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FIRST GENERAL COUNSEL'S REPORT

SENSITIVE

Staff Member: Delbert K. Rigsby

Audit Referral: 98-03

Audit Referral Date: July 17, 1998

Date Activated: January 14, 1999

Expiration of Statute of

Limitations: February 8, 2001 to April 14,
2002

SOURCE:

AUDIT REFERRAL

RESPONDENTS:

Chicago's Committee for '96 and
Walter K. Knorr, as treasurer

1996 Democratic National Convention Committee, Inc.
and Andrew Tobias, as treasurer

**RELEVANT STATUTES
AND REGULATIONS:**

2 U.S.C. § 431
2 U.S.C. § 437
2 U.S.C. § 441(b)
26 U.S.C. § 9008
11 C.F.R. § 100.7(a)(1)(iii)
11 C.F.R. § 104.13
11 C.F.R. § 107.1
11 C.F.R. § 114.1(a)(2)(viii)
11 C.F.R. § 9008.3(a)(4)
11 C.F.R. § 9008.3(b)(2)
11 C.F.R. § 9008.7
11 C.F.R. § 9008.8
11 C.F.R. § 9008.51
✓ 11 C.F.R. § 9008.52

INTERNAL REPORTS CHECKED: Audit Documents
Disclosure Reports

FEDERAL AGENCIES CHECKED: None

21-01-402-4149

Audit Referral: 98-04

Audit Referral Date: July 17, 1998

Date Activated: January 14, 1999

Expiration of Statute of

Limitations: February 8, 2001 to

April 14, 2002

SOURCE:

AUDIT REFERRAL

RESPONDENTS:

1996 Democratic National Convention Committee, Inc.
and Andrew Tobias, as treasurer

Chicago's Committee for '96 and Walter K. Knorr, as
treasurer

Democratic National Committee and Andrew Tobias, as
treasurer

City of Chicago

**RELEVANT STATUTES
AND REGULATIONS:**

2 U.S.C. § 431
2 U.S.C. § 434
2 U.S.C. § 437
2 U.S.C. § 441a(a)
2 U.S.C. § 441b(a)
2 U.S.C. § 441b(b)(2)
26 U.S.C. § 9008
11 C.F.R. § 100.7(a)(1)(iii)
11 C.F.R. § 104.13
11 C.F.R. § 107.1
11 C.F.R. § 114.1(a)(2)(viii)
11 C.F.R. § 9004(a)
11 C.F.R. § 9008.3(b)(2)
11 C.F.R. § 9008.7
11 C.F.R. § 9008.8
11 C.F.R. § 9008.12(b)(3)
11 C.F.R. § 9008.52(c)

INTERNAL REPORTS CHECKED: Audit Documents
Disclosure Reports

FEDERAL AGENCIES CHECKED: None

21-04-402-4150

I. GENERATION OF MATTERS

Audit Referral 98-03 was generated by an audit of Chicago's Committee for '96 (the "Host Committee") and Walter K. Knorr, as treasurer, undertaken in accordance with 11 C.F.R. § 9008.54. The Audit Division's referral materials are attached. Attachment 1. The audit covered the period between August 11, 1994 through March 31, 1997.

Audit Referral 98-04 was generated by an audit of the 1996 Democratic National Convention Committee, Inc. (the "Convention Committee") and Andrew Tobias, as treasurer, undertaken in accordance with 26 U.S.C. § 9008(g). The Audit Division's referral materials are attached. Attachment 2. The audit covered the period between February 6, 1995 through September 30, 1996.

II. FACTUAL AND LEGAL ANALYSIS

A. Law

The Federal Election Campaign Act of 1971, as amended ("FECA"), provides that no corporation may make a contribution or an expenditure in connection with, *inter alia*, any political convention held to select candidates for president or vice president. 2 U.S.C. § 441b(a). Furthermore, no political committee may knowingly accept or receive any prohibited contribution. *Id.* The FECA, the Presidential Election Campaign Fund Act and the Commission's regulations provide a number of exceptions to the FECA's general prohibition of corporate contributions in connection with federal elections.¹ *See, e.g.,* 2 U.S.C. § 441b(a) and (b)(2). Pursuant to one such exception, corporations are permitted to donate funds that may be used in connection with presidential nominating conventions, in certain circumstances. *See*

¹ Presidential nominating conventions of political parties are defined to be elections. 2 U.S.C. § 431(1)(B).

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11 C.F.R. § 114.1(a)(2)(viii) (excluding activity permitted under 11 C.F.R. §§ 9008.52 or 9008.53 from the definition of corporate contributions and expenditures). Specifically, corporations that have offices or facilities in a particular local area may contribute funds to two types of local organizations that may assist presidential nominating conventions, which are known as municipal funds and host committees.

