



FEDERAL ELECTION COMMISSION
Washington, DC 20463

April 22, 1999

CERTIFIED MAIL
RETURN RECEIPT REQUESTED

ADVISORY OPINION 1999-8

Stephen J. Harmelin
Dilworth Paxon LLP
3200 Mellon Bank Center
1735 Market Street
Philadelphia, PA 19103-7595

Dear Mr. Harmelin:

This responds to your letters dated February 17 and March 16, 1999, as supplemented by your letters dated April 13 and April 15, on behalf of Citizens for Arlen Specter ("the Committee"), requesting an advisory opinion concerning the application of the Federal Election Campaign Act of 1971, as amended ("the Act"), and Commission regulations to the investment of Committee funds.

The Committee was the principal campaign committee of Senator Arlen Specter for his 1998 re-election campaign, and Senator Specter has so designated it for a possible 2004 re-election campaign. You are the Committee's treasurer, and do not anticipate any significant expenditures until 2003 when the Senator may seek re-election. Until recently, all funds remaining from the 1998 campaign were maintained in a Merrill Lynch money market account earning a return equivalent to the overnight interest rate paid on federal funds transactions. In view of the length of time the funds will be available for investment and the alternative opportunities available in today's economy, you have determined that the investment of the Committee's funds should be prudently diversified to extend to mutual funds and similar investments earning a substantially greater rate of return.

Accordingly, you are placing the Committee's excess funds with the Vanguard Group's family of mutual and bond funds, with the initial investment to be allocated

among Vanguard's Prime Money Market Fund, GNMA Fund, United States Growth Fund, Selected Value Fund, and Intermediate-Term Tax-Exempt Municipal Bond Fund. Based on your evaluation of market trends, you will determine the specific Vanguard funds in which to invest and the appropriate allocation of the investments.

You state that, to avoid any potential conflict of interest or appearance thereof, Senator Specter has instructed that, although the excess funds should be invested with Vanguard, neither he "nor members of his staff" should be informed of the specific Vanguard funds selected. You state, however, that the reporting of the investment fund returns will identify the specific fund that is the source of the return. You also state that no expenditure of the Committee will be made directly from the Vanguard investment account. You ask whether the Committee may invest funds in mutual or bond funds of the type described above.

The Act and Commission regulations require that each political committee designate at least one State bank, Federally chartered depository institution, or depository institution the accounts of which are insured by the Federal Deposit Insurance Corporation or the National Credit Union Administration, as its campaign depository. All funds received by a political committee must be deposited in the checking account or other accounts maintained in its campaign depository. 2 U.S.C. §432(h)(1); 11 CFR 103.2 and 103.3(a). No disbursements, other than petty cash, may be made by such committee except by check or similar draft drawn on those accounts. 2 U.S.C. §432(h)(1) and (2); 11 CFR 102.10 and 102.11.

Nevertheless, Commission regulations specifically provide that political committees may transfer funds from the depository for investment purposes. 11 CFR 103.3(a). Moreover, the regulations contemplate a variety of such investments in describing cash on hand to include "certificates of deposits, treasury bills and any other committee investments valued at cost," and in requiring that committees report other receipts "such as dividends and interest." 11 CFR 104.3(a)(1), (a)(3)(x), and (a)(4)(vi); see also 2 U.S.C. §434(b)(2)(J) and 434(b)(3)(G). In advisory opinions, the Commission has also permitted the investment of political committee funds in a variety of investment vehicles. These have included government securities and money market funds (Advisory Opinion 1997-6); a cash management account maintained by an investment and brokerage firm (which could contain money market funds, U.S. Government obligations, or other securities) (Advisory Opinion 1986-18); and "an open-end, diversified investment trust which is a professionally managed money market fund" (Advisory Opinion 1980-39).¹

The ability of a committee to transfer funds to other investment accounts is conditioned, however, by the requirement that these funds must be returned to the campaign depository account before they can be used to make expenditures. 11 CFR 103.3(a); Advisory Opinions 1997-6, 1986-18, and 1980-39. The Commission has

¹ See also Advisory Opinion 1975-41 in which the Commission permitted the investment of campaign funds in Government treasury notes.

narrowly modified this requirement with respect to interest or other income earned by and credited to a committee's investment accounts with a securities firm that is automatically and directly reinvested in the investments held in the account. Although such income should be reported as an "other receipt" by a committee to reflect when it is credited, the amounts do not need to be deposited in the campaign depository account in view of the fact that the reinvestment of funds is merely a conversion of one form of cash on hand to another, and not an expenditure. Advisory Opinion 1997-6.

Based on the foregoing, the Commission concludes that the Committee may invest its funds in the Vanguard Group's family of mutual and bond funds. In doing so, the Committee must comply with the disclosure and other relevant provisions of the Act and Commission regulations. The income from each of the investments, such as interest and dividends, must be disclosed in a timely manner, even if such income is directly reinvested as described above. Advisory Opinion 1997-6. In view of the fact that the specific funds in the Vanguard investment account (e.g., the United States Growth Fund, the Selected Value Fund) will be the payers of the dividends, interest, or other income, those are the entities that should be identified for itemization purposes.² In addition, no Committee disbursements may be made directly from the Vanguard account; the funds to be used must first be transferred to a Committee depository account. Neither the transfer of Committee funds to Vanguard nor the transfer of funds back to the depository account needs to be reported.

As a final matter, the Commission notes that you do not anticipate Committee payment of management fees or expenses in connection with the Vanguard investments. You state that the operating expenses of a fund are paid from the fund's gross returns before it calculates the net investment return to individual shareholders, and are thus reflected only in the share price. Therefore, from the perspective of a shareholder, the expenses are incurred on a pre-income basis and the shareholder does not pay such expenses. The Commission concludes that, in this situation, the Committee does not have to report what might be characterized as an allocable share of the expenses as an expenditure. See 2 U.S.C. §§434(b)(4)(A) and (5)(A); 11 CFR 104.3(b)(2)(i) and (4)(i). Because the fund is paying these expenses before the determination is made as to the amount of income credited to the Committee, this situation is distinguishable from a situation where a contribution by credit card is made and expenses are deducted by the credit card company or other processors. In those circumstances, the entire amount of the cardholder's transaction is a contribution even though the amount that the committee receives is reduced by the deducted expenses, and those expenses are reportable as operating expenses of the committee. See Advisory Opinions 1995-34 and 1991-1. In the situation here, to treat the allocable share of the fund's expenses as a Committee expenditure would, in essence, double the amount of the expenses.

² The Commission assumes that the Committee will receive periodic account statements from Vanguard which itemize the interest, dividends, or other returns for each of the various mutual and bond funds. The Commission also notes that the Committee is obligated to retain and preserve all such statements and similar records that show the interest, dividends, or other income credited to the account. 11 CFR 102.9 and 104.14(b); see also Advisory Opinion 1997-6, n.2.

The Commission expresses no opinion regarding any tax ramifications of the proposed activity or the application of any rules of the U.S. Senate to the activity because those issues are not within its jurisdiction.

This response constitutes an advisory opinion concerning application of the Act and Commission regulations to the specific transaction or activity set forth in your request. 2 U.S.C. §437f.

Sincerely,

(signed)

Scott E. Thomas
Chairman

Enclosures (AOs 1997-6, 1995-34, 1991-1, 1986-18, 1980-39, and 1975-41)