FEDERAL ELECTION COMMISSION
WASHINGTON, D C 20463

MAR 1 5 2005

CERTIFIED MAIL
RETURNED RECEIPT REQUESTED

W. Alan Wilk, Esq.
Dykema Gossett PLLC
124 W. Allegan Street, Suite 800
Lansing, MI 48933

RE: MUR 5488

Dear Mr. Wilk:

On July 28, 2004, the Federal Election Commission notified your clients, Brad Smith for Congress ("the Committee") and James Bailey, in his official capacity as Treasurer, of a complaint alleging violations of certain sections of the Federal Election Campaign Act of 1971, as amended ("the Act"). On February 9, 2005, the Commission notified your client, Bradley Smith, in his personal capacity as candidate, of the same complaint. A copy of the complaint was forwarded to your clients at that time.

Upon further review of the allegations contained in the complaint, and information provided by your clients, the Commission, on March 9, 2005, found that there is reason to believe your clients, Brad Smith for Congress and James Bailey, in his official capacity, as Treasurer, and Bradley Smith, in his personal capacity as candidate, violated 2 U.S.C. § 441a(f) of the Act by accepting excessive contributions. The Factual and Legal Analysis, which formed a basis for the Commission's finding, is attached for your information. Please note that Respondents have an obligation to preserve all documents, records and materials relating to the Commission's investigation.

You may submit any factual or legal materials that you believe are relevant to the Commission's consideration of this matter. Please submit such materials to the General Counsel's Office within 15 days of receipt of this letter. Where appropriate, statements should be submitted under oath. In the absence of additional information, the Commission may find probable cause to believe that a violation has occurred and proceed with conciliation.

In order to expedite the resolution of this matter, the Commission has also decided to offer to enter into negotiations directed towards reaching a conciliation agreement in settlement of this matter prior to a finding of probable cause to believe. Enclosed is a conciliation agreement that the Commission has approved. If you are interested in expediting the resolution of this matter by pursuing preprobable cause conciliation, and if you agree with the provisions of the enclosed agreement, please sign and return the agreement, along with the civil penalty, to the Commission. In light of the fact that conciliation negotiations, prior to a finding of probable cause to believe, are limited to a maximum of 30 days, you should respond to this notification as soon as possible.

Requests for extensions of time will not be routinely granted. Requests must be made in writing at least five days prior to the due date of the response and specific good cause must be demonstrated. In addition, the Office of the General Counsel ordinarily will not give extensions beyond 20 days.

This matter will remain confidential in accordance with 2 U.S.C. §§ 437g(a)(4)(B) and 437g(a)(12)(A) unless you notify the Commission in writing that you wish the matter to be made public. If you have any questions, please contact Audra Wassom, the attorney assigned to this matter, at (202) 694-1650.

Sincerely,

Scott E. Thomas
Chairman

Enclosures
Factual and Legal Analysis
Conciliation Agreement

FEDERAL ELECTION COMMISSION

FACTUAL AND LEGAL ANALYSIS

RESPONDENTS: Brad Smith for Congress and James Bailey, in his official capacity as Treasurer; and Bradley Smith.

MUR: 5488

I. INTRODUCTION

This matter was generated by a complaint filed with the Federal Election Commission by John Truscott. Complainant alleges that Brad Smith for Congress and James Bailey, in his official capacity as Treasurer, and Bradley Smith (collectively "Respondents"), violated the Federal Election Campaign Act of 1971, as amended ("the Act") by improperly accepting contributions in excess of the normal limits. The evidence demonstrates that there is reason to believe that Respondents violated 2 U.S.C. § 441a(f) of the Act by improperly accepting excessive contributions. Accordingly, the Commission finds reason to believe that Respondents violated the Act.

II. FACTUAL AND LEGAL ANALYSIS

A. Background

Brad Smith for Congress ("the Committee") is the principal campaign committee for Bradley Smith, who ran in the Republican primary for Michigan's 7th Congressional District in the 2004 election. James Bailey was the Committee's treasurer at all relevant times. Mr. Smith personally lent the Committee $100,000 on September 30, 2003. On March 31, 2004, Mr. Smith lent the Committee another $40,000.[1] Resp. at 1.