A host committee may be created to represent a city hosting a nominating convention in matters involving a presidential nominating convention. 11 C.F.R. § 9008.51. Corporations that have offices or facilities in a particular local area may contribute funds to a host committee that may also promote that area by assisting a convention. 11 C.F.R. § 9008.52(c). The principal objective of a host committee is the encouragement of commerce in the convention city, as well as the projection of a favorable image of the city to convention attendees. 11 C.F.R. § 9008.52(a). Host committees may accept funds from local businesses (except banks), local labor organizations and other local organizations or individuals, which may be used for expenses in connection with a presidential nominating convention only for permissible host committee expenditures such as those examples listed in 11 C.F.R. § 9008.52(c)(1)(i) through (ix).² *Id.*

Government agencies and municipal corporations may also provide services to a party convention. The Commission's regulations permit local businesses (excluding banks), local labor organizations and other local organizations or individuals to donate funds or make in-kind donations to a separate fund or account of the government agency or municipality to pay for expenses listed in 11 C.F.R. § 9008.52(c). 11 C.F.R. § 9008.53(b)(1). However, the fund or account must not be restricted for use in connection with any particular convention, and the

² Host committees may also accept goods or services from commercial vendors under the same terms and conditions set forth at 11 C.F.R. § 9008.9 for convention committees. 11 C.F.R. § 9008.52(b).

donations to the fund or account must be unrestricted and not solicited or designated for use in connection with any particular convention. *Id.*

In order to be eligible to receive public funds to finance the presidential nominating convention, a national party committee must establish a convention committee, which is responsible for conducting the day-to-day arrangements and operations of that party's presidential nominating convention and must register with and report to the Commission as a political committee. 11 C.F.R. § 9008.3(a)(1), (a)(2) and (b). A national party committee and its convention committee also must file a written agreement with the Commission agreeing to conditions set forth in 11 C.F.R. § 9008.3(a)(4)(i) through (viii) to be eligible for public funding. 11 C.F.R. § 9008.3(a)(4). As part of this agreement, the national party committee and its convention committee must agree to comply with 2 U.S.C. §§ 431 through 451, 26 U.S.C. § 9008, and applicable Commission regulations. 11 C.F.R. § 9008.3(a)(4)(vii). Thus, the committees must agree to abide by 2 U.S.C. §§ 441a and 441b, which prohibit, *inter alia*, corporate and labor organization contributions or expenditures in connection with conventions and limit other contributions, and they must agree to comply with the applicable expenditure limitation set forth at 26 U.S.C. § 9008(d) and 11 C.F.R. § 9008.8. 11 C.F.R. § 9008.3(a)(4)(vii) and (i), respectively. The national committee of a major party may not make expenditures with respect to a publicly-financed presidential nominating convention which, in the aggregate, exceed the amount of payments to which such committee is entitled under 26 U.S.C. § 9008(b)(1). 26 U.S.C. § 9008(d)(1). Thus, a convention committee's expenditure limitation is equal to its entitlement to public funds. 26 U.S.C. § 9008(d). The Commission may initiate an enforcement action if a convention committee knowingly helps, assists or participates in the making of a

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convention expenditure by a host committee, government agency, or municipal corporation that is not in accordance with 11 C.F.R. §§ 9008.52 or 9008.53. 11 C.F.R. § 9008.12(b)(7).

Convention expenses include all expenses incurred by or on behalf of a political party's national committee or convention committee with respect to and for the purpose of conducting a presidential nominating convention or convention-related activities. 11 C.F.R. § 9008.7(a)(4). Such expenses include administrative and office expenses for conducting the convention including stationery, office supplies, office machines, and telephone charges, but exclude the cost of any services supplied by the national committee at its headquarters or principal office if such services are incidental to the convention and not utilized primarily for the convention. 11 C.F.R. § 9008.7(a)(4)(x). Generally, convention expenses incurred with respect to a presidential nominating convention are subject to the expenditure limitation. *See* 11 C.F.R. § 9008.8(a). Nevertheless, certain expenditures related to a convention are not subject to the expenditure limitation. Convention related expenditures that are made by a host committee in accordance with 11 C.F.R. § 9008.52 shall not be considered convention committee expenditures and shall not count against the convention committee's expenditure limit. 11 C.F.R. § 9008.8(b)(1). Additionally, permissible host committee expenditures are not considered private contributions for the purpose of adjusting the convention committee's entitlement to public funds. 11 C.F.R. § 9008.5(b).

Host committees may receive funds or in-kind donations from local businesses (excluding banks), local labor organizations, and other local organizations and individuals for specific purposes related to hosting a national party convention. 11 C.F.R. § 9008.52(c)(1). The purposes for which a host committee may use funds in connection with a nominating convention are specified in 11 C.F.R. § 9008.52(c)(1)(i) through (xi) and include: (i) "promoting the

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suitability of the city as a convention site;" (ii) "welcoming the convention attendees to the city;" (iii) "facilitating commerce;" (vi) "local transportation services;" (vii) "law enforcement;" (viii) "convention bureau personnel to provide central housing and reservation services;" (ix) "hotel rooms at no charge or at a reduced rate;" and (x) "accommodations and hospitality for committees of the parties responsible for choosing the site of the conventions." See 11 C.F.R. § 9008.52(c)(1)(i)-(iii) and (vi)-(x). Host committees may also provide "use of an auditorium or convention center" and "construction and convention related services," such as "construction of podiums, press tables, false floors, camera platforms, additional seating, lighting, electrical, air conditioning and loud speaker systems, offices, office equipment, and decorations." 11 C.F.R. § 9008.52(c)(1)(v). Finally, in addition to those facilities and services specifically enumerated in 11 C.F.R. § 9008.52(c)(1)(i) through (x), a host committee is permitted to provide "other similar convention-related facilities services" under 11 C.F.R. § 9008.52(c)(1)(xi).

The FECA defines contributions to include a "gift, subscription, loan . . . or anything of value made by any person for the purpose of influencing any election for federal office."

