recordkeeping finding where no logs (or affidavits) are available is a matter of policy for the Commission to determine.

II. COMMITTEES ARE REQUIRED TO KEEP MONTHLY LOGS FOR EMPLOYEES PAID EXCLUSIVELY WITH FEDERAL FUNDS

A state party committee "must keep a monthly log of the percentage of time each employee spends in connection with a Federal election." 11 C.F.R. § 106.7(d)(1). To determine if a state party committee must allocate the salary, wages, and benefits of its employees, it must examine the percentage of time that its employees spent on federal election activity ("FEA") or activity in connection with federal elections. Salaries and benefits for employees who spend more than 25% of their compensated time on FEA or activities in connection with a federal election in a given month must be paid only from a federal account. 2 U.S.C. § 431(20)(A)(iv); 11 C.F.R. § 106.7(d)(1)(ii); *see* 2 U.S.C. § 441i(b)(2). Employees who spend less than 25% of their time on FEA or activities in connection with a federal election may be allocated as administrative costs or paid from the federal account. 11 C.F.R. § 106.7(d)(1)(i). Employees who spend none of their compensated time on FEA or activities in connection with a federal election may be paid entirely with funds that comply with state law. 11 C.F.R. §§106.7(c)(1) and 106.7(d)(1)(iii). The Committees concede that failure to keep logs for employees "who were paid either in part or with no federal funds would support a recordkeeping finding." Attachment at 2. The Committees, however, object to "any finding that employees who were paid exclusively with federal funds required any entry in a time log." *Id.*

We conclude that, read literally, the regulations support the conclusion that state party committees must maintain a monthly log under 11 C.F.R. § 106.7(d)(1) for all employees, including those paid from and reported as solely 100% federal funds. Although 100% of the time spent on federal activity represents the whole or complete time spent on federal activity, this is still a percentage and therefore must be documented.

We understand the Committees' concern about the necessity for a log when employees are paid with 100% of federal funds. Section 106.7(d) supports the statute's requirement that state and local party committees treat as "federal election activity," payable with 100% federal funds, the salaries and benefits of any employee who spends more than 25% of his or her compensated time during the month on activities in connection with a federal election. 2 U.S.C. §§ 431(20)(A)(iv), 441i(b)(1). Where employees are paid with 100% federal funds, there is by definition no concern

that an inadequate share of federal funds was used to pay these employees.[2] Thus, the Committees might question why the Audit Division would inquire about time logs in this situation and, in the absence of such logs, impose a recordkeeping finding

The additional purpose served by the logs is to differentiate salary and benefits payments that qualify as FEA – which are reported on line 30(b) of the Detailed Summary Page – from payments to employees who spent less than 25% of their compensated time during a month on activities in connection with a federal election, but whose salaries and benefits the Committee voluntarily chose to pay with 100% federal funds. Payments in this latter category should be reported as federal operating expenses on line 21(b) of the Detailed Summary Page, not as FEA. *See* 11 C.F.R. §§ 104.14(b)(1), 104.17(a)(4). In these audits, it appears that many of the Committees recognized this distinction because a number of the Committees reported payroll payments as other federal operating expenditures on Schedule B, line 21b. The Audit Division submits that it needs the logs to verify that the salary and benefit payments at issue have been disclosed on the correct lines of the Detailed Summary Page. *See* 11.CF.R. § 104.14(b)(1).

In support of their assertion that a log is not required for employees that are paid with 100% federal funds, the Committees cite a proposed regulation which was never promulgated, which provided: "Committees must keep time records for all employees for purposes of determining the percentage of time spent on activities in connection with a Federal election." *Prohibited and Excessive Contributions; Non-Federal Funds or Soft Money*, 67 *Fed. Reg.* 35654, 35684 (May 20, 2002) (Proposed section 300.33(b)(1)). The Committees apparently assert that the fact that the Commission (1) moved the recordkeeping requirement from proposed section 300.33 to section 106.7; and (2) changed the words "all employees" in the proposed provision to "each employee," in 11 C.F.R. § 106.7(d)(1), signifies that the monthly log requirement excludes employees paid with 100% federal funds.[3]

There is no indication in the regulatory history that the Commission moved this proposed provision into section 106.7 and changed the language because it intended to exclude employees

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[2] We recognize the Commission's 3-3 split on a similar issue in the Georgia Federal Elections Committee audit involving employees whom the committee asserted spent *no* time on activity in connection with federal elections. In that audit, the Commission split on the issue of whether the Commission could require a committee to keep a log for such employees. In a motion that failed 3-3, three Commissioners asserted that "the Commission does not have jurisdiction to impose recordkeeping and documentation requirements on employee activity that a State party committee claims is solely non-Federal." *See* Commission Agenda Document No. 11-10-B (Motion on Audit Division Recommendation memorandum on the Georgia Federal Elections Committee, *considered in Open Session* Mar. 3, 2011). Here, unlike with the Georgia Federal Elections Committee, a number of the employees of each of the Committees may have spent 100%, or some part thereof, of their time on activities in connection with a federal election and were paid with 100% federal funds, so the three Commissioners' concerns regarding jurisdiction over "solely non-federal" activity may be reduced.