[1] As of December 31, 2003, for the purpose of calculating the OPFA under one of the relevant formulas, Respondents' aggregate gross receipts minus any contributions or loans by Smith from personal funds appear to have been between $89,000.38 and $100,722.38. The Form 3Z-1, which reflects the exact amount of his gross receipts minus personal expenditures for the primary election, was incomplete. RAD sent an RFAI and the Committee filed two amendments to the Form 3Z-1, neither of which appears to be

Gene DeRossett, one of Mr. Smith's opponents in the Republican primary election, had loaned his own campaign a total of $451,000 out of his personal funds by March 31, 2004. DeRossett made loans to his campaign from personal funds in the following amounts and on the following dates: (1) $57,000 on April 8, 2003; (2) $139,000 on June 26, 2003; (3) $25,000 on December 30, 2003; and (4) $230,000 on March 31, 2004.[2] On April 19, 2004, Mr. DeRossett's campaign filed the 24-Hour Notice of Expenditures from Personal Funds (FEC Form 10) disclosing total expenditures of $451,000. *See* 11 C.F.R. § 400.21(b).

Respondents, who subsequently used Mr. DeRossett's personal loans as the basis for claiming eligibility for higher limits under the millionaires' amendment, are unsure of whether they received a copy of Mr. DeRossett's April 19, 2004 Form 10.[3] Resp. at 3, n.2. On April 22, 2004, The Committee repaid Mr. Smith $50,000 of the $140,000 he had previously lent.[4] Respondents state that they had constructive knowledge of Mr. DeRossett's Form 10 sometime in May when they viewed a copy of the form on the FEC website. Resp. at 2. Although Respondents state that Mr. Smith signed and faxed the FEC Form 11 (Notice of Opposition Personal Funds Amount) to the Commission on June

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correct. Therefore, this Office can only determine that Respondents' gross receipts minus the candidate's personal expenditures for the year-end 2003 were between $89,000.38 and $100,722.38.

[2] As of December 31, 2003, DeRossett's aggregate gross receipts minus any contributions or loans by DeRossett from personal funds equaled $223,215.37.

[3] Because Respondents were not eligible for increased limits, it is not necessary to evaluate this claim.

[4] On April 19, 2004, apparently unrelated to DeRossett's filing the Form 10 on the same date, Club for Growth endorsed Brad Smith. The response states that as a result of this endorsement, Smith expected to receive "substantially increased individual contributions to his campaign," and therefore decided that his Committee could repay part of his loan. Resp. at 2.

11, 2004, according to the Commission's records, Mr. Smith's FEC Form 11 was received on June 15, 2004.[5] Resp. at 3. Acting pursuant to their claimed eligibility for higher limits, Respondents accepted $40,500 in contributions that exceeded the standard $2,000 limit between June 10, 2004 and August 2, 2004. *See* Attachment 1.

B. Analysis

Pursuant to the "millionaires' amendment" to the Bipartisan Campaign Reform Act of 2002, a candidate for the U.S. House of Representatives might be permitted to raise contributions under special increased contribution limits if he or she has an opponent that has spent more than $350,000 of personal funds on his or her campaign. 2 U.S.C. § 441a-1(a). In order to determine whether the candidate is eligible for increased contribution limits, the candidate must compute the "opposition personal funds amount" ("OPFA"). Only if the OPFA exceeds $350,000 is the candidate eligible for increased contribution limits. *Id.*

1. Formula for Calculating OPFA

In describing the OPFA, the Act provides that:

> (A) *In general.* The opposition personal funds amount is an amount equal to the excess (if any) of --
>
> (i) the greatest aggregate amount of expenditures from personal funds (as defined in subsection (b)(1)) that an opposing candidate in the same election makes; over
>
> (ii) the aggregate amount of expenditures from personal funds made by the candidate with respect to the election.

[5] As discussed below, the OPFA was incorrectly calculated and the Committee was not eligible for higher limits. Accordingly, there is no reason to reach any conclusion on the issue of whether the Form 11 was either necessary or timely filed.