2 U.S.C. § 431(8)(A)(1). "Anything of value" includes all in-kind contributions. 11 C.F.R. § 100.7(a)(1)(iii). The term "person" includes an individual, partnership, committee, association, corporation, labor organization, or any other organization or group of persons, but does not include the Federal Government or any authority of the Federal Government. 2 U.S.C. § 431(11).

Each treasurer of a political committee shall file detailed reports of its receipts and disbursements. 2 U.S.C. § 434(a)(1) and (b). Each in-kind contribution shall be reported as both a contribution and an expenditure. 11 C.F.R. § 104.13(a)(1) and (2). Each committee representing a national political party in making arrangements for the convention of the party to

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nominate a presidential candidate must file a full and complete financial statement with the Commission in accordance with the requirements of 11 C.F.R. §§ 107.1 and 9008.3(b). *See* 2 U.S.C. § 437(2). Host committees are required to file post-convention and quarterly reports that disclose all receipts and disbursements, including in-kind contributions made with respect to a presidential nominating convention. 11 C.F.R. § 9008.51(b). Each committee or organization which represents a state, or a political subdivision thereof, or any group of persons, in dealing with officials of a national political party with respect to matters involving a convention held in such state or political subdivision to nominate a presidential candidate must file a full and complete statement with the Commission in accordance with the requirements of 11 C.F.R. § 107.2. *See* 2 U.S.C. § 437(1) and 11 C.F.R. § 9008.51(c).

B. ANALYSIS

1. Telephone Charges

A total of \$726,835 in local and long distance telephone charges related to the Convention Committee were paid by the Host Committee and the City of Chicago. During the field audits of the Host Committee and the Convention Committee, the Commission's Audit staff identified Host Committee payments to Ameritech, beginning October 26, 1996 to April 14, 1997, which totaled \$512,637 for local telephone charges related to Convention Committee telephone numbers or accounts apparently assigned to the Convention Committee. Attachment 1 at 4; Attachment 2 at 5. The Audit staff also identified Host Committee payments to AT&T, beginning February 8, 1996 to February 25, 1997, which totaled \$87,688 for long distance telephone charges related to Convention Committee telephone numbers or accounts apparently assigned to the Convention Committee. *Id.* Memoranda from the Host Committee also attributed the expenditures for telephone charges to the Convention Committee. *Id.*

Additionally, the Audit staff identified payments from the City of Chicago to Ameritech, beginning January 30, 1996 to August 20, 1996, which totaled \$105,621 for local telephone charges on behalf of the Convention Committee. *Id.* The Audit staff also identified payments from the City of Chicago to AT&T, beginning February 12, 1996 to August 20, 1996, which totaled \$20,889 for long distance telephone charges on behalf of the Convention Committee. *Id.*

The Audit staff concluded in the Exit Conference Memoranda (the "ECM") for the audits that the telephone charges were convention overhead expenses which did not contribute toward promoting the City of Chicago or preparing the convention site for the convention. Attachment 1 at 5; Attachment 2 at 4, 5. In support of its conclusion, the Audit staff cited the Explanation and Justification for 11 C.F.R. § 9008.52, 59 Fed. Reg. 33614 (June 29, 1994), which states that the revised rules do not permit host committees to pay the convention committee's or the national party's overhead and administrative expenses for the convention. Finally, the Audit staff concluded that the telephone charges were in-kind contributions to the Convention Committee and recommended that the Convention Committee provide documentation that such expenditures were permissible host committee expenses pursuant to 11 C.F.R. § 9008.52(c). Attachment 2 at 5, 6.

In response to the Host Committee ECM, the Host Committee argued that the contract among the City of Chicago, the Convention Committee and the United Center³ required the Host Committee to provide the telecommunications system. Attachment 1 at 5. Moreover, the Host Committee argued that the telecommunications system was a convention-related service and

³ The United Center is a sports facility in Chicago, Illinois that is managed and operated by a partnership known as the United Center Joint Venture. The 1996 Democratic National Convention was held at the United Center.

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"served to accomplish a wide variety of tasks directly related to the Convention," such as construction and security. *Id.*

Similarly, the Convention Committee stated in response to the Convention Committee ECM that it interpreted 11 C.F.R. § 9008.52(c) to permit the Host Committee to pay for telephone service charges for the convention, and that the regulation does not distinguish between the costs of office telephones and the costs of using the telephones. Attachment 2 at 6. Moreover, the Convention Committee argued that the Explanation and Justification for 11 C.F.R. § 9008.52 should not be given precedence over the plain language of the regulation, and that the language of the Explanation and Justification is ambiguous. *Id.*

In the audit reports that were approved by the Commission on June 25, 1998, the Commission determined that the Host Committee made in-kind contributions totaling \$600,325 to the Convention Committee, and that the City of Chicago made in-kind contributions totaling \$126,510 to the Convention Committee. *Id.* Furthermore, in the Audit Report of the Convention Committee, the Commission determined that the Convention Committee should make a repayment of \$726,835 to the United States Treasury for the in-kind contributions received from the Host Committee and the City of Chicago.⁴ Attachment 2 at 6. On September 8, 1998, the Convention Committee submitted legal and factual materials to demonstrate that no repayment is required to be paid to the United States Treasury. 11 C.F.R. § 9007.2(c)(2)(i). The Convention Committee also requested an opportunity to address the Commission in open session pursuant to 11 C.F.R. § 9007.2(c)(2)(ii). The oral hearing was held on January 13, 1999. On January 5,

⁴ The Commission decided that an interim repayment of \$120,562 by the Convention Committee to the United States Treasury for unspent funds would be considered a credit against the repayment due for accepting in-kind contributions from the Host Committee and the City of Chicago relating to the telephone charges, which resulted in a net repayment amount due of \$606,273 (\$726,835-\$120,562). In August 1998, the Convention Committee closed its accounts and refunded \$46,144 in unspent funds to the United States Treasury.

