

101 (or something close to it) Best Practices to Manage Campaign Finances in Texas

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Campaign Finance Reporting in Texas is very important to our political system. It helps to ensure a sense of fair play in the election process. The principal brick in the foundation of the system is the requirement to disclose all campaign finance activity. This information sharing is very important for our system of government in Texas, as it shines a light on the integrity of our election system. We have to use good judgement to ensure we interpret and apply the rules correctly so we do not make mistakes.

The purpose of this white paper is to help Republican candidates, Republican elected officials, and the Republican Party adhere to the Texas Ethics Commission rules and avoid criticism that can contribute to losing elections. This paper is not an exhaustive list, but it is focused on the most common issues that can trip up a contender.

For candidates, or any other political entity in Texas, the first step after deciding to enter the arena is to file with **the Texas Ethics Commission (TEC), or your Local Filing Authority (LFA), and declare a Campaign Treasurer**. This form is important for the TEC, for once it is filed, it declares that you are a candidate and now have the right to collect donations for your campaign. This form also establishes the rule for you to keep good campaign reports and file your various campaign finance reports. For candidates and office holders, you are the responsible party for reporting, even when you appoint a treasurer. This is slightly different for PACs, as PAC treasurers are the responsible party for their organization.

Even though you are operating a Texas campaign you will likely need to **register with the IRS**. The failure for not filing correctly can mean that you have to pay taxes on the campaign donations received. When you launch your campaign, you will need to register and file **Form 8871** to declare to the IRS that you are an exempt political organization. However, this step is not required if donations do not exceed certain limits, which vary depending on the type of political organization that is formed. You also need to file **Form SS-4** to obtain an Employer Identification Number (EIN). An annual tax return must also be filed on **Form 990** (there are different versions depending on the amount of donations you receive). Form 990 is due the 15th day of the 5th month following the end of the fiscal year (it is possible for a political entity to use a non-calendar year as a fiscal year). At the end of the year, your campaign will need to issue **1099s** to certain required vendors (see IRS rules) who were paid

more than \$600 during the tax year. If you do not obtain **W-9s** (Request for Taxpayer Identification Number and Certification) from the applicable vendors, you will be required to withhold tax from the payments. Managing vendors can be problematic and is one task in particular where a bookkeeping service can provide very important assistance.

When thinking about campaign finance, the IRS, or Generally Accepted Accounting Principles (GAAP), it is important to remember that **TEC reporting generally does NOT balance like usual business world accounting records**. For example, what if a donor experiences fraud on one of his bank accounts, causing a bounced check. The donor replaces the check, which then clears. But for TEC reporting, both checks must be reported, even though one was not any good and the funds never received. In many ways, political campaigns must utilize an accounting system that enables you to remain compliant with the IRS rules, i.e., issuing 1099s. However, it is necessary to understand the subtle differences in reporting required by the TEC.

Make a plan to follow and manage the reporting requirements. Be sure you clearly understand the rules and how the filing process works for your particular race. Avoid the late-night worry and frustration of filling out the reports at the last minute and possibly making errors under such pressure.

Understand the filing requirements for your particular race. There are differences in filing requirements, dependent on the position you seek. For example, judicial candidates have to worry about contribution limits which apply *“in connection”* to a donor, not just *“from”* a particular donor. If you have to reject a donation, you need to complete the rejection during the reporting period, so you do not have to report an incorrect donation; otherwise your report will show an incorrect donation that will not be reflected as a rejection until the next reporting period. There are also windows of time when donations cannot be received that are much more expansive for judicial candidates when compared to legislative candidates.

Know where and how you need to file your campaign finance reports. While the rules are managed by the TEC, most filers are required to file locally. Make sure to understand clearly where you need to file and how you need to file, either electronically or on paper (many LFAs still require paper submissions). Unless you are a legislative candidate, you will generally file locally, unless your district crosses county lines. In that case, you will file with the TEC. If you file with the TEC, you will be required to file online, unless you are granted a waiver.

Know your filing schedule. Beyond the mid-year and annual reports, reports are required 30 days and 8 days before elections. Daily reports are required if contributions in excess of \$1,000 are received within 8 days of the election.

All pledges must be reported. Any promised donation, if agreed to be accepted, must be reported, even if not paid during the reporting cycle. Any pledges that are not accepted do not have to be reported, just like any donation that is received, but rejected, as long as the rejection occurs in the same reporting period as the pledge or donation is received.

If you are an officeholder, you need to carefully track officeholder contributions. Donations given with the intent to be used to offset costs incurred by the officeholder in performing the duties/activities of his or her office are not reimbursable with public money. Keep these funds in a separate bank account, and keeping a separate credit card to differentiate these particular items would be useful in filling out your campaign reports.

