SANDLER, REIFF & YOUNG, P.C.

50 E STREET, S.E., SUITE 300
WASHINGTON, DC 20003

JOSEPH E. SANDLER
sandler@sandlerreiff.com
NEIL P. REIFF
reiff@sandlerreiff.com

COUNSEL:
JOHN HARDIN YOUNG
young@sandlerreiff.com

TELEPHONE: (202) 479-1111
FACSIMILE: (202) 479-1115

June 3, 2005

Via Email

Mai T. Dinh, Esq.
Acting Assistant General Counsel
Federal Election Commission
999 E Street, N.W.
Washington, D.C. 20463

Re: Notice of Proposed Rulemaking: State, District and Local Party Committee Payment of Certain Salaries and Wages

Dear Ms. Dinh:

These comments are submitted in response to the Commission's above-referenced Notice of Proposed Rulemaking, 70 *Fed. Reg.* 23072 (May 4, 2005), proposing amendments to the Commission's regulations relating to the payment of salaries and wages by state and local party committees. These comments are being provided in our personal capacity as attorneys who represent more than thirty state and local Democratic Party committees; these comments do not necessarily represent the views of any particular client.

In the event the Commission determines that a hearing will be held on these proposed rules, the undersigned request an opportunity to testify at that hearing.

This rulemaking is being undertaken in response to the decision in *Shays v. Federal Election Commission*, 337 F.Supp.2d 28 (D.D.C. 2004). In that case, the District Court , *inter alia*, set aside the Commission's current regulations (11 CFR §§106.7(c)(1) & 300.33(c)(2)), which require state parties to pay salaries and wages for employees who do not work in excess of 25% on federal elections within a single month solely with funds that comply with state law. *Shays*, 337 F. Supp at 114.

As a threshold matter, since the Commission has appealed both the procedural and substantive basis for the District Court's decision and order, the Commission should hold this rulemaking in abeyance until all judicial proceedings related to this issue are concluded.

To the extent that the Commission is ultimately required to amend its regulations regarding the salaries and wages of state and local party employees, the following points should be considered:

1) Allocation ratio to be applied to employees who work 25% or less of any given month in connection with federal elections and federal election activities.

The Commission has proposed that state party committees pay the salaries and wages of employees who work 25% or less of a given month on federal elections, utilizing a fixed ratio of 25% federally permissible funds/75% non-federal funds. While we believe that this would be a fair ratio for employees working in a presidential election cycle, it does not make sense to impose this ratio in other cycles. In the NPRM, the Commission notes that, "prior to the BCRA, salaries and wages of State party committees' employees were considered administrative expenses that were allocated based on ballot composition." 70 *Fed. Reg.* at 23073. Consistent with that principle, the Commission should utilize the otherwise applicable fixed minimum percentage for salary and wage expenses in an election cycle where there is no presidential election. Thus, a state or local party committee would pay a minimum of 15 or 21% federal for such expenses depending on whether that state had a Senate race during the election cycle. In a presidential cycle, the use of the 25% ratio would be appropriate, since the otherwise applicable minimum percentages (28% and 36%) exceed the 25% time threshold. Finally, the Commission should incorporate into its regulations its comment made in footnote 4 on page 23073 of its NPRM, to the effect that that employees who do not spend any time in a given month on Federal election related activities can, as under the existing regulation, be paid entirely with non-federal funds.

We would also support, as an optional alternative, the Commission's proposal to establish an allocation ratio that is directly proportional to the employees' time spent in connection with federal elections in a given month. This option would be fully responsive to the concerns of the District Court about "potential abuse," since the percentage of an employee's salary a state party committee would be required to pay in federal funds would match the actual percentage of time spent by that employee in connection with federal elections. However, as a matter of recordkeeping and reporting, this method would be quite difficult to track and report and should only be made

available as an option for party committees—not as a required method. We assume that the Commission only intends to permit this method for employees who do not exceed the 25% federal threshold in any given month.