[3] In their Request, the Committees appear to assert that section 106.7 applies to the allocation of expenses, and not to Federal Election Activities (FEA). We reiterate that section 106.7 supports the statute's requirement that state and local party committees treat as "federal election activity," payable with 100% federal funds, the salaries and benefits of any employee who spends more than 25% of his or her compensated time during the month on activities in connection with a federal election. 2 U.S.C. §§ 431(20)(A)(iv), 441i(b)(1).

paid with 100% federal funds. Rather, as the Commission explained, the proposed regulation at 300.33(b)(1) would have required state party committees to keep detailed time records for all employees to provide documentation for allocation purposes. *Prohibited and Excessive Contributions: Non-Federal Funds or Soft Money*, 67 *Fed. Reg.* 49064, 49078 (Jul. 29, 2002). The Commission rejected the original proposed provision because it chose not to allocate employee salary, noting "in response to the NPRM, a State party committee asserted that time sheets would be 'burdensome,' that written certifications by employees would be 'equally impractical,' but that a tally sheet kept by the employer would be 'more reasonable.' The same commenter nonetheless urged the Commission not to require any particular method of documentation." *Id.* The Commission, acknowledging the reasons provided by the commenters, decided to "require[] only that a monthly log be kept of the percentage of time each employee spends in connection with a Federal election." *Id.* Thus, the Commission chose a recordkeeping requirement in the form of a monthly log as a lesser burden than the detailed time records as part of an allocation formula.

Nothing in the Commission's explanation for this requirement indicates that the Commission's change in the location of the recordkeeping requirement or change from the plural "all employees" to the singular "each employee" excludes employees paid with 100% federal funds. To the contrary, the subparagraphs of the regulatory provision imposing a monthly log requirement anticipate three allocation scenarios – paid with 100% federal funds under (d)(1)(i) or (ii), allocation between federal and non-federal under (d)(1)(i), and paid with 100% state funds under (d)(1)(iii). The Committees fail to explain how the language of the regulation, or its drafting history, supports imposing a monthly log requirement in the latter two scenarios but somehow excludes the first scenario where employees are paid with 100% federal funds.

The Committees also assert that the proposed finding is inconsistent with the Commission's approach in prior audits in other election cycles.[4] The Committee cites the 2006 audit of the Georgia Federal Elections Committee, and the 2006 Audit of the Tennessee Republican Party Federal Election Account as examples of audits where no recordkeeping finding was addressed for failure to maintain a log pursuant to section 106.7(d)(1). The Committees are correct about the findings in those prior audits – the Commission did not pursue a separate recordkeeping finding under section 106.7(d)(1), regardless of whether those committees maintained the logs.[5]

[redacted]

[4] The Committees suggests that the Commission should provide the regulated community with advance notice of its decision to apply the requirements of 11 C.F.R. § 106.7(d)(1) to employees paid with 100% federal funds. We do not believe there is a notice issue because nothing in section 106.7(d)(1) addresses a different category of employees for which committees would not be required to keep a log.

[5] In the audit of the Georgia Federal Elections Committee, the Commission split on whether that committee was required to keep a log. *See supra* note 2.

[redacted]

The Commission, as an administrative agency charged with administering the Federal Election Campaign Act, has discretion in deciding which matters of non-compliance will be findings in its audit reports. *Cf. Nader v. FEC*, 823 F. Supp. 2d 53, 65 (D.D.C. 2011); *Akins v. FEC*, 736 F. Supp. 2d 9, 21 (D.D.C. 2010) ("The FEC has broad discretionary power in determining whether to investigate a claim, and whether to pursue civil enforcement under the [FECA]."); *see also Heckler v. Chaney*, 470 U.S. 821, 831 (1985).

III. RECOMMENDATION

The Office of the General Counsel recommends that the Commission conclude that 11 C.F.R. § 106.7(d)(1) requires the Committees to keep a monthly log for employees paid exclusively with federal funds.

