House Government Oversight Committee

FINAL REPORT ON INVESTIGATION 1-2019:

COMMONWEALTH LOBBYING DISCLOSURE LAW

October 30, 2019

House Government Oversight Committee

Majority Chair Seth Grove

Minority Chair Matt Bradford

Representative John Lawrence

Representative Kevin Boyle

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Report Title Page

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I. Referral from House Leadership

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House of Representatives

COMMONWEALTH OF PENNSYLVANIA

HARRISBURG

Date: **May 6, 2019**

To: **The Majority and Minority Chairs and Members of the Government Oversight Committee**

From: **Majority Leader Bryan Cutler**
Minority Leader Frank Dermody

Re: **Committee Referral for Investigation**

Under the provisions of House of Representatives Rule 45A, we hereby refer the following to the House Government Oversight Committee for their consideration and investigation.

Background

Chapter 13 A of Title 65 (regarding lobbying disclosure) establishes comprehensive regulation of direct and indirect lobbying activities designed to influence the actions of the General Assembly and the Executive Departments of the Commonwealth.

To ensure that the practice of lobbying is and remains transparent, except where specifically exempted, the Chapter requires individuals and entities engaged in lobbying as an individual, firm or principle, to register with the Department of State (DOS) and report lobbying expenditures and other information to it on a regular basis.

The Chapter also establishes ethical standards applicable to lobbyists. Further, it delineates prohibited conduct by lobbyists and principals and vests the Pennsylvania Ethics Commission (the PEC) with the authority to offer advisory opinions and investigate and hold hearings into alleged violations of the Chapter's requirements. Violators face administrative penalties for negligent and intentional violations as well as possible criminal prosecution.

In response to some indications that a percentage of lobbyists had in the past failed to register and report as required, the General Assembly passed HB 1175 of 2018 which was signed into law by the Governor as Act 2 or 2018. Act 2 amended various sections within Chapter 13A and was designed to encourage compliance by increasing administrative penalties for failure to truthfully register and report. Specifically, the legislation:

- Increased the maximum administrative penalty that may be imposed by the Ethics Commission when it has been determined that a lobbyist or principal has committed an unlawful act from $2,000 to $4,000.

- Increased the maximum administrative penalty that may be imposed for negligent failure to report as required by the law from $50 per late day to:

    - $50 per late day for the first 10 days;
    - $100 per late day after the first 10 late days through the 20th late day; and
    - $200 per late day after the first 20 late days.

- Provided that a registered principal's quarterly expense reports and all registration and reporting forms shall be subject to Title 18 § 4904 (regarding unsworn falsification to authorities).

Additionally, Act 2 sought to make it more convenient to register and report and verify compliance, and to increase access to reported information by:

- Mandating registration and reporting by lobbyists and principals be done using the DOS's computerized filing system, and

- Requiring the DOS to:
    - post all filings on its publicly accessible website within seven days of receipt; and
    - issue electronic receipts to registrants who file documents electronically.

The legislation became effective on April 15, 2018.

Reason for and Scope of the Referral

Since the goal of Act 2 was to increase compliance and transparency, we are requesting the Committee conduct a review of the Department of State's implementation of its provisions to determine whether those goals have been realized. Specifically, the Committee should gather information to identify, as much as possible, the rates of registration and reporting compliance under the law prior to Act 2, and the impact, if any, that it has had on those rates. The Committee should seek to determine the reasons why non-compliance still exists if in fact it does. Finally, the Committee should make appropriate recommendations for legislation that it believes will further enhance the goals of The Lobbyist Disclosure laws to ensure the People of the Commonwealth have confidence in the integrity of the processes through which laws are made and enforced.

II. Executive Summary

On May 6, 2019, the House Government Oversight Committee (Committee) received a joint referral from Majority Leader Representative Bryan Cutler and Minority Leader Representative Frank Dermody, requesting the Committee investigate compliance with the Commonwealth's Lobbying Disclosure Law (Act 134 of 2006) as amended by Act 2 of 2018. The referral was designated No. 1-2019.

The Committee's review of the statute, its administration by the Pennsylvania Department of State and enforcement by the State Ethics Commission leads it to the conclusion that, while the vast majority of principals, lobbying firms and lobbyists diligently follow the law regarding registration and reporting of expenditures, the actual rate of compliance cannot be determined. This is the primarily the result of the way the law is structured and, to a lesser degree, implemented. Changes in the law are needed to enhance its goal of providing the public with an accurate picture of the level of spending to influence decision making by state officials and employees in the legislative and executive branches.

If the statute were changed to require all who are registered at the end of a registration period to either terminate or re-register by a fixed date, the problems now encountered would be eliminated to a great extent. The unfairness of requiring small entities and individuals who, under the present law, would be required to pay the $300 fee even though they may not know whether they will engage in lobbying in the new period, can be eliminated. The Committee believes the current fee structure itself is inequitable and should be changed. That issue is discussed further on in this report. It includes a recommendation that the registration fee be eliminated altogether, and the program be supported by a portion of the sales and use tax which is now applied to expenditures for lobbying services.

The Committee believes the primary expense reporting should fall on lobbyists rather than on principals. There are several weaknesses in the current system which would be alleviated by this change. Presently, most money spent by principals on lobbying is done through lobbyists, either employed by them or retained under contract. Lobbyists typically report to their principals the total spent on behalf of each principal at the end of each quarter. The responsibility for reporting this to the Department of State is placed on the principal and the law requires lobbyists to "verify the accuracy" of their principals' reports. Though this verification process is intended to create a system of checks and balances to ensure expenses above the thresholds are reported, in reality most lobbyists have little information about the actual amount spent by their principals as spending may have been done directly or through another lobbyist. For this reason, the law allows the lobbyist to make a qualified verification, affirming it is based on information and belief. Lobbyists almost universally provide a qualified verification, citing a lack of knowledge of the principal's finances, rendering the requirement meaningless.

When lobbyists spend money on gifts, hospitality, transportation and lodging, they are permitted to allocate the costs among their principals, unless the expense was related to advocacy on behalf of a particular principal or group of principals. The ability to allocate to many sources undermines the transparency that was intended by the reporting thresholds for these expenses. As more fully explained in Finding 3, there is a substantial impact on what the public sees as the true level of expenditures on gifts, hospitality, transportation and lodging provided to state officials and employees.

The Committee studied the Act's audit requirement and its implementation. The law requires the Department of State to select 3% of principals, lobbying firms and lobbyists each year to be audited for compliance. The audits are to be conducted by a CPA or CPA firm selected every two years. Audits are required to adhere to generally accepted auditing standards and to test whether each registration or report is materially correct. The audit contract requires the auditors to utilize the subject's files, bank statements, cash receipts and disbursement journals, deposits, cancelled checks and any other documents necessary to make the determination.

The Committee learned, in reality, auditors do not independently review the subject's cash disbursements to verify whether reported expenses are accurate. Rather, their review is limited to asking subjects to provide documentation to support what they reported as expenses. The receipts are also used to document whether the expenses were properly allocated among direct and indirect lobbying and gifts and hospitality. Because they do not independently review all of the subject's expenditures (or a statistically valid sample), this method would not uncover any under-reporting of expenses. For instance, if the subject reported $5,000 during the period, they would be found in compliance if they submitted receipts even if, in fact, they spent $10,000.

The statute prohibits the Department from engaging an auditor in successive two-year periods. This provision not only results in a loss of expertise in the business of lobbying and the applicable law every two years, it reduces the pool of qualified applicants for the contract.

The Committee learned the current auditors, who were engaged to audit reports and registrations filed during 2017 and 2018, were themselves a registered principal and utilized an affiliated lobbyist during the same period. There is nothing in the Act to prohibit this and there is no suggestion their work to date has been impacted by it. However, the Committee believes the potential for a conflict of interest should counsel against selecting a firm which itself is in the audit pool.

The Act requires audit reports to be kept confidential though reports must be provided to the Ethics Commission on request if the Commission is investigating a violation. Regulations give the Department discretion to provide an audit report to the Commission. The Committee is of the opinion the confidentiality provisions serve little purpose and are unnecessary. The law currently requires the Department to select 3% of principals, lobbying firms and lobbyist in a public lottery. Thus, the identity of audit subjects is a matter of public record. If an audit report is disclosed to the Commission and deemed worthy of enforcement action the details will be made public through the Commission's subsequent order. Conversely, if an audit results in no adverse findings, disclosing this fact would not disclose any private information. Releasing audit reports with negative findings would not only provide transparency, it would encourage compliance and act as a guide to other registrants to comply with the Act.

Perhaps the most significant fact learned during the Committee's review of the audit requirement is the Department acknowledged it has never exercised its discretion to provide the Commission with an audit report containing adverse findings. Nor has the Commission ever requested one, though it pointed out it would have no reason to request a report without knowing whether it documented a violation.

Though the Department declined to release audit reports to the Committee, citing confidentiality, it agreed to release a summary of adverse findings during the past three years. These showed during the years 2015-2017, auditors found on average 20% of subjects had filed a late registration and 8% had submitted a late expense report. None of these were forwarded to the Commission for possible investigation.