Put excess cash in a separate account that can only be accessed with 2 signatures. For campaigns large enough to warrant it, there should be 2 bank accounts set up. One account should fund day to day operations, paying campaign operating expenses. It should be noted that when you send checks, there is a chance that someone could possibly forge a check. By saving the largest amount of cash in a second account, where you do not normally write checks, you can reduce the risk of fraud. It is good practice to require 2 signatures to withdraw funds from this second account.

Candidates and officeholders should review all bank account activity. You should monitor all donations and expenses. While you should take advantage of available volunteer resources to help manage your campaign, as a candidate, officeholder, or county party official, you are the responsible party for ensuring the accepted donations are correctly deposited and for the expenses to be paid as approved.

Candidates and officeholders should review all online donation activity. Accepting donations online is a very powerful tool, but at the same time it decentralizes and dehumanizes the donation acceptance process. Monitoring all donations enables you to reject all donations you do not want to accept. By controlling your donation activity, you lessen the chance of causing a negative campaign issue and having to submit a report that shows one or more donations that should not have been accepted.

For credit card contributions, you must record donor Intent, even if you are charged a fee to accept a donation online or via a credit card terminal. The merchant service fee will need to be recorded as an expense. For example, if you have a website and you accept donations, a donor makes a \$100 contribution. However, you must pay a service fee of 3%, so your net contribution is \$97, with \$3 being retained by the website service provider and the credit card company. Your report needs to reflect \$100 for the contribution, and a \$3 expense for the merchant service fee.

Report all direct campaign expenditures (DCE). All such expenditures incurred with or without the approval of consent of the candidate or officeholder must be reported. The person or PAC who makes the DCE is the party responsible for reporting, but part of that reporting requirement is to send notice to the candidate or officeholder for his or her review. These notices must be included in the campaign finance report. Candidates or officeholders are not required to chase DCE statements, but are required to report them when received.

A candidate or officeholder may pay him or herself a reasonable reimbursement for the use of a personal asset for political purposes (*Ethics Advisory Opinion No. 347*). In practical purposes, this particular type of reimbursement usually applies to the use of a personal automobile for political campaign activities. The best method for reimbursement is to pay for the gas out of personal funds,

keeping detailed records of the miles driven, and file a reimbursement rate for a reasonable per mile charge. The TEC follows the IRS mileage rate when determining reasonableness. There are now many GPS-connected apps that record all miles driven and are considered acceptable recording-keeping tools for tracking miles driven and calculating mileage reimbursements.

Effective January 1, 2018, there is a new **Vendor Rule** that requires disclosure of all applicable services be disclosed, in particular when resold through a vendor (*Ethics Commission Rules §20.56*). For example, this rule means if your political consultant arranges print and mail services and billed you for it, then you must coordinate with them to obtain the information necessary to properly disclose the printing vendor expense. This new rule may suggest a change in operations, as it just might be easier from now on to pay these third-party vendors directly, instead of through your consultants. Paying these third-party vendors directly will help keep you informed about these arrangements, leading to better and more accurate reporting.

Find an attorney who specializes in elections laws. Having an attorney on retainer can be a key asset in helping to solve a difficult problem. A candidate should be sure to pick and retain an attorney early in the election process, as an attorney has to manage conflicts of interest in his practice and will not be able to work for every campaign. Every campaign needs a lawyer well versed in election law and available when needed.

Corporate contributions, monetary and in-kind, are strictly prohibited and include for-profit, non-profit corporations, and labor unions. In general, it is okay to accept contributions from **Professional Corporates (PCs) and Professional Associations (PAs)**. **While Limited Liability Companies (LLCs) and Limited Partnerships (LPs) are okay as long** as there are no corporate partners, and they file their Federal tax returns as partnerships. If they file as an S corporation, that would make them ineligible to make political contributions. These criteria can be hard to verify; be very wary of donations from these entities. If you are in doubt, do not hesitate to ask the contributor what type of business it is, so you have the information necessary to make an informed decision. You can also check certain company formation information with the Texas Secretary of State.

All non-monetary contributions must be reported, also known as in-kind contributions. For example, often donors contribute goods and/or services such as yard signs, bumper stickers, printing services, office space, food and drinks, supplies, discounts on services, etc. For in-kind contributions, you must report such donations at their fair market value. Also, you must report an expenditure for these items, so the report balances. In other words, you must record these items as in-and-out transactions.

All personal funds deposited into the campaign account are considered a loan to a campaign. A candidate's personal money given to the campaign needs to be reported as a loan, even if it is not expected to be repaid. Donations are from outside parties, not from candidates.