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2000, the Office of General Counsel submitted a draft Statement of Reasons to the Commission regarding the Convention Committee's repayment. On February 3, 2000, the Commission directed the Office of General Counsel to revise the Statement of Reasons to reflect the determination that telephone expenses paid by the Host Committee and the City of Chicago on behalf of the Convention Committee are not in-kind contributions to the Convention Committee. On February 10, 2000, the Office of General Counsel submitted a revised Statement of Reasons to the Commission. On April 13, 2000, the Commission approved the revised Statement of Reasons, which states that there is no repayment due by the Convention Committee in connection with telephone expenses paid on its behalf by the Host Committee and the City of Chicago.

Any expenditures by a host committee that are not in accordance with 11 C.F.R. § 9008.52 are considered contributions, and not exempt from the prohibition on corporate contributions set forth in 11 C.F.R. § 114.1(a)(2)(viii). Some of the funds received by the Host Committee to promote the city and prepare the convention site were donated by corporations. If the Host Committee made expenditures that were not in accordance with 11 C.F.R. § 9008.52, the Host Committee would appear to have made contributions with prohibited funds in connection with a federal election, and the Convention Committee would appear to have received prohibited contributions in connection with a federal election. 2 U.S.C. § 441b(a).

However, the telephone charges of \$600,325 paid by the Host Committee on behalf of the Convention Committee are permissible expenses under 11 C.F.R. § 9008.52(c)(1)(v). Section 9008.52(c)(1)(v) lists office equipment as a permissible host committee expense, and the cost of using the equipment is a part of providing the equipment. In addition to paying for the telephone equipment and the installation of the telephone equipment, the Host Committee is permitted to

pay for telephone charges associated with using the telephone equipment. Therefore, the telephone charges are not in-kind contributions to the Convention Committee.

The Office of General Counsel recommends that the Commission find no reason to believe that the Chicago's Committee for '96 and Walter K. Knorr, as treasurer, made prohibited contributions to the 1996 Democratic National Convention Committee, Inc. in violation of 2 U.S.C. § 441b. Likewise, the Office of General Counsel recommends that the Commission find no reason to believe that the 1996 Democratic National Convention Committee, Inc. and Andrew Tobias, as treasurer, accepted prohibited contributions from the Chicago's Committee for '96 in violation of 2 U.S.C. § 441b.

Similarly, the City of Chicago is permitted to pay for the telephone charges on behalf of the Convention Committee. The City of Chicago paid telephone charges totaling \$126,835. The Commission's regulation, which concerns receipts and disbursements of government agencies and municipal corporations for party conventions, permits those government agencies and municipal corporations to receive donations for expenses listed in 11 C.F.R. § 9008.52(c). 11 C.F.R. § 9008.53(b). The cost of using office equipment is a permissible host committee expense under 11 C.F.R. § 9008.52(c)(1)(v).

The City of Chicago and the Host Committee must file a full and complete financial statement with the Commission pursuant to 2 U.S.C. §§ 437(1) and (2). If the telephone expenses were considered in-kind contributions, the Host Committee and the City of Chicago would need to be report those contributions. Because the expenditures are not considered in-kind contributions, the Host Committee did not have an obligation to report the telephone expenses as contributions to the Convention Committee. Moreover, the City of Chicago did not have an obligation to report the telephone expenses as contributions to the Convention Committee. Thus,

the Office of General Counsel recommends that the Commission find no reason to believe that the Chicago's Committee for '96 and Walter K. Knorr, as treasurer, failed to report an in-kind contribution to the 1996 Democratic National Convention Committee, Inc. in violation of 2 U.S.C. § 437(1). Furthermore, the Office of General Counsel recommends that the Commission find no reason to believe that the City of Chicago failed to report an in-kind contribution to the 1996 Democratic National Convention Committee, Inc. in violation of 2 U.S.C. § 437(1). Likewise, since the telephone expenses were not in-kind contributions, the Convention Committee had no obligation to report in-kind contributions from the Host Committee and the City of Chicago in connection with the telephone expenses. Thus, the Office of General Counsel recommends that the Commission find no reason to believe that the 1996 Democratic National Convention Committee, Inc. and Andrew Tobias, as treasurer, failed to report an in-kind contribution from the Host Committee in violation of 2 U.S.C. § 437(2). The Office of General Counsel also recommends that the Commission find no reason to believe that the 1996 Democratic National Convention Committee, Inc. and Andrew Tobias, as treasurer, failed to report an in-kind contribution from the City of Chicago in violation of 2 U.S.C. § 437(2).

The Convention Committee accepted the full public grant. In-kind contributions are both contributions and expenditures. 11 C.F.R. §§ 100.7(a)(1)(iii) and 100.8(a)(1)(iii). If the telephone expenses were considered in-kind contributions, the Convention Committee would have exceeded its expenditure limit. 11 C.F.R. § 9008.8(b)(1). However, the payment of the telephone expenses did not constitute in-kind contributions. For the 1996 election cycle, the expenditure limit for presidential nominating conventions receiving public funds was \$12,364,000, and the Convention Committee spent \$12,313,383. Therefore, the Office of

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General Counsel recommends that the Commission find no reason to believe that the 1996 Democratic National Convention Committee, Inc. and Andrew Tobias, as treasurer, exceeded the expenditure limit for publicly financed presidential nominating conventions in violation of 26 U.S.C. § 9008(d), as a result of receiving in-kind contributions relating to telephone charges.