2) Methods for allocating fringe benefits of employees

The Commission requests comment on whether it should afford to state and local party committees the option of treating fringe benefits, for purposes of the allocation regulations, as either a salary expense *or* as an administrative expense. This issue was raised in Advisory Opinion 2003-11, in which the Commission ruled that such fringe benefits were to be treated, for this purpose, as salary and wages rather than as administrative expenses. In connection with that Advisory Opinion Request, our firm (along with Charles Spies) submitted comments to the Commission suggesting that committees should have the option of treating fringe benefit payments as either a salary or wage expense or as an administrative expense.

In that comment, we suggested that requiring state parties to treat fringe benefit payments as salaries and wages creates several practical problems. First, prior to issuance of the AO, Commission staff initially advised the regulated community that such expenses were in fact administrative expenses. Second, requiring the payment of such expenses as salaries and wages creates a difficult administrative problem for state parties because such expenses are often required to be paid on behalf of the employee *prior* to the month for which the 25% determination must be made. Third, many fringe benefit expenses are not billed on a monthly basis, but rather, on a quarterly or annual basis.

Based upon our experience subsequent to the issuance of Advisory Opinion 2003-11, party committees have, in fact, struggled with determining how to pay for such expenses. For example, we are aware of several instances where committees would pay for an employee's health insurance with federal funds, only to find out that the employee did not work in excess of 25% of their time in connection with federal elections. Under the Commission's current regulations, there is no mechanism to recoup the lost federal funds in such a case. Furthermore, based upon other proposed modifications to the salary and wage rules, such expenditures, if required to be paid for solely as a salary and wage expenses would be required to be paid for with an unduly high amount of federal dollars. Accordingly, we urge the Commission to amend its rules to permit the payment of fringe benefits, at the option of the state party committee, as either an administrative expense or as a salary and wage expense.

3) Payment of Fundraising Expenses

The Commission requests comments on whether it should revise section 106.7(c)(4) to be consistent with Advisory Opinion 2004-12. In that AO, the Commission decided that, if a state party raises federal and non-federal funds in a single event, and pays the expenses on a funds received method, the federal funds raised may be spent on Federal election activity. We believe that the same principle should apply to events that raise Levin funds as well, as long as federal or Levin funds are used to pay for the percentage of fundraising expenses attributable to Levin funds on a funds received basis. We believe that this approach is consistent with the BCRA in that any funds that are raised that are used in connection with federal election activities will be paid for with either Federal or Levin funds. Furthermore, this methodology ensures that the federal portion of funds raised for such activities are paid for with federal funds. Of course, any non-federal proceeds that were raised by spending non-federal funds for that portion of the fundraising activity would not be eligible for use in connection with federal election activities.

Therefore, a strict reading of the Commission's initial regulation caused an unduly burdensome and unfair condition for state parties in that federal dollars, for which the federal portion of such costs of raising such funds were properly paid for with federal funds, could not be used in connection with federal election activities. Essentially, this would have required state parties to pay all of its fundraising expenses with federal dollars since compliance with the strict reading of the regulation would be next to impossible. The Commission appeared to recognize the unintended consequence of the language of its regulations and, in AO 2004-12, ruled that it was the intent of the Commission to permit state parties to pay for the costs of all fundraising events on a funds received method without otherwise undermining a party committee's ability to use federal funds raised at such events for Federal election activities.

Ultimately, the Commission's position in that advisory opinion mandates conforming amendments to the Commission's regulations in several places. In that regard, we suggest the following amendments to the Commission's regulations:

11 C.F.R. § 106.7(c)(4) – *Certain fundraising costs.* State, district, and local party committees may allocate the direct costs of certain fundraising programs or events between their Federal, Levin and non-federal accounts provided that any non-federal proceeds from the activities or events will ever be used for Federal election activities if such funds were raised through the use of non-federal funds to pay for the direct fundraising costs of raising such non-federal funds. Direct costs of fundraising include

disbursements for the planning and administration of specific fundraising events or programs. Such non-federal funds may not be commingled with Levin funds.