Attachment

Request for Legal Consideration from Neil Reiff, as counsel representing the Mississippi Democratic Party PAC, the Massachusetts Democratic State Committee – Fed. Fund, the State Democratic Executive Committee of Alabama, the Nebraska Democratic Party, the Vermont Democratic Party, the South Dakota Democratic Party, the Democratic Party of South Carolina, and [redacted].

SANDLER, REIFF, YOUNG & LAMB, P.C.

September 28, 2012

Shawn Woodhead Worth
Secretary
Federal Election Commission
999 E Street, NW
Washington, DC 20463

Dear Ms. Worth:

The undersigned serves as counsel to the following Democratic State Party Committees:

Mississippi Democratic Party PAC
Massachusetts Democratic State Committee – Fed. Fund
State Democratic Executive Committee of Alabama
Nebraska Democratic Party
Vermont Democratic Party
South Dakota Democratic Party
Democratic Party of South Carolina
[redacted]

This letter serves as a request for consideration of a legal question raised during each of the Audits of the above referenced committees for the 2010 election cycle. This request is being made in accordance with the FEC's recent Policy Statement, Notice 2011-11, Policy Statement Regarding a Program for Requesting Consideration of Legal Questions by the Commission, 76 *Fed. Reg.* 45798 (August 1, 2011). Our office received notification of this proposed finding, via conference call, on September 10, 2012.

Specifically, during this call, our office was notified by the Audit Division that it intended to include, as a finding in the Interim Audit Report for each Audit that the committee failed to comply with Commission recordkeeping requirements by failing to maintain employee time logs for those employees who were paid exclusively with federal funds. It is my understanding that all of the above referenced committees would be affected by this proposed finding. Our clients disagree with this proposed finding as a "novel" approach to this issue" and "inconsistent with prior Commission matters dealing with the same issue" 76 *Fed. Reg.* at 45799.

During the fieldwork and the Exit Conference for each of these committees, the Audit Division raised the issue of time logs and suggested that, according to 11 C.F.R. § 106.7(d)(1),

logs must be kept for all employees percentage of time spent on federal activity regardless of whether they were paid all, in part, or with no federal funds. During the fieldwork, each committee conceded that the failure to keep logs for employees who were paid either in part or with no federal funds would support a recordkeeping finding. However, each committee objected to any finding that employees who were paid exclusively with federal funds required any entry in a time log.[1]

DISCUSSION

Commission regulations at 11 C.F.R. § 106.7(d)(1) require that party committees "keep a monthly log of the percentage of time each employee spends in connection with a Federal election." Contrary to the proposed regulation that preceded the final regulation, the final regulation does not appear to specify that such a log be kept for all employees.

The proposed regulation at proposed 11 C.F.R. § 300.33(b)(1) stated: "Committees must keep time records for all employees for purposes of determining the percentage of time spent on activities in connection with a Federal Election." Notice of Proposed Rulemaking, *Prohibited and Excessive Contributions: Non-Federal Funds or Soft Money*, 97 Fed. Reg. 35654, 35684 (May 20, 2002) (emphasis added).

Although the Commission left provisions regarding the allocation of salary in the final section 300.33, it also created a new section of the regulations, 11 C.F.R. § 106.7, to address all issues relating to the allocation of expenses between federal and non-federal activities by state and local party committees. In doing so, it moved the recordkeeping requirement, in its entirety from proposed section 300.33 to section 106.7. The shift of this language from section 300.33 which relates to Federal Election Activities, to section 106.7, which deals exclusively with the allocation of expenses is significant. In our view, this shift signifies that the Commission believed that the recordkeeping requirement related solely to issues relating to the use of non-federal funds and did not intend to create a universal, burdensome recordkeeping requirement for all employees.

More significantly, the Commission changed the language of the proposed regulation and specifically deleted the word "all" from the proposed version of the regulation. This clearly shows the intent of the Commission to not require time records for all employees but only for those covered by 11 C.F.R. § 106.7, which would include only those employees that the party was claiming to pay either entirely non-federal funds or with a combination of federal and non-federal funds.

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[1] Notwithstanding this concession, it should be noted that prior to the 2010 election cycle, it is my understanding that the committees were permitted to demonstrate during the audit process that employees did not exceed the 25% threshold by providing affidavits where inadequate records were maintained. Provision of these affidavits would negate a potential finding that the committee potentially over-funded its federal account from its non-federal account. Once these affidavits were adequately provided, and the over-funding issue resolved, the Commission did not pursue any separate recordkeeping finding for employee time log recordkeeping. Although the Audit Division continues to allow affidavits to be provided to resolve over-funding issues, to the extent that providing for a separate recordkeeping finding under any circumstances where the committee provides subsequent, acceptable documentation during the audit process appears to be inconsistent with past practice in Commission audits.