Though this past practice is concerning, the Committee has been assured by the Department it will be holding discussions with the Commission to develop a plan for providing audit reports on a routine basis in the future.

The Committee is of the opinion the statutory requirement to select 3% of all principals, lobbying firms and lobbyists each year is not a cost-effective approach and impacts the level of compliance which should flow from the threat of an audit. Statistically the requirement means a subject would only be audited once every thirty-three years. Additionally, a registrant with an unblemished record of compliance would stand the same chance of being audited as an entity which is habitually late in registering or reporting. The Committee recommends the 3% requirement be eliminated in favor of allowing the Department and Commission to develop a risk-based approach to audit selection, using standards and guidelines which would be published.

The Committee heard from users as well as the Commission that the Department's electronic registration and reporting system, now mandated by Act 2 of 2018, is sometimes unreliable in documenting timely filing and updating registration and reports. In the past, the Commission has attempted to cite registrants for not updating their registration on time, only to find that an attempt was made but the system did not reflect it. This has had a substantial impact on its enforcement efforts since apparent violations must be manually investigated to ensure the information is accurate.

The Department is aware of the system's shortcomings and has advised the Committee that it plans to develop a new system in the near future, though no start date has been set. The Committee recommends that the Department establish a group which includes all parties, including users, to guide the development of the new system.

As previously noted, the Committee is of the opinion that the uniform $300 registration fee is inequitable and no doubt results in some principals failing to register, particularly when their lobbying activity begins toward the end of the two-year registration cycle. A fee which is more proportional to the level of lobbying activity would be fairer. Because the Commonwealth levies sales and use tax on lobbying services, the Committee believes this is an ideal measure of lobbying activity. The flat fee should be eliminated and a portion of the sales and use tax should be used to offset the Department's administrative costs.

Finally, the Committee reviewed the regulations which govern lobbying reporting and registration. The regulations are promulgated by a committee, the makeup of which is established in the Act. The regulatory committee adopted the current regulations in 2009 and has not met to update them since this time. As a result, the regulations conflict with the statute, particularly by not accounting for the changes made in Act 2 of 2018. In addition, some of the regulations, though perhaps necessary when the law was first enacted, are no longer good policy.

For instance, the regulations state that a lobbyist's registration statements are not required to be signed. This has resulted in at least one lobbyist who had no knowledge a lobbying firm had registered him, being assessed thousands of dollars for failing to provide a photograph as required by the Act. Also, the regulations require the Commission to send a warning letter to a registrant who has failed to file a timely report, giving the subject 30 days within which to comply. If the subject complies, no penalty may be assessed. Though this provision serves a purpose when applied to a registrant who negligently fails to file a single report on time, it makes no allowance for repeat offenders. This has resulted in subjects gaming the system by habitually filing late reports, knowing that no penalties can be assessed unless and until they have ignored the warning. The regulation should be changed to permit the Commission to exercise discretion to waive penalties in appropriate cases.

III. The Evolution of Lobbying Regulation in Pennsylvania

Background

The business of lobbying state legislatures, the Congress and other public officials in support of or in opposition to proposed legislation or executive action has been part of the nation's political fabric since its founding. United States Senator William McClay, whose Harrisburg home sits three blocks from the State Capitol Building, is said to have complained in 1799 that "New York merchants employed 'treats, dinners, attentions' to delay passage of a tariff bill." (Robert C. Byrd, History of the Senate 1789-1989). According to the Center for Responsive Politics, in the 1850's Samuel Colt gifted members of Congress and their families his famous firearms to curry support for a change in patent laws. Later, during the Gilded Age of rapid industrial expansion across the US, when railroads managed to secure more than 200 million acres of government land doled out through Congressional grants, at least one magnate lamented the daily deluge of requests for free transportation received from Senators and Congressmen. (Byrd, *id.*)

Anecdotes like these affirm a public belief that lobbying is a method by which special interests thwart the common good. As Senator Byrd observed, however, Congress "could not adequately consider [its] workload without them." (*Id*.)

Beyond the good which results from helping public officials sort through myriad proposals and policy choices, the courts have recognized lobbying as an integral part of the public's First Amendment rights to express their views to decision-makers and petition the government to redress grievances. These constitutional foundations, though, have not placed the practice of lobbying and its practitioners beyond the reach of all government regulations. After the passage of the Federal Regulation of Lobbying Act in 1945, the first federal law governing lobbying by domestic interests generally, the Supreme Court held the registration and reporting requirements in this Act passed constitutional muster when applied to compensated lobbyists directly engaged in advocating for the passage or defeat of legislation by Congress. *U.S. v. Harriss*, 347 U.S. 612 (1954). In doing so, the Court struck a balance between the regulations' obvious restraint on free speech against the need for members of Congress to evaluate who and what is behind such advocacy. That, the Court determined, was itself "a vital national interest" which tipped the scale. The Court observed:

> "Present-day legislative complexities are such that individual members of Congress cannot be expected to explore the myriad pressures to which they are regularly subjected. Yet full realization of the American ideal of government by elected representatives depends to no small extent on their ability to properly evaluate such pressures. Otherwise the voice of the people may all too easily be drowned out by the voice of special interest groups seeking favored treatment while masquerading as proponents of the public weal. This is the evil which the Lobbying Act was designed to help prevent." (*Id.* at 625)

Though the High Court has not weighed in on the constitutional limits of lobbying regulations which have been enacted since *Harriss* was decided, several Circuit Courts of Appeal have upheld more recent federal and state lobbying regulations in favor of disclosure, again weighing free speech against the rights of the public to know who is paying, and in what amount, to influence government decision-making.[1]

[1] See: *Calzone v. Summers*, 909 F.3d 940 (8th Cir. 2018); *National Assoc. of Manufacturers v. Taylor*, 582 F.3d 1 (D.C. Cir. 2009); *Florida League of Professional Lobbyists, Inc. v. Meggs*, 87 F.3d 457 (11th Cir. 1996); *Minnesota Citizens Concerned for Life, Inc. v. Kelley*, 427 F.3d 1106 (8th Cir. 2005); *Minnesota State Ethical Practices Bd. v. National Rifle Ass'n of America*, 761 F.2d 509 (8th Cir. 1985).

Pennsylvania's first law: The 1961 Act

Pennsylvania's effort to statutorily regulate lobbyists and lobbying of state officials has evolved over nearly sixty years beginning with the enactment of the Act of September 30, 1961 (P.L.1778, No.712).[2] This law was a basic attempt to identify and, to a degree, regulate those who were engaged in lobbying of members of the General Assembly. It required compensated lobbyists to register with the Chief Clerk of the House and Secretary of the Senate and identify their employer as well as the person or entity on behalf of whom they advocated. Registration had to occur before any advocacy for the defeat or passage of legislation had begun. Amendments to registration statements were required as soon as any changes were made, and registrations expired at the end of each session of the General Assembly. Violators of these requirements faced up to one year in jail and a $500 fine.

Act 212 of 1976

The 1961 Act was later amended by Act 212 of 1976[3] which expanded its reach to include lobbying activities directed at the Commonwealth's executive branch. It applied registration requirements to those advocating the Governor to approve or veto legislation, as well as state agencies regarding the promulgation, amendment or repeal of any regulation. The amendment allowed a five-day period within which to register or amend a registration after lobbying activities or compensation to do so was established while creating exemptions for those who received less than $500 per year in compensation and those whose expenses for lobbying were less than $300 in a calendar month. "Expenses" included expenditures for meals, entertainment, costs of communication to the General Assembly or agency, or "any other expenditure connected with lobbying" but did not include costs incurred by a lobbyist to maintain their office.

In addition, Act 212 established a requirement for semi-annual reporting of expenditures. Costs for meals, entertainment, and communication to members and staff of the General Assembly, Governor, and Commonwealth agencies were required to be detailed separately. Lobbyists were required to report the identity of any Commonwealth official or employee who received "pecuniary benefits" in excess of $150 during any reporting period. Lobbyists were

[2] https://drive.google.com/file/d/1_dMGhzjrLarZeKIJP1fXg1q9O7nBr8p8/view?usp=sharing.
[3] http://www.palrb.us/pamphletlaws/19001999/1976/0/act/0212.pdf.

also required to separately state expenses for the period incurred on behalf of each lobbyist's employer or client. If a lobbyist failed to file a report, the employer or client represented was required to report the amount advanced or reimbursed to the lobbyist for the period. Reports were made available for public inspection.

Act 212 also established ethical standards for the regulated community. Lobbyists were prohibited from receiving compensation contingent on the passage or defeat of legislation or the occurrence or non-occurrence of formal action by an agency. The Act increased penalties upon conviction for violating the law to a maximum fine of $2,500 and, for individuals, a five-year disqualification from engaging in lobbying activities.