Don't wait until the last minute to track donations and expenses. Take the sage advice of **Benjamin Franklin** who said, "*By failing to prepare, you are preparing to fail.*" It is overly stressful to gather the necessary information when the filing deadline is approaching. Often calls to donors or vendors are required to verify the necessary information. When you are tired and stressed, it is easy to make

mistakes. Instead of waiting to draft reports when the deadline is approaching, this is where a bookkeeping service can provide ongoing data collection as the campaign progresses, data that is both accurate and timely.

Other tips to bear in mind when contemplating campaign finance filing:

- **Don't wait until the last second to file your report.** Avoid stress and give yourself some room with the deadline to ensure you can handle any technical issues that you encounter when filing.
- **The TEC staff is there to help.** Utilize them to help, they are a great resource. However, they are barred from preparing your report, as all government employees are.
- **Attend a TEC seminar** to learn more about the rules of campaign finance reporting.
- **Judicial candidates need to take particular care**, as the reporting rules and requirements are generally more onerous and have more limitations.
- **Hold the keys to the checkbook very tightly – Treasury Management 101.** When managing your expenditures, set up intentional bottlenecks and second signature checks, to ensure you do not make it easy for unscrupulous people to commit fraud.
- **Anonymous contributions are never allowed.** In other words, never pass the hat. If you receive an anonymous contribution you may give it to a tax-exempt charity before the end of the reporting period.
- **Cash contributions are capped at \$100.**
- **There is a difference between receipt of a donation and acceptance of a donation.** You have until the end of a reporting period to reject any donation and return it. If you do not reject an item that should have been rejected before a report due date, the item must be disclosed in the report. You can report the rejection in the next report.
- **You cannot amend a report to enable a reimbursement to yourself.** You must make the decision whether or not the personal expenditure is reimbursable at time of filing. You can be subject to penalty if you try to amend a past report and reimburse yourself.
- **Do not hold fundraising events at the very end of a reporting period.** Give yourself breathing room to make wise decisions about accepting or rejecting donations.
- **Do not purchase personal property.**
- **Do not rent property from certain close relatives or one in which you as the candidate or officeholder have an interest.**
- **Do not pay your spouse or child out of political funds.** It is okay if paid out of *personal* funds, but you must disclose the political expenditure.
- **Do not accept contributions in the capitol or any extension building.**
- **Maintain all detailed records for at least 2 years from the filing deadline.**
- **If you are a local filer, you can still use the TEC website** to help create the report.
- If you lose your election, or decide to leave office and end your campaign, make sure to **file your Final Campaign Finance Report**. This action will advise the TEC that you are no longer required to submit reports.
- **Remember the itemization thresholds:** political contributions exceeding \$50 and political expenditures exceeding \$100, in aggregate, during the reporting period.

Use common sense. If you have to look in the mirror and ask if this is okay, then it is probably best to not to proceed. When dealing with ethics issues, steer the ship in a way to keep yourself out of trouble, now and in the future. It was **Ronald Reagan**, who said, ***“There are no easy answers, but there are simple answers. We must have the courage to do what we know is morally right.”***

Winning elections is difficult and managing the operations of a campaign is a stressful, challenging experience. You are dealing largely with volunteers and finding ones with the right experience or with the desire to work on certain “tedious” chores, like paperwork and recordkeeping, is not an easy task. A political bookkeeping service can be a vital resource in helping Republican candidates manage the finances of a campaign. Red Elephant Reports shares your same values and is in the business of helping the Texas GOP fulfill its obligations to the IRS and the TEC. We help to bring peace of mind by ensuring campaign finance reports are filed correctly, helping to avoid criticism. We use our financial and political experience to create customer-centric solutions to help Republican candidates and Republican county parties remain fully compliant with campaign finance reporting.

To find out more, visit GOPreports.com.

DISCLAIMER: this white paper does not constitute legal advice and if a candidate, county party official, elected office, or other interested reader has specific legal questions they should contact the TEC or an attorney.

Helpful Links:

Texas Ethics Commission Home Page

www.ethics.state.tx.us/index.html

Texas Ethics Commission Forms & Instructions

www.ethics.state.tx.us/main/forms.htm

Texas Ethics Commission Filing Schedules

www.ethics.state.tx.us/schedule/filing_schedules.htm

TEC Vendor Rule (To be effective 1/1/2018)

www.ethics.state.tx.us/rules/proposed_July_2017.html#Expends

IRS Tax Information for Political Organizations

www.irs.gov/charities-non-profits/political-organizations

IRS Notice on Tax Exempt Organizations Issuing 1099s

www.irs.gov/charities-non-profits/information-returns-forms-1099

IRS Tips on Issuing 1099s

www.irsvideos.gov/sbv_1099webinar/pdf/1099_and_Backup_Withholding_Handouts.pdf