



FEDERAL ELECTION COMMISSION  
WASHINGTON, D.C. 20463

July 18, 2011

**MEMORANDUM**

**TO:** Patricia Carmona  
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**SUBJECT:** Proposed Interim Audit Report on the Colorado Republican Federal Campaign Committee (LRA 827)

**I. INTRODUCTION**

The Office of the General Counsel has reviewed the proposed Interim Audit Report (“IAR”) on the Colorado Republican Federal Campaign Committee (“the Committee”).<sup>1</sup> Our comments address issues pertaining to the Committee’s allocation account as presented in Finding 1 (Misstatement of Financial Activity) and Finding 2 (Allocation of Expenditures), and the Committee’s disclosure of disbursements as presented in Finding 3 (Disclosure of Disbursements). We concur with any findings not specifically discussed in this memorandum. If you have any questions, please contact Allison T. Steinle, the attorney assigned to this audit.

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<sup>1</sup> We recommend that the Commission consider this document in Executive Session because the Commission may eventually decide to pursue an investigation of matters contained in the proposed IAR. 11 C.F.R. §§ 2.4(a) and (b)(6).

## **II. FINDING 1 (MISSTATEMENT OF FINANCIAL ACTIVITY) AND FINDING 2 (ALLOCATION OF EXPENDITURES)**

The Committee maintained five federal bank accounts and three non-federal bank accounts in 2007 and 2008. We understand that the Committee labeled one of these federal accounts as an "allocation account," and to date has not indicated that the account was originally intended to function as anything other than an allocation account established pursuant to 11 C.F.R. § 106.7. However, the Committee not only used this account to pay for allocable expenses during the audit period, but also paid for \$2,893,303 in 100% federal activity and \$19,000 in 100% non-federal activity out of the allocation account. The disbursements out of the account included, but were not limited to, disbursements for payroll, legal fees, mailers, and consulting services. The Committee also not only transferred funds into the allocation account from the other federal and non-federal accounts, but also made \$147,830 in transfers back out of the allocation account to other federal accounts.

Finding 2 of the proposed IAR concludes that these transactions resulted in an overfunding of the allocation account in the amount of \$131,725. In addition, it is our understanding that the Committee failed to report at least some of the 100% non-federal activity paid out of the allocation account, and Finding 1 of the proposed IAR includes these amounts in its misstatement calculation. The proposed IAR, however, does not explicitly state that the Committee's failure to report these amounts is included in the misstatement amount, nor does it state the exact amounts that the Committee failed to report out of the allocation account.

We agree with the Audit Division that the Committee overfunded the account by transferring more funds from the non-federal accounts than were needed to cover the non-federal share of the Committee's allocable activity. We also agree with the Audit Division that any activity not reported out of the allocation account should be included in the misstatement amount.

We recommend, however, that Finding 2 of the proposed IAR also conclude that the Committee impermissibly transferred funds from its non-federal account to pay for non-allocable activity, and impermissibly paid for 100% non-federal activity out of its allocation account. The Commission's regulations prohibit committees from transferring funds from a non-federal account to reimburse a federal account for non-allocable activity. 11 C.F.R. §§ 102.5(a), 106.7(f)(1). The Commission's regulations also permit committees to use allocation accounts "solely for the purpose of paying the allocable expenses of joint federal and non-federal activities." 11 C.F.R. § 106.7(f)(1)(ii). An expense payable with 100% non-federal funds is, by definition, not allocable, and thus transfers of non-federal funds to a federal account and payment of 100% non-federal expenses thereafter by the federal account are not permissible.<sup>2</sup>

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<sup>2</sup> We note that that under a strict reading of 11 C.F.R. § 106.7(f)(1)(ii), the Committee was also prohibited from using the allocation account to pay for the 100% federal activity using 100% federal funds. However, had the Committee paid for the 100% federal activity out of a federal operating account also used to pay for allocable activity pursuant to 106.7(f)(1)(i), as opposed to an allocation account established pursuant to 106.7(f)(1)(ii), it could have done so as long as the 100% federal activity was not funded by non-federal funds. *See* 11 C.F.R. §§ 102.5(a), 106.7(f)(1)(i). Therefore, we read 11 C.F.R. § 106.7(f)(1)(i) and (ii) together to only prohibit the transfer of non-federal funds and the payment of 100% non-federal expenses thereafter.