2. Hotel Charges

In the Audit Report of the Convention Committee, the Audit staff noted that published reports indicated that the Democratic National Committee ("DNC") assumed approximately \$25,000 in hotel bills incurred at the Democratic National Convention because of "concerns that a donor who originally paid the bill might have used foreign funds."⁵ Attachment 2 at 7. The donor, Mr. Gregory Cortes, has been a volunteer fundraiser for the DNC. *Id.* The hotel bills related to suites for Marvin Rosen, the Finance Chairman of the DNC, and R. Scott Pastrick, the Convention Committee Treasurer and DNC Treasurer, and two additional rooms at the Four Seasons Hotel in Chicago, Illinois. During the audit fieldwork, the Audit staff requested documentation regarding these expenses and asked whether a portion of the expenses, such as the expenses for Mr. Pastrick, relate to the convention. The Convention Committee responded with a memorandum that stated, "during the week of the convention, Mr. Pastrick's sole function, other than a five minute speech at the Monday Convention session, was to serve in a fundraising capacity for the DNC." *Id.* The Convention Committee also stated that during the week of the convention, Mr. Pastrick did not have any responsibilities as treasurer of the Convention Committee, and provided a copy of Mr. Pastrick's speech to the convention. *Id.*

⁵ This information appeared in the *Washington Post* on December 12, 1996 and January 8, 1997. See Attachment 3.

In the ECM, the Audit staff requested documentation, such as the hotel bills and a copy of Mr. Pastrick's appointment calendar during the convention week. The Convention Committee refused to submit such documentation to the Audit staff, but responded that "it is fundamental to the Convention financing system that the costs of national party fundraising at the Convention should not be paid for with public Convention grant. . . . Thus, it is clear that no part of Mr. Pastrick's expenses should have been allocated to the [Convention Committee]." Attachment 2 at 8. Nevertheless, the Audit Report noted that the hotel expenses for Mr. Pastrick and the expenses for the two additional rooms should be allocable, in part, to the Convention Committee. Attachment 2 at 7.

The Convention Committee asserted that Mr. Pastrick's hotel expenses should have been paid by the DNC since his responsibilities during the convention week were to raise funds for the DNC. Although this Office agrees with the Convention Committee's assertion that public funds should not be used to pay the costs of national party fundraising, *see* 59 Fed. Reg. 33608 (June 29, 1994), the Commission has also noted "instances in which the national committee has sought to pay for expenses that are clearly convention-related." 59 Fed. Reg. 33608 (June 29, 1994). Events that are "clearly separate from the convention such as fundraising for the party committees" are not considered convention expenses and should not be paid for with public funds. 59 Fed. Reg. 33609 (June 29, 1994). However, the Convention Committee did not provide the Audit staff with documentation which was requested that would support this conclusion, such as Mr. Pastrick's itinerary during the convention week. Moreover, it appears likely that Mr. Pastrick did perform some duties as treasurer of the Convention Committee during the convention week, which was the important time of the year for the Convention Committee. If Mr. Pastrick performed any duties as treasurer of the Convention Committee

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during the convention week, his hotel expenses should have been allocated, in part, to the convention. 11 C.F.R. § 9008.7.

The Convention Committee also did not provide the Audit staff with information regarding the two additional hotel rooms that were paid for by the DNC, such as the purpose for reserving those rooms and the activities that were conducted in those rooms. These expenses for the additional hotel rooms may also need to be allocated, in part, to the convention. 11 C.F.R. § 9008.7.

The failure to allocate Mr. Pastrick's expenses and the expenses for the two additional rooms means that the Convention Committee received an apparent in-kind contribution from the DNC. The hotel expenses allocated to the Convention Committee should count against the Convention Committee's expenditure limitation. However, if the hotel expenses estimated at \$25,000 are allocated, in part, to the convention, the Convention Committee would still not exceed its expenditure limit because the Convention Committee has a surplus of \$50,617.⁶ Thus, the Office of General Counsel recommends that the Commission find no reason to believe that the 1996 Democratic National Convention Committee, Inc. and Andrew Tobias, as treasurer, exceeded the expenditure limit for publicly financed presidential nominating conventions in violation of 26 U.S.C. § 9008(d), as a result of receiving in-kind contributions relating to hotel expenses. Nevertheless, it appears that the Convention Committee failed to report this in-kind contribution from the DNC on its disclosure reports to the Commission. 2 U.S.C. § 437(2);

⁶ The Audit Report of the Convention Committee indicated a deficit of \$676,218 on the Statement of Net Outstanding Convention Expenses (NOCE Statement) because the telephone expenses were counted as in-kind contributions. If the telephone expenses were not considered in-kind contributions and counted against the expenditure limit, the NOCE Statement would have indicated a surplus of \$50,617. See Audit Report of the Convention Committee at p. 19 and 20. The Commission has determined in the Statement of Reasons on the 1996 Democratic National Convention Committee, Inc. that the telephone expenses are not in-kind contributions.