Add new section 106.7(c)(4)(iii) – Any non-federal funds which are raised in connection with events or programs for which the costs are allocated pursuant to this section may not be designated as Levin funds or otherwise be used in connection with any federal election activities.

11 C.F.R. § 106.7(e)(4) – *Fundraising Costs.* Expenses incurred by State, district, and local party committees directly related to programs or events undertaken to raise funds to be used, in whole or in part, for activities in connection with Federal and non-Federal elections that are Federal election activities pursuant to 11 CFR 100.24 should be allocated as provided in 11 CFR 300.32(a)(4).

11 C.F.R. § 300.32(a)(4) - State, district, and local party committees that raise Levin funds to be used, in whole or in part, for Federal election activity must pay the direct costs of such fundraising with either Federal or Levin funds in accordance with 11 CFR 300.33(c)(3). The direct costs of a fundraising program or event include expenses for the solicitation of funds and for the planning and administration of actual fundraising programs and events.

11 C.F.R. § 300.33(c)(3) – *Fundraising costs* for Federal, Levin and non-Federal accounts. If Federal, Levin and non-Federal funds are collected by a State, district, or local party committee through a fundraising activity, that raises Federal and Levin or Federal, Levin and non-Federal funds, that committee must allocate its direct fundraising costs using the funds received method and according to the following procedures:

(i) The committee must allocate its fundraising costs based on the ratio of funds received into its Federal, Levin and non-federal accounts to its total receipts from each fundraising program or event. This ratio shall be estimated prior to each such program or event based upon the committee's reasonable prediction of its Federal, Levin and non-Federal revenue from that program or event, and must be noted in the committee's report for the period in which the first disbursement for such program or event occurred, submitted pursuant to 11 CFR 104.5. Any disbursements for fundraising costs made prior to the actual program or event must be allocated according to this estimated ratio.

(ii) No later than the date 60 days after each fundraising program or event from which Federal, Levin and non-Federal funds are collected, the committee shall adjust the allocation ratio for that program or event to reflect the actual ratio of funds received. If the Levin or non-Federal account has paid less than its allocable share, the committee shall transfer funds from its Federal to its Levin or non-Federal account, or Levin to non-Federal account, as necessary, to reflect the adjusted

allocation ratio. If the Federal or Levin account has paid more than its allocable share, the committee shall make any transfers of funds from its Levin or non-Federal to its Federal or Levin account to reflect the adjusted allocation ratio within the 60-day time period established by this paragraph. The committee shall make note of any such adjustments and transfers in its report for any period in which a transfer was made, and shall also report the date of the fundraising program or event that serves as the basis for the transfer. In the case of a telemarketing or direct mail campaign, the date for purposes of this paragraph is the last day of the telemarketing campaign, or the day on which the final direct mail solicitations are mailed.

(iii) Any non-federal funds raised pursuant to this section may not be designated as Levin funds, or otherwise be used in connection with any federal election activities if the costs of raising such funds were paid for with non-federal funds. Notwithstanding, any non-federal funds raised pursuant to this section may be designated as Levin funds as long as the costs of raising such funds were paid for with Federal or Levin funds.

It should be noted that our suggested regulatory changes apply a funds received method to section 300.33(c)(3). This would replace the current regulatory language which merely states that Federal and Levin funds used to pay for such fundraising activity. It has been our understanding through discussions with FEC Commissioners and staff that it was the intent to apply a funds received method to fundraising for Federal and Levin funds. The lack of clarity of the current regulation has been the cause of some confusion and the Commission should specifically adopt a funds received method in this section.