Act 93 of 1998

During the twenty-two years which followed the passage of Act 212, several bills were introduced to amend the existing law, but none reached the Governor's desk until Senate Bill 254 of 1998. Senate Bill 254 was originally crafted to make changes to the state's open meetings law, the Sunshine Act. Minor amendments were approved in the House and Senate and the bill was returned to the House on concurrence where a comprehensive amendment was added which created three new chapters to Title 65, Public Officers. The amended language included the codification of the Public Officials and Employees Ethics Act in Chapter 11 and the creation of Chapter 13 which repealed the Lobbying Registration and Regulation Act of 1961 and created a new Lobbying Disclosure Act. The bill was signed into law by Governor Ridge as Act 93 of 1998[4] on October 15, 1998.

Act 93 substantially expanded the activities regulated as "lobbying" and changed the registration and reporting requirements for lobbyists, lobbying firms and their employers or clients. Beyond advocating for the passage or defeat of legislation and administrative regulations, Act 93 extended the term "lobbying" to include goodwill expenditures - providing gifts, entertainment, meals, or lodging "for the purpose of advancing the interest of the lobbyist or principal." In addition, the law identified "indirect communication" - efforts to encourage individuals or the general public to take action to influence legislative or administrative action - as lobbying. Lobbying directed at "administrative action" was expanded beyond agency regulatory rulemaking to include the "development or modification of guidelines or a statement

[4]https://www.legis.state.pa.us/cfdocs/legis/li/uconsCheck.cfm?yr=1998&sessInd=0&act=93.

of policy," the "approval or rejection of a regulation," nominations and appointments of Commonwealth officers and employees and "the proposal, consideration, promulgation or rescission of an executive order."

The Act also shifted administration of the law from the Clerk of the House and Senate Secretary to the State Ethics Commission (SEC or Commission). A committee composed of the Secretary of the Senate, the Chief Clerk of the House, the Chairman of the State Ethics Commission, the Attorney General, the Secretary of the Commonwealth, the Auditor General and the General Counsel, or their designees, were charged with promulgating regulations necessary to administer it. Because the Act of 1961 only provided for criminal penalties, it resulted in infrequent enforcement. To remedy this, the new law authorized the Commission to assess civil penalties for violations.

For the first time, "principals," (i.e. those who lobbied for their own interests or employed a lobbyist to do so) were required to register as well as lobbyists and lobbying firms. Spending thresholds which triggered registration were established. In general, the Act required any lobbyist who was compensated more than $2,500 per quarterly reporting period and any principal whose total expenses for lobbying purposes exceeded $2,500 per quarterly reporting period to register biennially with the Commission and submit expense reports. Principals were required to identify each lobbyist representing them by name, registration number, and the acronyms of any affiliated political action committees (PAC's). Likewise, each lobbyist was required to identify the name, registration number and acronyms of any affiliated PAC's and each principal they represented. Additionally, a principal which identified itself as an organization or association was required to disclose the number of its dues-paying members.

Most notably, the primary obligation for reporting expenses shifted from lobbyists to principals. Lobbyists were only required to submit a quarterly expense report if they had expenses not reported by their principals. Each reporting principal or lobbyist was required to disclose the general subject matter or issue being lobbied. A spending threshold for filing reports was set at $500 in any quarterly reporting period.

Though principals and lobbyists were permitted to make good faith estimates when reporting expenses for personnel and offices, as well as direct and indirect communication, the new law required reporting of the actual costs for gifts, entertainment, meals, transportation, lodging and receptions provided to state officials and employees or their immediate families.

Consistent with the reporting requirements by public officials under the Public Official and Employee Ethics Act, the threshold for lobbyists and principals to report the identity of recipients for gifts was set at $250 in the aggregate during a calendar year. Reporting for expenses for hospitality, transportation and lodging was required if the cost exceeded $650 on any single occurrence. Principals and lobbyists were also required to provide written notification to any official or employee they were reporting as a recipient of such gifts or hospitality to enable the recipient to comply with their own obligations to report gifts and hospitality under the Ethics Act.

To ensure public officials and the public would know the true source of funding for lobbying activities, principals were required to identify any individual or entity which contributed more than ten percent of the total resources they received during the reporting period.

In addition to the expense thresholds for registering and reporting, the Act established certain non-monetary exemptions from its registration and reporting requirements. These included religious organizations advocating to protect their freedom of religion, public officials acting within their official capacity, individuals who limited lobbying to preparing testimony and testifying before legislative or administrative proceedings, those not compensated other than reimbursement for traveling expenses, those whose total compensation was less than $2,500 during any reporting period, and principals whose expenses did not exceed this amount.

The law also prohibited registered lobbyists from serving as an officer or treasurer of a candidate's political action committee as well as any agreement to convert a lobbying fee into a campaign contribution.

For the first time, the law established a registration fee of $100, payable biennially. Income from the fee was placed in a restricted "Lobbying Disclosure Fund" to support the administration of the law.

In an effort to monitor compliance, the Act also required the Ethics Commission to randomly select principals and lobbyists for an audit of their registration statements and expense reports, though it required audit reports and findings remain confidential unless they resulted in an investigation and Commission order.

The Act applied to everyone engaging in lobbying, including attorneys. There was a concern during debate that the courts might find that to be an unconstitutional infringement on the Supreme Court's plenary authority to regulate the practice of law. In this case, attorneys who lobbied would be exempt from the Act's requirements and thus given a significant advantage over non-attorney lobbyists. To prevent such a bifurcated system, the Act included a "partial severability clause" under which all provisions of it were declared severable except any part of the law held to be invalid as an improper regulation of attorneys. The clause was therefore designed to ensure everyone, or no one, was regulated.

As the Legislature anticipated, Act 93's applicability to attorneys was challenged in the Commonwealth Court soon after its enactment. In a 4-3 decision, *Gmerek v. State Ethics Com'm, 751 A.2d 1241 (Pa. Commw. Ct. 2000)*, the Commonwealth Court agreed that some of its provisions, when applied to attorneys, did indeed amount to regulation of the practice of law. Invoking the "partial severability clause," the court thus declared the entire law invalid.

The decision was appealed to the Pennsylvania Supreme Court but ultimately the question of whether it unconstitutionally regulated the practice of law was never resolved by a majority of that Court. Rather, two members of the Court agreed outright with the Commonwealth Court's view that lobbying by attorneys encompassed rendering of legal advice and was therefore inextricably intertwined with the practice of law. Justice Castille voted to affirm but on the narrower grounds that reporting requirements in the statute conflicted with Rule 1.6 of the Rule of Professional Conduct for attorneys, which establishes an attorney's obligation to maintain client confidences. On the other hand, Justice Saylor, joined by two other justices, was of the opinion that the statute was sufficiently narrow to be within the constitutional prerogative of the General Assembly and executive branches to regulate those who sought to influence them. These three justices believed the implications on the practice of law were marginal and tangential. Because Justice Flaherty had left the Court and did not participate in the decision, the Court was evenly divided, resulting in an affirmance of the decision of the Commonwealth Court. Consequently, the Lobbying Disclosure Act of 1998 was rendered a nullity though only two of six justices supported the Commonwealth Court's rationale. *Gmerek v. State Ethics Commission, 807 A.2d 812 (Pa. 2002)*.

In 2003, one year after the *Gmerek* decision, the Supreme Court adopted a new rule of professional conduct, Rule 1.19, to reconcile the conflict between regulation of the practice of law and the business of lobbying found by the affirming justices in that decision. The new rule required attorneys acting as lobbyists to conform their conduct to any statutory or regulatory requirements established by the General Assembly, any agency within the Executive branch or local ordinance which are consistent with the Rules of Professional Conduct. Rule 1.19 satisfied Justice Castille's concern about attorneys' obligations under Rule 1.6 and lobbying disclosure requirements, by expressly providing that Rule 1.6 did not prohibit disclosure of client confidences mandated as part of lobbying regulations. Also, in 2003, at the beginning of the legislative session the Senate adopted Senate Resolution 3[5], which required lobbyists to register with the Secretary-Parliamentarian of that chamber and file quarterly reports of expenses for lobbying Senators or Senate employees. The procedures and reporting thresholds mirrored those established in the invalidated 1998 statute.

In 2006 Governor Rendell amended Executive Order 1980-18,[6] which established a code of conduct for employees under the Governor's jurisdiction, to include provisions requiring lobbyists to register with the Secretary of Administration and file quarterly reports of expenditures for lobbying officials and employees. Exemptions and thresholds were the same as the Senate's parameters. Notably, this order served as a precursor to Governor Tom Wolf's Executive Order 2015-01,[7] which established an Executive Branch Employee Gift Ban which remains in place today.

The Current Law: Act 134 of 2006

Though the Supreme Court paved the way in 2003 for the House and Senate to resurrect lobbying regulation applicable to all practitioners and all public officials and employees, it was not until 2006 that the legislature responded by enacting Act 134 of 2006[8] which remains the current law. Act 134 incorporates most of the provisions from Act 93 of 1998 but, in addition to making a few technical changes, includes some substantive ones as well.

The Act expressly applies to all regulated professionals engaged in lobbying, including attorneys. If an attorney is found to have violated the law, the Act requires the Disciplinary Board of the Pennsylvania Supreme Court to be notified.