To be sure, there is no reason, as a matter of policy, to make a finding that state party committees have violated Commission recordkeeping requirements by requiring time sheets that serve no purpose. When queried by our office during the teleconference call as to the reason such documentation should be kept, the Audit Division replied that such time sheets would help track state party allocation transfers for payroll, by employee. However, the Commission already has access to sufficient information from committee payroll and other financial records, as well as the actual reports filed by the committee which show whether that the employee's payroll was intended to be paid for exclusively with federal funds. Adding a time log requirement for such employees serves absolutely no additional purpose other than to increase the recordkeeping requirements of state parties. In fact, it is my understanding that several state partics have chosen to not allocate their payroll costs because they find the time recordation requirements to be too burdensome.

We also find it troubling that the Audit Division has chosen to include this finding in an Audit Report with respect to a regulation that the Commission has addressed in the Audit context on several occasions in prior cycles without once making a separate recordkeeping violation finding. The 2010 election cycle was the fourth election cycle under this regulation and the Audit Division's decision to include this as a finding now after three prior cycles under this regulation is clearly inconsistent with the Commission's approach in prior audits where no time logs were maintained. For example, in the 2006 Final Audit Report for the Georgia Federal Elections Committee, the Commission determined that the failure to maintain proper documentation would result in the requirement that employees must be disclosed on Line 30(b):

> The Audit staff's review of payroll expenses reported on Schedules H4 revealed that GFEC failed to maintain supporting documentation detailing the time spent on federal activities for employees whose salaries and related expenses totaled $231,366. Absent the supporting documentation, GFEC should have disclosed these salary and related expenses as non-allocable FEA on Schedules B, Line 30b, (Federal Election Activity Paid Entirely with Federal Funds).
>
> The Audit staff discussed this matter with GFEC's representatives during the audit and requested monthly logs, timesheets and affidavits. GFEC representatives were unable to locate any of the items requested.....
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> ....The Commission considered the Audit Division's Recommendation Memorandum in which the Audit Division recommended that the Commission adopt a finding that GFEC had not maintained adequate documentation detailing the time spent on federal activities for employees whose earnings and related payroll expenses were allocated on Schedules H4.
>
> Final Audit Report of the Georgia Federal Elections Committee for the 2006 Election Cycle, p. 10 (emphasis added).

Similarly, the Commission treated the same issue for the Tennessee Republican Party Federal Election Account as purely an over-funding and reporting issue in its 2006 Audit. The Audit Report did not discuss any specific recordkeeping violation.

According to these prior audits, the recordkeeping requirement exists for the sole purpose of determining the appropriateness of allocation by the committee under section 106.7(d) and the Commission did not create a separate recordkeeping finding in these prior audits. The recordkeeping requirement merely supports the need to further document the use of non-federal funds for these activities. Therefore, the separate recordkeeping finding is clearly duplicative and unnecessary.

Thus, this recordkeeping provision is not mandated by the Federal Election Campaign Act and it was the Commission who created this regulation for the apparent and sole purpose of assisting the Commission in monitoring compliance with the 25% provision found in 2 U.S.C. § 431(20)(A)(iv). The payment by a state party of an employee's salary and benefits with 100% federal dollars, and the disclosure of such payments on Line 30(b) of the committee's report is a clear concession that it is subject to the mandate found in this statute and the need to comply with the FEC's recordkeeping requirement is completely moot with respect to that employee.

I can assure you that state parties have, as a general matter, proceeded with this assumption, and I would expect that, due to the burden of the recordkeeping requirement, that few, if any, maintain time logs for 100% federal employees. If the Commission wishes to create a new standard for this recordkeeping requirement, it should do so by providing the regulated community with advanced notice and not penalize state parties by creating a new and novel finding of a violation of Commission regulations during the Audit process.

Based upon the above, it is clear that the Audit Division's recommendation to include a separate finding of a violation of Commission regulations if a state party committee does not maintain time logs for employees who are paid exclusively with federal funds is inconsistent with Commission regulations. Therefore, the Commission should direct the Audit Division to omit such a finding in the Interim Audit Report.

If you have any additional questions regarding this matter, I can be reached at (202) 479-1111.

Sincerely,

Neil Reiff