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11 C.F.R. §§ 107.1 and 9008.3(b). Therefore, the Office of General Counsel recommends that the Commission find reason to believe that the 1996 Democratic National Convention Committee, Inc. and Andrew Tobias, as treasurer, violated 2 U.S.C. § 437(2) by failing to report the receipt of this in-kind contribution from the Democratic National Committee. Moreover, it appears that the DNC failed to report the in-kind contribution on its disclosure reports to the Commission. 2 U.S.C. § 434(b). Therefore, the Office of General Counsel recommends that the Commission find reason to believe that the Democratic National Committee and Andrew Tobias, as treasurer, violated 2 U.S.C. § 434(b) by failing to report this in-kind contribution to the 1996 Democratic National Convention Committee, Inc.⁷

III. DISCUSSION OF CONCILIATION AND CIVIL PENALTY

⁷ The DNC is not prohibited from making contributions to the Convention Committee. This Office is not recommending that the Commission find reason to believe that the DNC violated the Presidential Election Campaign Fund Act for making contributions to the Convention Committee because there is no provision in that statute or in the FECA which prohibits the making of contributions to a convention committee which receives full public funding.

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IV. RECOMMENDATIONS

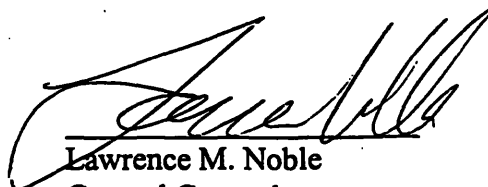
1. Open a Matter Under Review relating to AR 98-03.
2. Open a Matter Under Review relating to AR 98-04.
3. Find no reason to believe that Chicago's Committee for '96 and Walter K. Knorr, as treasurer, made prohibited contributions to the 1996 Democratic National Convention Committee, Inc. in violation of 2 U.S.C. § 441b.
4. Find no reason to believe that the 1996 Democratic National Convention Committee, Inc. and Andrew Tobias, as treasurer, received prohibited contributions in violation of 2 U.S.C. § 441b.
5. Find no reason to believe that Chicago's Committee for '96 and Walter K. Knorr, as treasurer, failed to report in-kind contributions to the 1996 Democratic National Convention Committee, Inc. in violation of 2 U.S.C. § 437(1).
6. Find no reason to believe that the 1996 Democratic National Convention Committee, Inc. and Andrew Tobias, as treasurer, failed to report in-kind contributions from Chicago's Committee for '96 in violation of 2 U.S.C. § 437(2).
7. Find no reason to believe that the 1996 Democratic National Convention Committee, Inc. and Andrew Tobias, as treasurer, failed to report in-kind contributions from the City of Chicago in violation of 2 U.S.C. § 437(2).
8. Find no reason to believe that the City of Chicago failed to report in-kind contributions to the 1996 Democratic National Convention Committee, Inc. in violation of 2 U.S.C. § 437(1).
9. Find no reason to believe that the 1996 Democratic National Convention Committee, Inc. and Andrew Tobias, as treasurer, exceeded the expenditure limitation for publicly financed presidential nominating conventions in violation of 26 U.S.C. § 9008(d), as a result of receiving in-kind contributions relating to telephone charges.
10. Find no reason to believe that the 1996 Democratic National Convention Committee, Inc. and Andrew Tobias, as treasurer, exceeded the expenditure limitation for publicly financed presidential nominating conventions in violation of 26 U.S.C. § 9008(d), as a result of receiving in-kind contributions relating to hotel expenses.

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11. Find reason to believe that the 1996 Democratic National Convention Committee, Inc. and Andrew Tobias, as treasurer, failed to report an in-kind contribution from the Democratic National Committee in violation of 2 U.S.C. § 437(2), and enter into conciliation prior to a finding of probable cause to believe.
12. Find reason to believe that the Democratic National Committee and Andrew Tobias, as treasurer, failed to report an in-kind contribution to the 1996 Democratic National Convention Committee, Inc. in violation of 2 U.S.C. § 434(b), and enter into conciliation prior to a finding of probable cause to believe.
13. Close the file relating to AR 98-03.
14. Approve the attached Factual and Legal Analyses.
15. Approve the attached conciliation agreements.
16. Approve the appropriate letters.

Date

8/11/00


 Lawrence M. Noble
 General Counsel

Attachments

1. Audit Referral Materials relating to Chicago's Committee for '96
2. Audit Referral Materials relating to the 1996 Democratic National Convention Committee, Inc.
3. Washington Post newspaper articles
4. Factual and Legal Analysis for the 1996 Democratic National Convention Committee, Inc.
5. Factual and Legal Analysis for the Democratic National Committee
6. Proposed Conciliation Agreement with the 1996 Democratic National Convention Committee, Inc.
7. Proposed Conciliation Agreement with the Democratic National Committee

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FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

JUL 17 3 23 PM '98

July 17, 1998

Memorandum

Audit Referral 98-03

To: Lawrence M. Noble
General Counsel

Through: John C. Surina
Staff Director

From: Robert J. Costa *Plh Fr RJC 7-17-98*
Assistant Staff Director
Audit Division

Subject: Chicago's Committee for '96 - Matter Referred to the Office of General Counsel

On June 25, 1998, the Commission approved the Audit Report on Chicago's Committee for '96. Based on the Commission approved Materiality Thresholds, Finding II.A.2., Apparent Convention Committee Expenses Paid by the Host Committee and City of Chicago - Telecommunications. is being referred to your office.