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[5] https://drive.google.com/file/d/1SbnwD44zQLSQSXQFdUdfra_A2Z5vaenz/view?usp=sharing.
[6] https://www.pabulletin.com/secure/data/vol36/36-14/561.html.
[7] https://www.governor.pa.gov/newsroom/executive-order-2015-01-executive-branch-employee-gift-ban/.
[8] https://www.legis.state.pa.us/CFDOCS/LEGIS/LI/uconsCheck.cfm?txtType=HTM&yr=2006&sessInd=0&smthLwInd=0&act=0134.

In order to separate the administration of the Act from its enforcement, the Department of State is now the repository of lobbying registration and reporting records, while the Ethics Commission continues to be the enforcement arm.

Though principals remain primarily responsible for reporting expenditures, the Act also requires lobbying firms (i.e., those who employ lobbyists) to register and report expenses not reported by principals. It increases the threshold triggering quarterly expense report filing from $500 to $2,500 and gives the Department of State the authority to biennially increase that as well as the threshold for registration, if it finds a higher limit will not compromise the purpose of the law.[9] Like its predecessor, Act 134 establishes a $100 registration fee but gives the Department the authority to biennially increase it to offset the costs of administration.[10] In addition, it requires registered individuals and entities engaged in indirect communication to identify themselves in their communication. Though the law continues the requirement that lobbyists and lobbying firms identify their principals, they are no longer required to file separate registration statements for each principal they represent.

Act 134 also creates a code of conduct for lobbyists which addresses conflicts of interest by prohibiting lobbyists and their employer-firms from representing principals whose interest is directly adverse to the interest of another client during the same legislative session. Exceptions are made for lobbyists who reasonably believe they can provide "competent and diligent representation to each affected principal," and the affected principals provide "informed" consent after written notice about the conflict. Violators may be assessed an administrative penalty of up to $2,000 and can be barred from compensated lobbying for up to five years. Complaints against lobbyists who are attorneys that involve conflicts of interest are now forwarded to the Disciplinary Board of the Supreme Court for investigation. The Act also establishes "unlawful acts" which include but are not limited to the following:

- Instigating the introduction of legislation for the purpose of obtaining employment to oppose it;
- Counseling someone to violate the act or engage in fraudulent activity;
- Making a loan to a public official to influence legislative or administrative action;

[9] Under the authority provided in Section 13A08(j), the Commission raised the threshold to $3000 starting in January 1, 2017.
[10] The threshold has been raised twice since enactment of Act 134 and is currently set at $300.

- Refusing to identify to a state official or employee the principal on whose behalf the lobbyist is advocating;
- Coercing or bribing, extorting or unlawfully retaliating against a public official;
- Influencing a public official by promising to provide financial support to their candidacy or against an opponent;
- Engaging in conduct bringing lobbying or the executive or legislative branches into disrepute.

The Commission may impose civil penalties of up to $4,000 and debarment from lobbying for five years against violators. Unlawful acts also are graded as misdemeanor crimes and the Commission may, if appropriate, refer a case to the Attorney General for prosecution.

In contrast to Act 93 of 1998 which included a provision requiring the State Ethics Commission to select, by lottery, "a sufficient number" of reports and registration statements to audit, Act 134 places that responsibility on the Department of State. It requires the Department to contract with a CPA or CPA firm every two years to conduct the annual audits of three percent of registrants. Entities to be audited are selected in a public drawing "60 days following the close of each fourth quarter reporting period."

As with Act 93, audit results are to be kept confidential, though the law requires the DOS to release an audit report to the Commission "if the commission is investigating an alleged violation of this chapter involving the audited registration or expense report." The Commission is authorized to disclose the audit findings as part of a finding of fact in a Commission investigation.[11]

Like Act 93, Act 134 provides civil penalties for negligent violations of the registration and reporting requirements. The Act establishes a fine for each day of non-compliance, originally set at $50 per day but increased by Act 2 of 2018 to $100 per day for the 11th to 20th day and $200 for each day beyond that.[12] Intentional violations are made criminal offenses,

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[11] Though the language of the confidentiality provision in Act 134 appears at first blush to coincide with the confidentiality requirements contained in the 1998 Act, the practical effect of shifting administration of the act to the Department of State has had a substantial impact on enforcement. Prior to Act 134, when both administration and enforcement fell within the jurisdiction of the State Ethics Commission, audit results were provided to that agency and enforcement actions could be initiated if the Commission deemed it advisable. After the enactment of Act 134, with the transfer of administration to the Department of State, audit reports now go to that agency. The DOS has acknowledged that it has never provided an audit report to the Commission though its regulations give it discretion to do so. See: Audit Findings in the discussion of Audits, *infra*.

[12] 65 Pa.C.S. §13A09(c).

graded as misdemeanors of the second or third degree and the court is authorized to impose a fine up to $25,000. If the Department or the Commission "has reason to believe that an intentional violation of [the Act] has been committed," they are required to refer the matter to the Attorney General and, if the subject is an attorney, to the Disciplinary Board of the Supreme Court.[13]

The State Ethics Commission is the enforcement arm in lobbying regulation. It is empowered to conduct investigations of violations and has broad discretion to determine how to proceed and the appropriate penalty if allegations are determined to be a violation of the Act. Investigations may be started after an inquiry prompted by a citizen complaint or by referrals from the Department of State. In some instances, the Commission has opened an inquiry on its own initiative.[14]

If a matter involves negligent or unintentional "Prohibited Activities" defined in Section 13A07, the Commission may conduct a preliminary inquiry unless it is required or chooses to refer the complaint to another agency.[15] If warranted, the Commission may open an investigation and conduct hearings with compulsory process to determine facts. If the prohibited activity was intentional, the Commission may refer the matter to the Attorney General for investigation and prosecution.

Act 134 authorizes the Commission to bar an individual or entity from lobbying for up to 5 years if they fail to comply with the statutory requirements after a Notice of Non-Compliance is served and a hearing, if requested, is held.[16]

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[13] 65 Pa.C.S. §13A09(h).
[14] As a result of funding restrictions, the Commission's lobbying enforcement staff is small, consisting only of two individuals who also are involved in enforcement of the State Ethics Act.
[15] For example, if the allegation involves a conflict of interest by an attorney, Section 13A07(d)(8) require the Commission to refer the matter to the Disciplinary Board of the Supreme Court for investigation.
[16] 65 Pa.C.S. §13A09(d).

IV. Investigative Findings

On October 23, 2019, the Committee held a public hearing at which it heard testimony from representatives of Greenlee Partners, a large Harrisburg lobbying firm who discussed the law and its implantation from a user's perspective. They also offered recommendations for improving the transparency of lobbying and the money that flows into it. The Committee also heard from officials from the Department of State and the State Ethics Commission who explained how the law is administered and enforced and offered opinions about how it could be improved. The information provided by these witnesses was highly informative and valuable in helping the Committee to understand how the law was intended to work and how it actually does in the real world. Written testimony was submitted by Greenlee Partners and the State Ethics Commission and is attached in the Appendix.

Prior to the hearing, Committee staff interviewed lobbyists, principals, officials from the Department of State and the State Ethics Commission as well as auditors, representatives from the PA Association of Government Relations and individuals from firms who assist registrants in complying with their responsibilities under the Lobbying Disclosure Act. Some of the latter serve as advisors, assisting clients in the preparation of reports and updating registrations while others actually prepare these on behalf of their clients. These witnesses, too, offered a highly informed perspective into the business of lobbying and the strengths and weaknesses in the law.

The overall conclusion the Committee reached from information gathered is the vast majority of principals, lobbying firms and lobbyists diligently try to comply with the Act. However, the Committee also was made aware of the deficiencies in the current legal structure which makes it difficult to know exactly what the actual rate of compliance is among the thousands of individuals and entities that engage in lobbying either for their own benefit or on behalf of someone else. In that respect, the evidence gathered leads the Committee to conclude that, though intended to bring transparency to the expenditure of money to shape legislative and administrative public policy, in significant ways the current law could be improved. This report will address the Committee's conclusions and recommendations for change.[17]

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[17] In addition, the committee identified certain areas of the lobbying disclosure law that require further research. Only the areas and recommendations that fall within the scope of Referral for Investigation 1-2019 are discussed herein.

Finding 1: Current law makes it difficult to identify and enforce registration violations.

Section 13A05 requires all registered principals to file quarterly expense reports within thirty days of the end of a calendar-year quarter, identifying all expenditures if the total for the period exceeded $3,000, or, if not, a statement to this effect. Lobbyists are required to file a quarterly report if they made expenditures which were not included in a principal's report. Because a report is not necessarily due from a lobbyist, non-compliance is often difficult to discover unless an audit uncovers it. Conversely, since all principals must file a report, identification of principals who fail to do so is straightforward. After the due date for filing reports has passed, DOS provides the Commission with a list of those who have not complied.