We also recommend that Finding 1 of the proposed IAR clarify that the Committee was required to report all activity in the allocation account, including the 100% non-federal activity, and state the exact amounts that the Committee failed to report out of the allocation account. Allocation accounts permit state party committees to mix funds from a committee's federal and non-federal operating accounts to pay allocable expenses, but are considered federal accounts from which that committee must report all activity, including the non-federal portion of activity. See 11 C.F.R. §§ 104.17, 106.7(f); Explanation and Justification for Methods of Allocation between Federal and Non-Federal Accounts, 55 Fed. Reg. 26,058, 26,065-66 (June 26, 1990). This reporting requirement allows the Commission to verify that committees are transferring and using the proper amount of non-federal funds to pay for non-allocable non-federal activities, and do not use non-federal funds to subsidize federal activities. See 55 Fed. Reg. at 26,066 (noting that a reporting requirement "allow[s] the Commission to track the flow of non-federal funds into federal accounts, and [] ensure[s] that the use of such funds is strictly limited to payment for the non-federal share of allocable activities").

Finally, we note that two ongoing audits, the Georgia Federal Elections Committee ("GFEC") audit and the Minnesota Democratic Farmer-Labor Party ("MDFLP") audit, address similar, but not identical, issues. Both those audits involve payments for 100% federal activity and 100% non-federal activity out of so-called "payroll escrow" accounts, which in some ways resemble allocation accounts.<sup>3</sup> However, we do not believe that these pending audits affect the legal analysis in this case. We do not understand the Commission to have expressed any views as to the regulatory requirements for actual allocation accounts, which were not at issue in either the GFEC audit or the MDFLP audit, or as to the regulatory requirements for the payment of allocable expenses from federal accounts for committees that choose to pay their allocable expenses in that method. As noted above, to our knowledge, the allocation account here was an actual allocation account established pursuant to 11 C.F.R. § 106.7, and not as a payroll escrow

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<sup>3</sup> Specifically, the two committees in question established payroll escrow accounts to ease their administrative payroll processing burden. The payroll escrow accounts were funded by transfers from the committees' federal and non-federal operating accounts. The committees then made 100% federal, 100% non-federal, and allocable payroll disbursements for salary and taxes from the payroll escrow accounts. The committees did not disclose any non-federal activity associated with the payroll escrow accounts. In the GFEC audit, the committee asserted that its payroll escrow account was neither a federal account nor an allocation account, and thus stated that it was not required to report the account's non-federal activity. In response to the Audit Division's Recommendation Memorandum in that case, three Commissioners voted to conclude that the committee's payroll escrow account "did not violate the Act or Commission regulations" because it was "not an allocation account established pursuant to 11 C.F.R. § 106.7 to pay for allocable activities, but rather was a pass-through escrow account established to accommodate GFEC's payroll vendor and used for non-allocable disbursement . . . and the 'functional equivalent' of an allocation account is not a cognizable legal concept under the Act or Commission regulations." See Motion #1, Proposed Audit Division Recommendation Memorandum on the Georgia Federal Elections Committee (A07-14) (Mar. 3, 2011). While that motion was not adopted, the Commission voted unanimously to not require the Georgia committee to "further amend its reports in relation to the transactions involving the payroll escrow account." See Motion #4, Proposed Audit Division Recommendation Memorandum on the Georgia Federal Elections Committee (A07-14) (Mar. 3, 2011). Our comments on the proposed IAR on MDFLP conclude that it is unclear whether the MDFLP's payroll escrow account is legally distinguishable from the payroll escrow account in the GFEC audit, and recommend that the Audit Division raise the issue in the cover memorandum that forwards the audit report to the Commission. See Legal Analysis Memorandum to the Audit Division, Proposed Interim Audit Report on the Minnesota Democratic Farmer-Labor Party (LRA 835) (July 11, 2011).

account used exclusively to pay salary and taxes. Instead, it appears that this was an allocation account that was simply mismanaged.