2 U.S.C. § 441a-1(2)(A)(i)-(ii).[6]

The implementing regulations provide different formulas for calculating the OPFA based on the time at which it is being calculated and taking into account funds raised through contributions by each campaign. In this matter, the OPFA was being calculated in June of 2004, the year of the general election, so the applicable calculation was set forth in 11 C.F.R. § 400.10(a)(3):

> (3) To compute the opposition personal funds amount from February 1 of the year in which the general election is held to the day of the general election, one of the following formulas must be used:
> (i) If e>f, opposition personal funds amount = a-b-((e-f) ÷ 2).
> (ii) If e≤f, opposition personal funds amount = a-b.

The variables to be used in the formulas laid out in 11 C.F.R. § 400.10(a) are set forth in 11 C.F.R. § 400.10(b), as follows:

> (b) *Variables.* The variables used in the formulas set out in paragraph (a) of this section are defined as follows:

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[6] In 2 U.S.C. § 441a-1(b)(1)(A)(i)-(ii), the Act defines "expenditure from personal funds" as:

> (i) an expenditure made by a candidate using personal funds; and
> (ii) a contribution or loan made by a candidate using personal funds or a loan secured using such funds to the candidate's authorized committee.

In 11 C.F.R. § 400.4(a)(1)-(4), the implementing regulations further define "expenditure from personal funds" as:

> (a) ... the aggregation of all the following:
> (1) An expenditure made by a candidate, using the candidate's personal funds, for the purpose of influencing the election in which he or she is a candidate;
> (2) A contribution or loan made by a candidate to the candidate's authorized committee, using the candidate's personal funds;
> (3) A loan by any person to the candidate's authorized committee that is secured using the candidate's personal funds; and
> (4) Any obligation to make an expenditure from personal funds that is legally enforceable against the candidate.

a = Greatest aggregate amount of expenditures from personal funds made by the opposing candidate in the same election.

b = Greatest aggregate amount of expenditures from personal funds made by the candidate in the same election. ...

e = Aggregate amount of the gross receipts of the candidate's authorized committee minus any contributions by the candidate from personal funds as reported under 11 CFR 104.19(b)(2)(v) or (vi), during any election cycle that may be expended in connection with the election for the nomination for election, or election, to Federal office sought, as determined on December 31 of the year preceding the year in which the general election is held.

f = Aggregate amount of the gross receipts of the opposing candidate's authorized committee minus any contributions by that opposing candidate from personal funds as reported under 11 CFR 104.19(b)(2)(v) or (vi), during any election cycle that may be expended in connection with the election for the nomination for election, or election, to Federal office sought, as determined on December 31 of the year preceding the year in which the general election is held.

Because DeRossett's aggregate gross receipts minus any contributions or loans made by him to his campaign committee as of December 31, 2003 (variable "f") were higher than Respondents' corresponding figures (variable "e"), Respondents correctly used the "a-b" formula in 11 C.F.R. § 400.10(a)(3)(ii) for calculating the OPFA. In that formula "a" would be Mr. DeRossett's greatest aggregate amount of personal expenditures for his campaign and "b" would be Mr. Smith's greatest aggregate amount of personal expenditures for his campaign. *See* Definitions of Variables "a" and "b" in 11 C.F.R. § 400.10(b).

Rather than using the full $140,000 in personal loans, Respondents based their calculation on the net amount of personal expenditures. By subtracting the $50,000

repayment from the $140,000 total that Smith had loaned his campaign and using the net amount of $90,000 as variable "b" in calculating the OPFA, Respondents concluded that the OPFA was $361,000, which would allow Mr. Smith to accept increased contribution limits under the millionaires' provision.[7] Resp. at 4.