The discovery of registration violations is more difficult. Section 13A04(a) of the Act requires principals, lobbying firms and lobbyists who are not exempt under Section 13A06 to register with the DOS "within ten days of acting in any capacity as a lobbyist, lobbying firm or principal." Registration is valid for a two-year period, coinciding with each two-year legislative session, unless terminated sooner by the registrant. Under DOS' interpretation of the statute,[18] all registrations expire on December 31 of the even-numbered year but registrants "not actively lobbying [on January 1]…may choose to wait until [they] exceed the [$3,000 spending] thresholds for registration before renewing [their] registration."

The date registration is required is therefore not easily determined, even if a quarterly report of expenditures is filed, since quarterly reports filed by the principal only tell whether the threshold was exceeded, not when it occurred. At the Committee hearing, the Commission acknowledged it becomes virtually impossible to enforce the registration requirement unless a complaint is made[19] and the lobbying activity alleged to have occurred can be documented.[20]

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[18] See: Department of State Lobbying Disclosure Renewal instructions, https://www.dos.pa.gov/OtherServices/LobbyingDisclosure/LobbyingAccountServices/Documents/Lobbying-Disclosure-Renewal-Letter.pdf.

[19] An audit, of course, could identify the date of the expenditure and the date registration was required, though the Committee found significant shortcomings with the statute's audit provisions (65 Pa.C.S. §13A08(f)) and their implementation, See discussion, *infra*. An audit will not identify a party who has failed to register, however, since the pool of audit subjects includes only those who have.

[20] The Commission noted that, even when a specific allegation is made that someone is engaged in lobbying, it is difficult to prove. As they explained, merely showing that someone had a meeting with a public official doesn't prove the purpose was to advocate or influence decision-making. This difficulty is reflected in the Commission's Orders which have dismissed cases citing a lack of proof. The few sustained violations reported involved individuals who conducted large mail and email indirect lobbying campaigns, thus documenting the violation.

This is borne out by data from the State Ethics Commission 2018 Annual Report [21] which noted, "the Pennsylvania Department of State did not identify any lobbyists, principals, or lobbying firms, which had filed deficient Registration Statements and as such, the Commission did not pursue any penalties against same." The report notes two violations were pursued as a result of complaints filed by third parties. In each of those cases, however, the subject's lobbying activities and timing were readily apparent as each engaged in a mass-mailing to encourage constituents to contact their representatives about a pending bill without having registered as a principal.

The Commission's experience during Calendar year 2017[22] was similar. There were no referrals for registration violations from the DOS. One investigation was started by a private complaint, which resulted in a determination that no violation had occurred.

Though these statistics might simply reflect nearly 100% compliance by principals, lobbying firms and lobbyists in registering on time and providing required information, there is no definitive way to verify that.[23] A review of registrations each year disclosed numerous instances where a previously registered lobbyist or firm registered well into a new registration period. In one year, thirty-one lobbying firms had not registered by mid-May and their registrations for the previous year were listed as "expired."

This data does not provide any measure of who, if any, among the thirty-one firms simply had either not engaged in lobbying for the first five months of the new session or were in fact late in renewing their registration.

The law for the most part operates on a system of trust and voluntary compliance. A system that relies on self-reporting and voluntary compliance should nonetheless be structured, if possible, to assist in the identification of those who are not in compliance or who abuse it without having to resort to labor intensive methods such as audits and manual record reviews.

The ten-day rule and registration threshold exemption are designed to ensure businesses, non-profit organizations and individuals who engage in advocacy on a small scale are not burdened by having to register and pay a registration fee. Likewise, a party who has not

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[21] https://www.ethics.pa.gov/SiteAssets/Pages/Publications-Library/2018%20Annual%20Report.pdf.

[22] https://www.ethics.pa.gov/Documents/Publications%20Library/Annual%20Reports/2017%20Annual%20Report.pdf.

[23] As noted, however, the audit summary provided by DOS to the Committee disclosed during the period 2014-17, more than 20% of audit subjects on average each year were found to have registered late.

previously been registered may not know at the beginning of a legislative session that an issue of concern to them may arise sometime in the next two years. They cannot be expected to register until this happens. For first-time registrants, the threshold and ten-day rule serve a valid purpose.

However, many registrants are lobbyists and lobbying firms which are in the business of lobbying, or principals who have ongoing interests each year in government policies and decisions. While some principals who have registered in a prior period may not be able to anticipate at the beginning of a new registration period whether they will exceed the registration thresholds during that time, the Committee believes the current requirements could be modified to further the goal of compliance. For example, changing the law to require those who were registered during a legislative session to either affirmatively renew the registration by a fixed date unless they have terminated their prior registration would, like reporting deadlines, create a mechanism to identify who is and who is not in compliance. The Committee believes, on balance, the transparency which would arise from requiring re-registration or termination by a fixed date outweighs the burden imposed for those parties who were registered in the previous registration period. Though registration entails an obligation to report expenses each quarter, the law exempts those who expend no more than $3,000 from filing a detailed report. They merely report they spent "$0" or "less than the threshold."

Finding 2: The lack of lobbyists knowledge of principal's actual spending renders lobbyist verifying the accuracy of principals' reports relatively meaningless.

Section 13A05 of the Act requires principals to report expenses on a quarterly basis unless their expenses for lobbying did not exceed $3,000. In this case, they need only report the fact and not the actual amount. If expenses exceed the threshold, they must indicate the general topic of the lobbying effort and any lobbyist or lobbying firm that acted on their behalf. They need not disclose the amount paid to any of the listed lobbyists, however, only the total spent for direct lobbying, indirect lobbying and gifts, hospitality, transportation and lodging provided to a state public official or employee.

Lobbying firms and lobbyists are not required to report their expenditures if they are included in their principals' reports. However, the law requires lobbying firms and lobbyists not affiliated with a firm to sign and verify the accuracy of their principals' reports.[24] The statute, however, permits the lobbyist to affirm the principal's report with the qualification that it is "to the best of the attestor's knowledge" and permits, but does not require, the lobbyist to attach an explanation of the limits of its knowledge.

Lobbying firms and unaffiliated lobbyists typically inform their principals what they spent on their behalf and the principals then include this in their quarterly reports. The lobbyist or firm is not required to disclose what it reported to the principal, however.

If a lobbyist has knowledge all expenses by a principal were incurred though the lobbyist, it is a simple matter for the lobbying firm to verify the accuracy and affirm the principal's report. The lobbyist, however, may not know if a principal has expended money directly. If a principal employs its own lobbyists and or several lobbying firms to represent it, each will advise the principal of its own expenses but have no information about any expenditures made directly or through the others. Likewise, if a lobbyist or firm is unable to determine whether all its expenses on behalf of the principal have been reported by the latter, it will have no way of knowing what, if anything, it would be required to report as its own expense under 13A05(b)(6).

A review by the Committee of a sample of reports filed by principals disclosed invariably, lobbyists' and firms' affirmations are accompanied by the disclaimer. Frequently lobbyists disavow any knowledge of the principal's actual expenses "other than what was submitted by the firm to the principal for inclusion in its report." Disclaimers are often made even when no other lobbyist or firm has been identified in the principal's report.

Even though the affirmation requirement is intended to provide a modicum of checks and balances on the veracity of principal's reports, during the hearing held by the Committee, both lobbyists and the Ethics Commission acknowledged the lack of knowledge of actual expenditures by principals renders the affirmation requirement relatively meaningless. This lack

[24] 13A05(b)(4): "A lobbying firm or a lobbyist not associated with a lobbying firm shall sign the reports electronically submitted by each principal for whom the lobbying firm or lobbyist is registered to attest to the validity and accuracy to the best of the attestor's knowledge. A lobbying firm or lobbyist may attach a statement to the electronic report of a principal, describing the limits of the knowledge of the lobbying firm or lobbyist concerning the information contained in the expense report."

of transparency would be greatly diminished if lobbyists were made the primary reporters of expenditures and required to report what they spent on behalf of each principal.[25]

Finding 3: The lobbyists ability to apportion expenditures for gifts, hospitality, transportation and lodging among their principals skews the public's perception of the amount spent on public officials and employees.

Act 134 requires principals to file a quarterly report of the amount expended on direct and indirect lobbying as well as gifts and hospitality, transportation and lodging (collectively, "hospitality") provided to public officials, if the combined total exceeds $3,000 for this period. In addition, the report must disclose the identity of a public official or employee who is the recipient of gifts and hospitality if the total given to them during the course of the year exceeds $250 for gifts or $650 for hospitality.

When the $3,000 threshold is exceeded and the identity reporting threshold is reached, the principal must provide written notice to the recipient at least seven days prior to filing the expense report to assist them in meeting their obligations to file their annual Statement of Financial Interest required by the Pennsylvania Ethics Act, 65 Pa.C.S. § 1105(b)(5) and (7).[26] Section 13A09(g)3)) establishes an affirmative defense to any civil or criminal liability under either the Lobbying Disclosure Act or the Ethics Act if a public official did not receive the notice.

However, if a principal's expenses did not exceed the $3,000 threshold, it need only report this fact.[27] There is no requirement to report the amounts or the identity of the recipient even if the gifts and hospitality thresholds themselves were exceeded. The Commission acknowledged during the hearing these provisions in the law would allow a principal to spend $3,000 on gifts and hospitality each quarter and, if it had no other expenses, never have to disclose that.