All workpapers and related documents are available for review in the Audit Division. Should you have any questions, please contact Wanda Thomas or Rick Halter at 694-1200.

Attachment as stated.

II. AUDIT FINDINGS AND RECOMMENDATIONS

A. CONVENTION-RELATED EXPENDITURES

Section 9008.52(c) of Title 11 of the Code of Federal Regulations states, in part, that contributions received by host committees may be used for the following: to defray those expenses incurred for the purpose of promoting the suitability of the city as a convention site; to defray those expenses incurred for welcoming the convention attendees to the city, such as expenses for information booths, receptions, and tours; to defray those expenses incurred in facilitating commerce, such as providing the convention and attendees with shopping and entertainment guides and distributing the samples and promotional material specified in 11 CFR 9008.9(c); to defray the administrative expenses incurred by the host committee, such as salaries, rent, travel, and liability insurance; and to provide the national committee use of an auditorium or convention center and to provide construction and convention related services for that location such as: construction of podiums; press tables, false floors, camera platforms; additional seating; lighting, electrical, air conditioning and loudspeaker systems; offices; office equipment; and decorations.

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

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

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

On August 19, 1996, the City and the DNCC amended the Contract, in part, with a budget revision entitled "Chicago '96/City Budget." Each expense classification in the revised budget was identified by line number, line item, total amount budgeted, total cash spent, and total in-kind contributions allocated to that line item. The

Audit staff's review of management controls disclosed that the Committee's disbursements records included memoranda which identified expenditures made on behalf of the DNCC and the budget line number to which each expense should be allocated. The apparent objective of these controls was to facilitate managerial reporting and compliance with the budget.

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

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

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

2. Telecommunications

Section 9008.7(a)(4)(x) of Title 11 of the Code of Federal Regulations states that "Convention Expenses" include all expenses incurred by or on behalf of a political party's national committee or convention committee with respect to and for the purpose of conducting a presidential nominating convention or convention-related activities. Such expenses include administrative and office expenses for conducting the convention, including stationery, office supplies, office machines, and telephone charges; but exclude the cost of any services supplied by the national

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

committee at its headquarters or principal office if such services are incidental to the convention and not utilized primarily for the convention.

As mentioned above, 11 CFR §9008.52(c) permits host committees to provide the national committee use of a convention center and convention related services for that location such as offices and office equipment. Additionally, the E&J states, in part, that the revised rules at 11 CFR §9008.52(c) do not permit host committees or municipalities to pay the convention committee's or the national party's overhead and administrative expenses related to the convention.²

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

Committee records documented payments totaling \$600,325 for local and long distance telephone service. Furthermore, documents obtained by the Audit staff indicate that the City of Chicago paid an additional \$126,510.³ These payments were apparently made in execution of the Contract's provisions related to telecommunications, and, the Committee's expenditures are discussed in more detail below.

a. Ameritech

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

b. AT&T

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

² See 59 Fed. Reg. 33,614 (June 29, 1994).

³ These disbursements are outside of the scope of this audit report; however, we do note that pursuant to 11 CFR §9008.53(b) expenditures made by a municipality or government agency should also meet the requirements of 11 CFR §9008.52(c). Additional details on payments by the City are contained in the audit report on the DNCC.

assigned to the DNCC. Furthermore, internal Committee memoranda attributed all of the expenses to the DNCC.

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

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

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

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

Fund-Raiser Paid Tab For DNC Hotel Suites

Party Improperly Failed to Report Donation

By Charles R. Babcock
and Ruth Marcus
Washington Post Staff Writers

Two senior Democratic National Committee officials arranged for a party donor to pick up the tab for their expensive hotel suites during the Democratic convention, a payment that the DNC improperly failed to report to the Federal Election Commission, party officials said yesterday.

DNC finance chairman Marvin Rosen stayed at the \$3,000-a-night presidential suite at Chicago's Four Seasons Hotel and party treasurer R. Scott Pastrick stayed in a smaller suite, officials said. The total cost, which included bills for two additional DNC rooms, was between \$25,000 and \$35,000, according to sources familiar with the payment.

The bill was paid by Greg Cortes, an attorney and consultant from Puerto Rico who chaired the Hispanic Leadership Forum, which raises money from the Hispanic community. Cortes said in an interview he was asked to pay the bill by a DNC finance staff member. This happened after the Four Seasons declined to provide suites for free, the sources said.

It is common for donors to underwrite the costs of party functions, such as paying for a reception or donating the food served there. But both Democratic and Republican sources said it was unusual to solicit donors to pay for party officials' hotel rooms, particularly on such a scale.

The DNC itself limits staff to paying \$155 a night for hotel rooms, though costs may go higher at conventions, where rooms are at a premium. Some DNC staff members were angered by the decision to solicit donations to pay for costly suites, rather than using the money to benefit party candidates. "It obviously raises a question of judgment," one senior administration official said.

Rosen said he told the DNC staff that "we need a couple of suites to bring donors up to from time to time and have meetings ourselves. I think that's pretty customary." Asked why the DNC did not pay for the suites directly, he said, "We were trying to save whatever type of money we could. We were trying to get people to pay for as many events as the DNC would incur, ranging from breakfasts and dinners to rooms."

Pastrick did not return a telephone call yesterday.

The DNC has had other problems with fund-raising and reporting in recent months, with party officials already under fire for accepting questionable or illegal donations.

to properly scrutinize their origins. The DNC has returned about \$1.5 million in questionable or illegal donations and, under pressure, reversed its decision in October to not file a final pre-election report with the FEC. It has hired outside auditors to examine its books.