Bradley Smith himself called RAD on June 10, 2004, and RAD's telephone log notes that Respondents had a question about whether they were allowed to subtract the repayment from Smith's loans to his Committee in calculating the OPFA. The RAD analyst informed Respondents that she would have to research the issue and would not be able to call Respondents back until June 15, 2004.[8] Respondents, however, did not wait for RAD to call them back before accepting contributions under the increased limits on June 10, 2004. Respondents completed the FEC Form 11 on June 11, 2004. The form was received by the Commission on June 15, 2004. RAD was not able to reach Respondents when RAD attempted to call back on June 15, 2004. Respondents did not contact RAD again about their eligibility for higher limits.[9]

Complainant argues that Mr. Smith was not entitled to accept increased contribution limits, because the OPFA should have been calculated using the greatest aggregate of Mr. Smith's loans to his campaign, or $140,000. If the OPFA had been calculated using $140,000 as Mr. Smith's greatest aggregate amount of personal

[7] As noted above, the $50,000 repayment actually was made 3 days after the date on which the DeRossett campaign filed its Form 10 that Respondents claim to not have received.

[8] June 10, 2004 was a Thursday, and the RAD analyst had a pre-planned absence on June 14, 2004.

[9] It appears that RAD also did not try to contact the Smith campaign after the attempt to reach them on June 15, 2004.

expenditures for his campaign, the OPFA would have been $311,000. The amount of $311,000 is below the threshold amount of $350,000 required by the law; therefore, Complainant argues, Mr. Smith was not permitted to accept contributions under the increased limits in 2 U.S.C. § 441a-1(a)(1).

2. Greatest Aggregate Amount of Expenditures from Personal Funds

Respondents attempt to draw a distinction between the use of the term "greatest aggregate amount" in the description of the opposing candidate's expenditures from personal funds in 2 U.S.C. § 441a-1(a)(2)(A)(i) and the use of the term "aggregate amount" in the description of the candidate's expenditures from personal funds in 2 U.S.C. § 441a-1(a)(2)(A)(ii) to argue that the formula established by the implementing regulations, which requires the use of the greatest aggregate amount for both variables "a" and "b," is invalid.[10] Resp. at 5. As discussed below, this distinction in the statutory language appears to be meaningless. Further, and more importantly, the implementing regulations[11] and the Commission's subsequent interpretation do not support subtracting repaid loans from the formula used to calculate the OPFA. *See* Advisory Opinion 2003-

[10] A search of the legislative history surrounding the passage of the Bipartisan Campaign Reform Act of 2002 reveals no discussion of why the drafters of the legislation chose to use "greatest aggregate" in one part and "aggregate" in another. The Explanation and Justification for the Commission's Interim Final Rules on the millionaires' amendment clearly indicates that both the opposing candidate and the candidate's personal expenditures are to be calculated the same and even provide examples in which both candidate's expenditures are determined in the aggregate. 68 Fed. Reg. 3970 (Jan. 27, 2003). Finally, in the Commission's February 2003 publication of the Record, the interim final rules implementing the millionaires' amendment were summarized. In summarizing the calculation of the OPFA with the "a-b" formula, the article states that "a = opponent's personal funds spending" and "b = candidate's personal funds spending." This summarization further indicates that the two are to be calculated the same. Federal Election Commission, Record, Vol. 29/No. 2 (Feb. 2003).

[11] 11 C.F.R. §§ 400.4, 400.10(b).

31. Therefore, Respondents were not permitted to deduct the $50,000 repayment from the "greatest aggregate amount of expenditures from personal funds made by the candidate" in calculating the OPFA.

The Act and the regulations speak in terms of "aggregate" expenditures, not "net" expenditures. In fact, the regulations state that "an expenditure from personal funds shall be considered to be made on the date the funds are deposited into the account designated by the candidate's authorized committee as the campaign depository, ..., on the date the instrument transferring the funds is signed, or on the date the contract obligating the personal funds is executed, whichever is earlier." 11 C.F.R. § 400.4(b). Thus, it would appear that Smith made "an expenditure from personal funds" on September 30, 2003 when he lent his Committee $100,000 and again on March 31, 2004 when he lent his campaign $40,000.

The Commission previously considered "expenditures from personal funds" in the context of the millionaires' amendment in Advisory Opinion 2003-31. In the so-called Dayton AO, the Commission confronted the analogous situation of a candidate who stated that he did not intend to make personal expenditures in excess of the threshold amount but did intend to personally incur expenses on behalf of his own campaign for which he expected to be reimbursed. He asked whether, even after reimbursement, the advances would "permanently constitute an 'expenditure from personal funds' within the meaning of the Millionaires' Amendment."