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[25] The federal law governing lobbying of Congress and federal agencies requires lobbyists, rather than their clients, to report expenses. See: https://www.govinfo.gov/content/pkg/USCODE-2011-title2/pdf/USCODE-2011-title2-chap26.pdf.

[26] See: 65 Pa.C.S. §13A05(b)(3)(iv)): "Written notice must be given to each State official or employee who is listed in an expense report under this paragraph at least seven days prior to the report's submission to the department."

[27] The DOS electronic reporting system actually displays "$0" in the report, rather than "Less than the threshold." Though the actual amount would not be known in either event, the distinction is more than semantics.

Often, a gift or hospitality will be provided directly by a principal who will report it and identify the recipient if the reporting and hospitality thresholds are exceeded. However, lobbyists frequently entertain public officials and provide gifts and hospitality which are then allocated among each of their clients. Because gifts and hospitality must be reported by principals, rather than their lobbyists who actually provide it to the official, reports do not necessarily reflect the actual level of expenditures on these items.

The thresholds, and the ability to allocate expenses for gifts and hospitality among a lobbyist's principals, result in a substantial skewing of the public's perception of money actually spent on public officials and employees. According to the Department's lobbying reporting website, the dollar value of gifts and hospitality given to identified state officials and employees in 2018 was $39,262.[28] In reality, total amount of gifts and hospitality actually reported to DOS by lobbyists and principals in 2018 was nearly $1.5 million.[29] In 2017, the value of gifts and hospitality given to identified recipients was $32,318 whereas the total reported exceeded $1.65 million. These are the reported amounts. The actual amount spent no doubt exceeds these figures since they do not reflect non-reportable expenditures, i.e., those which were among expenses not meeting the overall $3,000 reporting threshold or from individuals and entities exempt from registration altogether.

Finding 4: The Act's audit provisions and the Department of State's implementation of them need to be revamped and improved.

Section 13A08(f) of the Act, and the implementing regulations, 51 Pa. Code § 61.1. Lotteries, requires DOS every two years to contract with a private CPA firm to conduct audits of "*3% of all principals, 3% of all lobbying firms and 3% of all lobbyists who have completed registration statements and expense reports filed with the Department under the act."* The audit subjects are selected in a public lottery held 60 days after the close of the 4th Quarter reporting period, usually around March 1. The scope of the audits is defined in the Act which specifies at subsection (f)(3):

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[28] See: "Public Reports" "Gift Expenditures by Source" at https://www.palobbyingservices.pa.gov/Public/wfSearch.aspx.
[29] https://www.dos.pa.gov/OtherServices/LobbyingDisclosure/Documents/2018-Lobbying-Disclosure-Annual-Report.pdf.

> "The certified public accountant shall conduct the audits in accordance with generally accepted auditing standards and shall test as to whether each registration or expense report is materially correct."

The scope of the work is further defined in the Department's Request for Quotes (RFQ) which is a document that DOS submits to CPA firms who have been pre-qualified and under a general contract with DGS to conduct audits for state agencies. It incorporates "Best Value Criteria" (BVC) that identifies the criteria that the agency will consider in selecting the successful candidate from among the pre-qualified contractors.

The BVC for 2018 (Solicitation Number: STATE-RFQ000142) for audit reports and registrations filed from January 2017 to December 2018 revealed a comprehensive set of requirements for the work to be performed. It noted that the exact number of audits could not be determined as the number of registrants fluctuates but at the time it was published, there were 1186 lobbyists, 142 lobbying firms and 1619 principals registered.

The BVC provided that the audits "shall be conducted in accordance with the Act and the regulations" and "include findings of any possible violations of the Act with respect to … registration and expenses." Required work includes "validation and compliance testing and financial reviews… performed in the contractor's offices or on site at the audit subject's place of business." It directs the auditor to conduct a pre-audit conference with the subjects and gather information "including but not limited to, clients files, bank statements, cash receipts journals, deposit slips, cash disbursement journal, cancelled checks and any additional documentation needed to complete the audit for the reporting period." From these, the auditors are to determine whether the registration statements and expense reports "are materially correct." Preliminary audit reports are to be made available to the subject for comment and final audit reports are to be submitted to the Bureau. The BVC describes the specific findings the audit should make regarding principals', lobbying firms' and lobbyists' registration and expense reports.

The Committee heard from some lobbyists and principals who had been audited, expressing concern that the audits were being conducted in a manner that was too superficial to be meaningful. Two principals from a consulting firm that assists registered principals and lobbying firms with compliance with the Act noted that three of their clients have been under audit during the current audit contract. They disclosed, though the auditors are supposed to review invoices, financial records, registration and expense reports as well as compliance with updating timelines, the auditors have so far simply sent letters asking the subjects to affirm their reports to DOS are accurate. The letters request the subjects to mail in their response.

Others expressed concern the statute prohibits DOS from contracting with a CPA or firm which previously performed these types of audits. Because lobbying audits focus primarily on compliance with statutes which are often complex, not clearly written and requiring reference to opinions from the State Ethics Commission to discern the proper interpretation, a level of particularized expertise in the legal requirements of the Act is required. The parties interviewed believe changing auditors every two years results in a loss of expertise and specialized knowledge which no doubt develops over the course of the two-year contract.

The Committee interviewed the CPA firm currently under contract. They advised that the lobbying audits are "performance" audits in contrast to "financial" audits. In describing the distinction, they offered that a performance audit focuses on whether the subject complied with statutory requirements such as filing reports and registrations timely, categorizing payments correctly, etc. In contrast, a financial audit attempts to independently verify proper accounting for revenue streams and expenditures. They explained financial audits require the auditor to review bank statements, deposits and checks written on and deposited into a client's accounts. In a performance audit, the auditor reviews the subject's lobbying registration and reports and asks for receipts to support the classification and timing of the expenditures rather than independently reviewing all receipts.

For example, they explained if the report claimed that $5,000 was spent on "direct lobbying," the auditor would request the subject to provide the receipts which document the expenses to determine if the report correctly categorized them. If the receipts show the expenditure was for "indirect lobbying," they will note this in a "finding" and advise the subject. The subject may then file an amended report to properly classify it. They acknowledged, however, because they do not independently review the subject's checking accounts and bank statements to verify what was reported, if a subject reported $5,000 for "direct lobbying" but in fact spent $10,000, a performance audit would not uncover this if the subject provided receipts only documenting $5,000 as a result of the limited scope.

When asked why the auditors do not independently verify reported expenses by reviewing checks and bank statements, they responded it would be difficult to determine, for instance, whether a check and receipt for a dinner was connected with lobbying or was a personal expense.[30] Additionally, they responded that a review of that nature would delve into "private" information and it's not their function to do this.[31]

The Committee is of the view that the limited scope of the audits conflicts with the statute's intent that the audit "test as to whether each registration or expense report is materially correct" and, pursuant to the contract review "bank statements, cash receipts journals, deposit slips, cash disbursement journal, cancelled checks and any additional documentation needed to complete the audit for the reporting period." As a practical matter, the audits may find technical reporting violations such as incorrectly categorized expenses but would not uncover instances where expenditures were under-reported.

During the course of the Committee's review of the audit contract, another issue which the Committee finds disconcerting was identified. The Committee learned that the current CPA firm, which is contracted to perform audits for calendar years 2017 and 2018, was itself registered as a principal and had an affiliated lobbying firm and lobbyists during the same periods. Though the statute does not prohibit hiring a CPA firm which was itself in the "pool" of potential audit subjects, the Committee is of the opinion this should have triggered a potential conflict of interest concern within the Department of State. When questioned regarding this matter the Ethics Commission agreed that questions could be raised about a private CPA firm's objectivity if, for example, it finds an auditee's interpretation of the reporting requirements was mistaken yet the auditors had the same interpretation when filing its own reports. Though there is nothing to suggest this particular CPA firm has acted in any manner other than professionally, the potential for a conflict remains a concern.

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[30] They acknowledged however that taxing authorities require a taxpayer to keep documentation to differentiate a personal expense from a business expense so records distinguishing the two should be available.

[31] This appears to conflict with the RFQ for Lobbying Disclosure Auditing Services through which DOS procured the current audit contractor. Beyond the general requirement in Section 3 that "Services shall be rendered in accordance with generally accepted auditing principles and the auditing standards of the American Institute of Certified Public Accountants," the RFQ, Section 4(A)(2), specifies that the "work includes, but is not limited to, validation and compliance testing and financial reviews." Further, Section 4(d) requires the contractor to, within 30 days "begin gathering information (including but not limited to clients (sic) files, bank statements, cash receipts journal, deposit slips, cash disbursement journal, cancelled checks and any additional documentation needed to complete the audit."

Finding 5: Keeping audit reports confidential serves little purpose and undermines compliance.

Section 13A08(f)(4) of the Act provides the audits are confidential "except that the Department shall make an audit report and findings available to the Commission if the Commission is investigating an alleged violation of this chapter involving the audited registration or expense report. The commission shall include the relevant portion of an audit as part of its findings of fact in a commission order which results from an investigation arising out of an audit."