4) Other issues regarding Payroll Expenses

In addition to the issues specifically raised by the Commission in its NPRM, the Commission should take this opportunity to address and resolve certain other issues related to the payment of payroll related expenses by state and local party committees:

(a) State Party committees should be allowed to create a holding account to submit payroll expenses

It has been our experience that party committees have confronted several practical problems in the administration of payroll operations under the Commission s rules. One of the largest problems has been working with payroll companies to properly debit the party committee s accounts based upon the ever changing designations of staff between federal and non-federal funds. Generally, many payroll companies are only willing to debit one bank account at a time, and are not generally receptive to the constant shifting

of a particular employee between payments from a committee s federal and non-federal accounts. This problem is exacerbated when attempting to remit payroll taxes to federal, state and local authorities where most payroll companies will only accept one account to debit such expenses. Thus, party committees have been forced, on occasion, to create two separate payroll entities and are constantly shifting employees between those two entities.

In order to alleviate this problem, the Commission should explicitly authorize a state or local party committee to establish a single payroll holding account into which both federal and non-federal funds are deposited for the sole purpose of transmitting payroll through a payroll company. Of course, the federal portion of payroll would be subject to full disclosure on the committee s federal report, and the Commission should have the authority to examine the holding account s activities upon request.

(b) The Commission s regulations should contain guidance for the situation in which a party committee does not estimate the proper amount of time that an employee works on federal elections in a given month

One of the biggest challenges for payroll administration by state and local party committees has been the estimation of whether a particular employee will spend more or less than 25% of her time on activity in connection with a federal election in a given month. Since fringe benefits are required to be paid in advance, and since many state party committees pay its employees on a bi-weekly or semi-monthly schedule, committees are forced, in many cases, to guess whether a particular employee will spend more or less than the 25% of her time on the subject activity. In many cases, the committee s guess has proven wrong. However, the Commission has provided no guidance on how to remedy such a situation. For example, can a state or local party committee recoup federal funds if it incorrectly guesses that the employee will work in excess of 25% in that month? Does a committee violate 2 U.S.C. § 441(b) if it wrongly presumes that an employee will work less than 25% of the month on federal elections but then exceeds the threshold? Is there a safe harbor if the committee reimburses the non-federal account within a certain number of days after the end of a month? Can a state party committee make adjustments to a subsequent month s payroll to fix any incorrect estimates in a prior month? Consistent with the approach taken in 11 C.F.R. § 106.7(d)(4), the Commission should issue regulations permitting state and local party committees to make the appropriate adjustments, by way of transferring from the federal to non-federal account or vice-versa, in these circumstances.

(c) The Commission s regulations regarding the scope of staff salaries is broader than the statutory language and should be narrowed

For the purpose of determining when a staff member s time exceeds the 25% threshold, the Commission s regulations (11 C.F.R. §§ 106.7(c)(1) & 300.33(c)(2)) define the subject activity in terms broader than the language of BCRA itself. The statutory language only covers activities in connection with a Federal election. 2 U.S.C. § 431(20)(A)(iv). However, the Commission s regulations cover both activities in connection with a Federal election *and* Federal election activity. This is not an insignificant distinction. In connection with a Federal election is a legal term of art that covers only activities that directly influence a federal election, such as an activity that expressly advocates the election or defeat of a federal candidate or activities that result in an in-kind contribution to a federal candidate. On the other hand, Federal election activity covers activities that, in many cases, do not even reference a federal candidate.

For example, under the Commission s current regulations, if an employee spends the entire month developing a generic get-out-the-vote campaign, or on generic voter registration drive, her salary may be required to be paid for solely with federal funds even though the activities that she worked on did not even make reference to a federal candidate. In light of the revisions that are being made to the payment of salaries for employees in this rulemaking, the Commission should revise these provisions to mirror the statutory language by removing Federal election activity. If Congress intended this provision to include activities such as the examples we have listed, it could have specifically included Federal election activity in the statutory provision addressing payment of salary expenses by state and local party committees.

Respectfully submitted,

Joseph E. Sandler
Neil P. Reiff