The Commission concluded that "Senator Dayton's payments from personal funds for the campaign expenses listed [in his advisory opinion request], will be both

expenditures and contributions ... and thus will constitute expenditures from personal funds within the meaning of the Millionaire's Amendment." The Commission concluded "the fact that Senator Dayton may subsequently receive reimbursement from the Committee for these expenses does not change their character as expenditures from personal funds. Neither the Millionaire's Amendment nor the Commission rules and forms implementing it contemplate reductions in expenditures from personal funds." In other words, Senator Dayton could not "back out" the reimbursed expenses from his "greatest aggregate amount of expenditures from personal funds" even after receiving the reimbursement.

In reaching this conclusion, the Commission determined "the OPFA is calculated using the 'aggregate amount[s]' of expenditures from personal funds for the candidate and the opposing candidate ... The word 'aggregate' used as an adjective is defined as a whole, 'or sum; total; combined' as compared with the adjective 'net' defined as 'remaining after deductions ...' The Random House Dictionary of the English Language, The Unabridged Edition (1983); see also Bryan A. Garner, A Dictionary of Modern Legal Usage (2d ed. 1995)." The AO goes on to state:

> In addition, Congress provided in one of the variables used for OPFA calculation for the subtraction of candidate contributions from personal funds. 2 U.S.C. 441a(i)(1)(E)(ii) [also 2 U.S.C. 441a-1(a)(2)(B)(ii)] (definition of "gross receipts advantage"). Congress did not make a similar provision for the subtraction of any amounts in the variables for the "[g]reatest aggregate amount of expenditures from personal funds" made by the candidate or opposing candidate. 2 U.S.C. 441a(i)(1)(D)(i) and (ii) [also 2 U.S.C. 441a-1(a)(2)(A)(i) and (ii)]; see also 11 CFR 400.10(b) (variables a through f).

A.O. 2003-31.

Thus, like Senator Dayton, Mr. Smith's "greatest aggregate amount of expenditures from personal funds" included <u>all</u> the expenditures he made on behalf of his campaign, or $140,000. Accordingly, the OPFA is:

$$451{,}000 - 140{,}000 = 311{,}000.$$

Because the correct OPFA is less than $350,000, Respondents were never entitled to receive increased contribution limits under 2 U.S.C. § 441a-1(a). As a result, the Commission finds reason to believe Brad Smith for Congress and James Bailey, in his official capacity as Treasurer, and Bradley Smith, in his personal capacity as candidate, violated 2 U.S.C. § 441a(f) by accepting $40,500 in excessive contributions, as detailed on Attachment 1.

Excessive Contributions of $6,000

Date	Name	Contribution Amount	Excessive Amount
6/10/2004	Lobkowicz, Philip	$6,000.00	$4,000.00
6/14/2004	Capra, James	$6,000.00	$4,000.00
6/18/2004	Daniels, George	$6,000.00	$4,000.00
6/18/2004	Kohler, Terry	$6,000.00	$4,000.00
6/18/2004	Smeads, Larry	$6,000.00	$4,000.00
6/18/2004	Sinquefield Rex	$6,000.00	$4,000.00
6/30/2004	Sinquefield, Jeanne	$6,000.00	$4,000.00
7/30/2004	Rhodes, Thomas	$6,000.00	$4,000.00
8/2/2004	Searle, Dan	$6,000.00	$4,000.00
Totals		**$54,000.00**	**$36,000.00**

Excessive Contributions - More than $2,000

Date	Name	Contribution Amount	Excessive Amount
6/30/2004	Beznos, Harold	$2,500.00	$500.00
7/27/2004	Smith, Diane	$4,000.00	$2,000.00
7/30/2004	Conner, Barry	$2,000.00	
7/30/2004	Conner, Barry	$2,000.00	$2,000.00
Totals		**$10,500.00**	**$4,500.00**
		$64,500.00	**$40,500.00**