The Committee questions whether the confidentiality requirement serves any purpose, given the identity of those selected for audit are known when they are selected through the public lottery. Likewise, the registrations and reports of those selected for audit are available to the public. If an audit concludes with no adverse findings against an individual or entity's registration or reporting compliance, there should be no concern about an invasion of privacy to disclose this information. On the other hand, if the audit results in findings that the requirements of the Act were not followed, in most cases, this information would disclose nothing more than what would be disclosed if the Commission were to elect to pursue the violation. Even if information which otherwise would remain confidential is made public, the Committee believes the benefits of disclosure of information would outweigh most privacy concerns. Disclosure of audit findings would provide notice to other practitioners which could potentially assist them in their own compliance and may for this reason, among others, result in increased compliance.

Most importantly, the goal of lobbying registration and reporting is to provide for transparency in the business of influencing governmental decision-making. Disclosure of audit findings would increase transparency by informing the public and the General Assembly about compliance with the law as well as its enforcement. The DOS strictly construes the confidentiality requirements in the Act, declining even to provide redacted copies of audit reports to the Committee. Instead, DOS provided only a "Summary of Audit Reports." The summary contained only limited information including the number of audits resulting in findings and the number for various categories of findings. Though the summary was useful in disclosing the number of instances where registrations and reports were filed out of time and the number of registrations and reports that had errors, the summaries did not permit the Committee to determine what those errors were or whether the methodologies used in conducting the audits were sufficient. The summary also disclosed a number of instances where the subject could not or would not provide requested information to the auditors but nothing about what information the auditors sought or what efforts were made to access it independently.

Finding 6: There is currently no follow up when audits disclose violations.

Section 13A08(f)(4) provides DOS must disclose an audit report to the Ethics Commission "if the Commission is investigating an alleged violation of this chapter involving the audited registration or expense report." Beyond this mandated disclosure requirement, lobbying regulations give the DOS discretion to disclose an audit report to the Commission.[32] The Commission advised, however, that the Department had never exercised its discretion to provide the Commission with an audit report. When asked if they had ever requested one, the Commission acknowledged that they had not, but noted that they would have no reason to request a report without knowledge of a violation.

DOS confirmed that they had not previously provided an audit report to the Commission. When asked why this was the case, they responded that the Commission had never requested one and they have chosen not to use their discretion to voluntarily disclose one.

In spite of the issues previously identified regarding the audits, they nonetheless have the potential to disclose instances of apparent violations as well as occasions when registrants simply chose not to cooperate. By not sharing the reports and the findings, the audit requirement is of limited value. Other than possibly providing a marginal compliance incentive to registrants, the audits have not returned value for the taxpayer money spent.[33]

Nonetheless, DOS has now advised the Committee, as a result of the Committee's inquiry, they have begun discussions with the Commission to identify the types of audit findings the Commission would wish to see without having to make a request for a specific audit report and they intend to turn that information over to the Commission as a matter of practice moving forward.

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[32] 51 Pa. Code § 63.3 provides that the Commission proceedings based on the registration and reporting requirements "may be initiated based on…. (3) A referral by the Department of any information arising from an audit, which, in the view of the Department, is appropriate for the Commission to consider."

[33] The cost of the current contract is $76,800. The cost of the contract covering 2015-16 was $106,400.

Finding 7: The statutory audit provisions should be changed to allow a risk-based selection process.

As noted, Act 134 requires that 3% of registrants be audited each year. Since the percentage is fixed, it not only constitutes the minimum number of audits but the maximum. Therefore, the probability of a random registrant being selected in any given year is one in thirty-three. Stated differently, an individual or entity risks being audited only once every 33 years. Though the threat of an audit could play a large role in ensuring compliance, the Committee believes the odds of being selected under the current law seriously diminishes its effectiveness.[34]

As previously noted, a review of registration and expense reports alone can identify instances where the subject may not be in compliance. Were the audit selection process to be changed to allow a risk-based approach to selection of audit subjects, more attention and resources could be applied to cases likely to uncover violations. Additionally, since a registrant would know that a track record of late filings, for example, would be more likely to be chosen, implementing a risk approach would no doubt increase the incentive to comply.[35]

Likewise, the use of an inflexible 3% formula results in a few registrants facing an audit while the vast majority are under no verification review at all. The law currently requires registrants to maintain records for a period of four years, and to produce them upon request of the Attorney General, the Disciplinary Board, the Department and the Commission. It is not clear, however, were the Commission to request records for its own targeted review, a claim could be made that such a "correspondence audit" violates the statutory requirement that audit subjects be randomly selected.

Finding 8: The DOS Electronic Registration and Reporting System needs to be updated.

The Department of State established an online registration and reporting system soon after Act 134 became law. Until the 2018 amendments, paper filings were also permitted. The Committee requested information about the initial cost of constructing the electronic system but learned it was built as part of a much larger contract with Microsoft. Though the final cost

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[34] It is questionable whether the threat of a possible audit has any compliance impact. In addition to the risk of being selected only once every 33 years, the Summary of Audit Reports" provided to the Committee disclosed numerous findings of late registration, late reporting, errors, failure to affirm reports and instances where registrants have simply declined to respond to the auditor's requests each year.

[35] 65 Pa.C.S. § 13A05(c).

attributable exclusively to that piece could not be determined, the amendment to the original contract to include development of this system added $437,000 to the original price. Additionally, there are annual costs to maintain the system. The cost in 2018 was $234,000 and was done through a staff augmentation under a state contract with OST, Inc.

The Department advised the Committee it has plans to replace the current system and expects that process to begin in 2020.

Many lobbyists interviewed stated they had consistently used the electronic system since it became available, while others only started to use it when forced by the change in the law to do so. While most who were interviewed expressed overall satisfaction with electronic registration and reporting, as well as the customer service provided by Department staff, some related frustration. The primary concerns expressed were about its reliability, noting that the system often is “down,” is not intuitive, and overall has design flaws. They cited for example, if a mistake is made or the system “crashes” while filing a report, the data must be re-entered from the beginning. Likewise, confirmation that the system has accepted the data is not always forthcoming, requiring the registrant to contact the Department to confirm their reports and registrations were timely filed.

It is important to note that the issues with the system also affect public access. Though DOS’ Lobbying Registration and Reporting website notes “registrations and quarterly expense reports can now be filed and reviewed online 24 hours a day, seven days a week, on numerous occasions when Majority committee staff attempted to access information and reports, the data was not available though recently, that has not been a problem.

Additionally, as a result of the current structure, these issues affect the Commission’s enforcement capability. For example, when the Committee questioned why there appear to be numerous instances in which a registration was not updated within fourteen days[36] after a required change was noted in affiliate’s report, the Commission responded that one of the problems they faced is that DOS has had issues in the past with the accuracy of its records. It has experienced instances where registrants have attempted to update a registration but have been unable to access the system or an update was not reflected in the records. For this reason, they cannot rely solely on the electronic records to cite an individual or entity but would need to investigate further to determine whether an attempt was made but was unsuccessful. They stated

[36] 13A04(d).

this kind of review is labor intensive, and it is beyond their available resources to investigate each potential violation.[37]

Finding 9: The $300 registration fee applicable to all discourages registration, is unfair and the revenue produced is insufficient to support the Department of State's operational costs.

Section 13A10 established an initial $100 fee for each principal, lobbying firm and lobbyists who registers with the Department of State. Section 13A08(j) requires the DOS to conduct a biennial review of the fee, beginning in January 2009, and adjust it, "if the department determines that a higher fee is needed to cover the costs of carrying out the provisions of this chapter." As noted above, the DOS has made two adjustments since then. Beginning with the 2015-16 registration period, the fee is set at $300. The DOS noted in a filing submitted to the Independent Regulatory Review Commission when the $300 fee was proposed, the increase was expected to generate only 63% of the funds needed to administer the program.

Some lobbyists who were interviewed by the Committee staff expressed the view $300 was an unreasonable amount to pay for exercising a right to make their views, and those of their clients, known to government officials. They point out fees are not assessed against lobbyists in the federal government's lobbying registration requirement.

They noted the Department originally sought to increase the fee to $700 per registrant when it contemplated an increase for the 2015-16 session but abandoned it when it drew opposition from lobbyists and others and settled on $300. Still, some feel that the uniform fee is inequitable and not justifiable and often acts as a disincentive to register at all. Some expressed the view the Department should not be permitted to seek increases in the fee without a showing enforcement and assessment of penalties against those who fail to timely register or report is vigorously pursued. Still others point to the fact a "one size fits all" fee structure is unfair. They feel the fee should be scaled so a principal which spends millions on lobbying is assessed a higher fee than a non-profit expending modest amounts above the thresholds.