### III. FINDING 3 (DISCLOSURE OF DISBURSMENTS)

We understand that the Committee reported a number of expenditures out of its federal accounts as Federal Election Activity ("FEA") on Schedule B, Line 30(b), but did not report these expenditures as being on behalf of one or more clearly identified candidates. In response to pre-audit Requests for Additional Information ("RFAs") from the Reports Analysis Division ("RAD"), the Committee indicated that these expenditures were related to absentee ballots and get-out-the-vote ("GOTV") activity and were not made on behalf of one or more clearly identified candidates. During audit fieldwork, the Committee provided the Audit staff with the same response, and provided them with a file of printed materials and robocall scripts that the Committee claimed were attributable to the expenditures in question. Some, but not all, of these printed materials and robocall scripts identify one or more clearly identified candidates, and many contained voter registration information. The Audit staff, however, was unable to tie the printed materials and robocall scripts provided by the Committee to any specific invoice or expenditure for review.

Finding 3 of the proposed IAR concludes that \$2,626,468 of these expenditures reported by the Committee as FEA were missing the identification of a specific candidate supported or opposed. The proposed IAR, however, does not explicitly state that the Audit staff was unable to tie the printed materials provided by the Committee to any specific invoice or expenditure for review.

FEA means four types of federal expenses that meet certain requirements: (1) voter registration activity within 120 days of the federal election ("Type I FEA"); (2) voter identification, generic campaign activity, or GOTV activity in connection with an election where a federal candidate is on the ballot ("Type II FEA"); (3) a public communication that refers to a clearly identified federal candidate and promotes or supports or attacks or opposes ("PASO") a federal candidate ("Type III FEA"); or (4) services of a state or local party committee employee who spends more than 25% of compensated time during a month on activities in connection with a federal election ("Type IV FEA"). See 2 U.S.C. § 431(20); 11 C.F.R. § 100.24. Not all of these types of FEA are made on behalf of a specific candidate, and some may qualify for exemptions. See 11 C.F.R. §§ 100.24, 100.149, 300.36.

Therefore, we do not agree that there is sufficient information to conclude that all of these expenses were missing the identification of a specific candidate supported or opposed. In particular, we note that while Type I and Type II FEA that does not refer to a clearly identified candidate may be paid with a mixture of federal and Levin funds, a state committee always has the option of paying for such generic activity with 100% federal funds, and if it does so, there obviously is no specific candidate to identify as supported or opposed. See 2 U.S.C. § 441i(b)(2)(B)(i). More information than we have here is needed to support an audit finding that an expense was made on behalf of one or more clearly identified candidates and must be disclosed as such. If the expenses were for public communications that referred to a clearly identified candidate for federal office, and promoted, supported, attacked, or opposed a candidate

for that office, they would be Type III FEA, and the Committee would be required to report the identification of the specific candidate supported or opposed. *See* 2 U.S.C. § 431(20); 11 C.F.R. §§ 100.24, 104.17(a). But since the materials provided by the Committee cannot be tied to any specific invoice or expenditure for review, it is not possible to examine each expense to determine whether it was properly reported. Without this link, it would also be difficult to determine whether the reported expense constituted Type II FEA for voter identification, generic campaign activity or GOTV, or whether any exemptions apply. *See* Legal Analysis Memorandum to the Audit Division, Proposed Interim Audit Report on the Maine Republican Party (LRA 817) (Dec. 17, 2010); Legal Analysis Memorandum to the Audit Division, Proposed Audit Division Recommendation Memorandum on the Kansas Republican Party (LRA 801) (Oct. 5, 2010).

To address this situation, we recommend that Finding 3 of the proposed IAR clarify that the Audit staff was unable to tie the printed materials and robocall scripts provided by the Committee to any specific invoice or expenditure for review. We also recommend that the expenses for printed materials and robocalls that are unavailable for review should not be categorized as FEA made on behalf of one or more clearly identified candidates. Instead, they should be treated in the report as a separate category of apparent federal expenses for which the Committee has not provided sufficient documentation to clarify that the disbursements were properly reported. This approach is consistent with our advice concerning similar undocumented expenses in the Maine Republican Party audit and the Kansas Republican Party audit. *See* Legal Analysis Memorandum to the Audit Division, Proposed Interim Audit Report on the Maine Republican Party (LRA 817) (Dec. 17, 2010); Legal Analysis Memorandum to the Audit Division, Proposed Audit Division Recommendation Memorandum on the Kansas Republican Party (LRA 801) (Oct. 5, 2010). Because this audit is only at the IAR stage, the Committee may help resolve this issue by providing information from its vendors or other sources that will tie the printed materials and robocall scripts to specific invoices.