After inquiries by The Washington Post, the DNC acknowledged that it should have listed the August hotel room costs as an "in-kind" contribution by Cortes on its FEC reports. DNC press secretary Amy Weiss Tobe said the cost wasn't listed because she had not responded to requests for documentation from the finance department, and DNC lawyers and accountants who prepared the party's FEC reports were not aware of Cortes's payment. She said the party would file an amended report with the FEC listing the cost as soon as it determines the amount.

Cortes declined to be specific about exactly who paid the bill, saying only that his "group" from Puerto Rico made the payment. He said he would get back to a reporter with details about the bill, but did not.

"They asked us to do it and we did it," Cortes said. "We didn't see anything unusual about it."

Republican National Committee press secretary Mary Mead Crawford said GOP officials do not ask donors to pay for hotel rooms, although party leaders may receive a complimentary room as part of an arrangement with a hotel. "The party pays for its staff and top officials and finance leaders pay their own way," she said.

Tobe defended the payments, saying they were necessary for Rosen and Pastrick to entertain donors. "We needed suites, the hotel wouldn't comp the suites, so we asked a donor to pick up the cost. It's appropriate for people within the party structure to have space available for entertaining, meetings or other purposes."

The Four Seasons Hotel housed the DNC's biggest donors, and Rosen and Pastrick wanted to be near them rather than at the DNC's convention headquarters at the Hyatt, officials said.

Rosen, a Miami lawyer, has headed the party's fund-raising operations since September 1995, overseeing a record harvest in which the party took in a record \$125 million this year. He is not on the DNC's staff but serves in a volunteer part-time capacity in which his role is to court the party's major donors. Pastrick, a Washington public affairs consultant, has been considered

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THE WASHINGTON POST

Wed. Jan. 8, 1997

ATTACHMENT 3
Page 2 of 2

DNC Assumes Hotel Bills First Paid by Business Consultant

By Charles R. Babcock
Washington Post Staff Writer

The Democratic National Committee is assuming about \$25,000 in hotel bills incurred at the party's Chicago convention last August, partly because of concerns that a donor who originally paid the bill might have used foreign funds, according to sources.

The DNC began investigating how the bill at the Four Seasons Hotel was handled last month after The Washington Post reported that Greg Cortes, an attorney and business consultant from Puerto Rico, had picked up the tab. Cortes

paid for a \$3,000-a-night suite for DNC finance chairman Marvin Rosen and a smaller suite for party treasurer R. Scott Pastrick after the hotel refused to provide the rooms for free.

The DNC failed to report Cortes's payment as an in-kind contribution to the party in its filings at the Federal Election Commission. DNC spokeswoman Amy Weiss Tobe had said earlier that the party would do so as soon as it determined the proper amount to report.

The party decided to pay the bill, sources said, because officials couldn't determine the source of

the funds Cortes used. Cortes would not return the DNC's phone calls and the hotel could not determine the original source of the wire transfer of funds that covered much of the bill, the sources said.

One source said officials were concerned in part that the wire transfer might have come from Cortes's business associates in South America. This would have added to the party's woes about improper contributions from foreign sources. The DNC has returned \$1.5 million to donors, most of it raised by Asian American fund-raiser John Huang. It is common for donors to un-

derwrite the costs of party functions—for example, by paying for a reception or donating the food served at an event. But both Democratic and Republican officials said it is unusual to solicit donors to pay for party officials' hotel rooms, particularly such expensive ones.

The DNC limits staff to paying \$155 a night for hotel rooms, though costs may go higher at conventions. Some staff members were angered by the decision to solicit donations to pay for suites, rather than using the money to benefit party candidates.

Rosen said last month that he told DNC staff, "We need a couple

of suites to bring donors up to from time to time and to have meetings ourselves. I think that's pretty customary." To save money, Rosen said, the DNC didn't pay for the suites directly. The DNC's biggest donors stayed at the Four Seasons, and Rosen and Pastrick wanted to be near them, rather than staying at the convention headquarters hotel, officials said.

Rosen, a Miami lawyer, has headed the party's fund-raising operations since September 1995. He is not on the staff but serves in a volunteer, part-time capacity. Pastrick, a Washington consultant, has been considered a top fund-raiser.

11-204-140-12

DR



FEDERAL ELECTION COMMISSION

Washington, DC 20463

MEMORANDUM

TO: Lawrence M. Noble
General Counsel

FROM: Mary W. Dove/Lisa R. Davis
Acting Commission Secretary

A handwritten signature, likely of Mary W. Dove or Lisa R. Davis, is written over the "FROM" line. The signature is in dark ink and appears to be a stylized combination of the first letters of the names.

DATE: August 15, 2000

SUBJECT: Audit Referrals #98-03 & #98-04 - First General Counsel's Report
dated August 11, 2000.

The above-captioned document was circulated to the Commission
on Monday, August 14, 2000.

Objection(s) have been received from the Commissioner(s) as
indicated by the name(s) checked below:

Commissioner Mason	—
Commissioner McDonald	—
Commissioner Sandstrom	—
Commissioner Smith	—
Commissioner Thomas	<u>XXX</u>
Commissioner Wold	—

This matter will be placed on the meeting agenda for

Tuesday, August 22, 2000.

Please notify us who will represent your Division before the Commission on this
matter.

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