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[37] The Committee's research of Commission Orders disclosed at least one instance corroborating the Commission's concern. In its order issued in MidAtlantic Community Papers Association, 16-009-L (https://www.ethicsrulings.pa.gov/WebLink/PDF/5a8355d7-7241-43e5-80ba-bb0669d82963/116-SL%20Mid-Atlantic%20Communty%20Papers%20Association.pdf) the Commission conceded there was no violation since "a communication failure and technical complications involving the Department of State' s electronic filing prevented Respondent from electronically timely filing the expense report." One lobbyist interviewed by the Committee lamented that Act 2 eliminated paper registrations and reports, noting that he didn't always trust the electronic system to record changes properly and that, when paper was acceptable "DOS gave you a receipt."

When the Department promulgated the regulation to increase the fee to $300, it noted in its regulatory filing with the Independent Regulatory Review Commission that the new fee would nevertheless only cover 63% of the Department's costs. The balance was paid out of the general fund.

The Department believes, and the Committee agrees, the current flat fee applies to all registrants is unfair. To illustrate, a part time, sole-practitioner lobbyist who receives more than $3,000 in compensation during the last quarter of a registration period must register and pay the same fee as a large corporation which expends hundreds of thousands of dollars on lobbying every year. To encourage registration, the Committee believes there should be no fee assessed for doing so, but rather, a fee should be imposed on the amount actually spent on lobbying.

Lobbying services are subjected to the Commonwealth's Sales, Use and Hotel Occupancy tax by their inclusion in the definition of a "sale at retail."[38] As a tax which is proportional to the level of spending on the activity, it more fairly assesses those who partake in it. However, under the current law, all revenue generated from the tax on lobbying services is deposited into the Commonwealth's General Fund. According to the Department, the average amount spent on lobbying during the period 2016-2018 was $116 million and the Department's annual costs to administer the program, including personnel and the contract to maintain the electronic registration and reporting system, is approximately $2 million. The sales and use tax produce roughly $7 million. If the fee were eliminated and a portion of the tax on lobbying were dedicated to supporting the program, the results would be more equitable.

Finding 10: The Department's annual reports should be timely completed and posted on the Internet.

The Department is required by Section 13A08(d) to "publish an annual report of lobbying activities in the Commonwealth." Though the statute does not define when the annual report must be published, as of June 2019, the only reports which appeared on the Department's website were for calendar years 2014 and 2015. The latter was dated February 2017. No other report appeared to have been published at this time.

[38] See: Tax Reform Code, 72 P.S. § 7201(k)(11).

In July, the Committee requested copies of any reports which had been prepared for 2016, 2017 and 2018. In August 2019, the Department provided electronic copies and apparently, at the same time, published them on their website.

The Committee would encourage the Department to timely comply with the requirement of an annual report. Because the Ethics Commission also publishes an annual report of its activities which includes information about it's lobbying enforcement, both agencies might join to produce a joint report.

Finding 11: The regulatory committee needs to meet to update regulations governing the administration and enforcement of the Act.

Section 13A10(d) of the Act establishes a committee with the authority to promulgate regulations necessary to administer and enforce the law. The Committee is comprised of the chairman of the Commission, the Attorney General (who also serves as chair), the chief counsel of the Supreme Court Disciplinary Board, the Secretary of the Commonwealth, an individual appointed by the President pro tempore of the Senate, an individual appointed by the Minority Leader of the Senate, an individual appointed by the Speaker of the House of Representatives, an individual appointed by the Minority Leader of the House of Representatives, or their designees, and a lobbyist appointed by the Governor shall have authority to promulgate regulations necessary to carry out this chapter.

The regulatory committee met and enacted regulations to implement Act 134 in 2009 but, according to the Department of State, has not met since. The current regulations do not reflect changes which have occurred, particularly with the enactment of Act 2 of 2018.

One provision which the Government Oversight Committee found concerning is 61 Pa. Code §63.4. It provides when an inquiry into violations of the registration or reporting requirements in Sections 13A04 or 13A05 is undertaken, and the Executive Director proceeds under a "noninvestigatory process," the Commission must send a warning to the registered address of the subject, giving them thirty days to "cure" the violation.[39] If the subject does not

[39] Though there are no time frames within which a warning letter must be sent, a review of Commission orders issued over several years shows it is generally not mailed until a required report or registration becomes more than 30 days past due. Thus, in reality, a "proceeding without investigation" usually results in a "grace period" of 60 days or more during which the subject can come into compliance without penalty. In each instance in which the Commission conducted an inquiry during calendar years 2016 through September 2019, the Commission proceeded

respond to a warning and cure the default, the Commission's staff will proceed by issuing a Notice of Alleged Non-Compliance. At this point, the subject may request a hearing and, if found in violation, civil penalties may be imposed.[40] However, if the subject comes into compliance, no penalties may be assessed.

The Commission's chief counsel explained this provision was added at the Commission's request as a way of encouraging compliance rather than exacting punishment. This has had a positive impact. According to the Commission's 2018 Annual report,[41] for calendar year 2018, the Commission issued a total of 105 Warning Notice Letters to principals regarding their failure to file required Quarterly Expense Reports or statements. Of those, all but nine principals filed their quarterly expense reports and/or otherwise complied with the requirements within the 30-day cure period and avoided any penalties. In each case in which the warning was ignored, the parties reached a negotiated settlement. In calendar year 2017, 85 warning notices were sent and 10 of those were ignored leading to the imposition of penalties.

Though the goal of compliance is laudatory, however, the regulation is mandatory and gives the Commission no discretion in cases where the facts call for sanctions, such as where the subject has a history of violations. A review of Commission orders disclosed one case where a subject had failed to file a report on time on seven separate occasions. In the first six instances, the subject apparently "cured" the default within the thirty-day period. On the seventh violation, the subject did not respond to the warning letter and the Commission assessed the maximum penalty, based on the history of violations. The Committee believes the regulation needs to be changed to untie the Commission's hands. It should not have to wait until a violator ignores the warning after repeatedly ignoring the report deadline.

Another regulation which the regulatory committee should address is 51 Pa. Code § 51.9(a)(2): "Registration statements are not required to be signed." The Committee has no information why this is not a requirement but in at least one instance we found in the

with a non-investigatory process. During that time period, more than 80% of deficiencies were resolved after issuance of a warning letter without further action.

[40] In most instances, however, the Commission's staff and the offender enter into a negotiated settlement which is submitted to the Commission for approval.

[41] *Id.* Note 31.

Commission's 2012 orders, it resulted in an individual being investigated and ultimately agreeing to pay a penalty that seems unjustified.

The individual was cited for failing to provide a photograph in connection with his registration as a lobbyist, something which is required to make a registration complete. The apparently unrefuted facts, however, disclosed the individual had retired from working as a staff person in the General Assembly and was approached by a lobbying firm about working for them on a part time basis. Though he expressed interest, no employment or contract resulted, and he did not hear back from the firm. Unbeknownst to him, however, the firm registered him as an affiliated lobbyist after the conversation and used the firm's address as his official address for contact.

More than a year later, the Commission conducted a review of registrants who had not submitted a photograph and sent warning letters to the subjects, however the person in question did not receive the warning letter as it was sent to the firm and not forwarded to him. He first learned of the issue only after the thirty day "cure" period expired. He contacted the Commission, explaining he was not aware he'd been registered as a lobbyist or that a warning letter was sent. Nonetheless, he agreed to a stipulated settlement including the payment of a fine that was significant due to the number of days he was "late." Had a signature been required upon registration, the issue of whether he was aware he'd been registered or not would have been conclusively established.

V. Recommendations

The Committee recommends the following actions to be taken by the General Assembly:

1. Enact legislation to make lobbyists the primary reporter.

2. Audits:

   a. Enact legislation to add a provision that auditee selection will be done by risk.
   b. Enact legislation to remove the confidentiality requirement.
   c. Enact legislation to remove the potential for conflict of interests to ensure auditors were not principals during the audit periods.

3. Enact legislation to ensure DOS can communicate audit findings to the SEC.

4. Enact legislation to clarify what DOS and SEC are to provide in their Annual Reports and provide a date for when they need submitted.

5. Enact legislation to clarify DOS is to staff the Lobbying Disclosure Regulation Committee and how often the Committee should meet to review regulations.

6. Enact legislation to ensure the primary reasons for the adoption of regulations are to ensure transparency and assist stakeholders in complying with the law.

7. Repeal requirements to charge a fee for lobbyist registration and use revenues from the sales and use tax on lobbying to cover the expenses of the Department for lobbying disclosure.

The Committee recommends the following actions be taken by the Department of State:

1. The Lobbying Disclosure Regulations Commission must meet to update its regulations based on the passage of Act 2 of 2018.
2. If the Department decides to upgrade is electronic registration and reporting, the following should be adopted:
   a. Ensure a high-level official within the Department has jurisdiction.
   b. Ensure the Department can cross-check data.
   c. Create a stakeholder advisory group of users to direct the development.
   d. Ensure the system is user friendly for the general public.
3. Ensure when individuals register as lobbyists, the Department requires that individual signs the paperwork.

4. The Department should continue using employees for Lobbying Disclosure and Campaign and Elections. This has proven to be an efficient and cost-effective means to staff both bureaus. The Department should also provide their cost allocation plans in their annual reports and budget documents.