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OFFICE OF GENERAL
COUNSEL

August 7, 2012

VIA FACSIMILE & U.S. MAIL

Jeff S. Jordan
Federal Election Commission
999 E. Street, NW
Washington, DC 20463

Re: Los Angeles County Democratic Central Committee, RR 12L-42
Our File No.: LAC3196.003

Dear Mr. Jordan:

This letter responds to your letter received by our client, the Los Angeles County Democratic Central Committee ("Committee"), on July 23, 2012, regarding the referral of the Committee and me, as Treasurer, to the Office of General Counsel for possible enforcement action under 2 U.S.C. § 437g.

At issue is the Committee's 2011 Year-End Report, and more specifically, the disclosure of \$117,343.83 in disbursements and \$55,107.88 in receipts relating to the unauthorized actions by the Committee's former treasurer, Ms. Kinde Durkee. As explained below, those disbursements, receipts and accompanying memo text entries were disclosed by the Committee after numerous consultations with Reports Analysis Division ("RAD") management and staff regarding how best to report cash-on-hand and other discrepancies resulting from Ms. Durkee's actions. Despite having numerous internal controls in place at the time of Ms. Durkee's embezzlement, the Committee was victimized by what may be the largest and most widespread fraud of this type to date. Immediately upon learning of Ms. Durkee's misconduct, the Committee terminated Ms. Durkee and adopted additional internal controls to reduce the Committee's exposure to such actions in the future.

While the Committee did not file a formal *sua sponte* submission to the Commission, the Committee has, in effect, self-reported violations by Ms. Durkee to the Commission on several occasions, including the aforementioned communications with RAD; during an audit hearing at which the Committee disclosed the facts and circumstances relating to unauthorized transactions; and in several written submissions to the Commissioners and Commission staff. Consequently, the Committee urges the Commission to take no further action against the Committee in connection with this matter.

1. The Committee filed its Year-End Report Based on Numerous consultations with the Reports and Analysis Division.

Upon learning of Ms. Durkee's misconduct, the Committee was left with incomplete records regarding the Committee's cash-on-hand and other discrepancies. In preparing the Year-End Report, the Committee, through its counsel, was in continuous contact with RAD, both at the management and staff levels. Based on those consultations, the Committee disclosed the disbursements, receipts and accompanying memo text entries at issue.

a. Disbursements of \$117,343.83. In accordance with the Commission's written guidance for political committees regarding embezzlement/misappropriation, the Committee reported the following disbursements on its Year-End Report:

- Schedule B, Line 29 (Other Disbursements): Durkee & Associates, 09/21/2011, \$48,457.87. The itemized disbursement was accompanied by a memo text entry stating, "Cash on hand adjustment due to unauthorized disbursements."
- Schedule L-B, Line 5 (Other Disbursements): Durkee & Associates, 09/21/2011, \$68,885.96. The itemized disbursement was accompanied by a memo text entry stating, "Cash on hand adjustment due to unauthorized disbursements."

The two itemized disbursements followed specific written guidance provided by the Commission for committees who discover a misappropriation or embezzlement of committee funds. Specifically, where a committee's reported cash on hand balance is inaccurate, the Commission advised making a one-time cash adjustment on the committee's next report to reflect the actual balance by either:

- Adjusting the beginning cash on hand balance of the report manually, with memo text referencing a Form 99 providing details concerning the embezzlement; or
- Making a one-time cash-on-hand adjustment entry on Schedule B with the purpose: "Cash-on-hand adjustment due to unauthorized disbursements."

(See Guidance for Political Committees Regarding Embezzlement/Misappropriation.) Moreover, the Committee's counsel received and discussed the foregoing written guidance as applied to the Committee with a number of RAD management and staff members at the Commission's regional conference held on October 25-26, 2011, in San Diego, California.

b. Receipts of \$55,107.88. The Committee disclosed the following receipts on Schedule A, Line 17, on its Year-End Report:

- Los Angeles County Democratic Party – State Candidate Committee, 09/13/2011, \$10,000;

- Los Angeles County Democratic Party – State Candidate Committee, 09/13/2011, \$19,672.39;
- Los Angeles County Democratic Party – State Candidate Committee, 09/13/2011, \$15,435.49; and
- Los Angeles County Democratic Party – State Candidate Committee, 09/13/2011, \$10,000.

Each of the itemized receipts was accompanied by a memo text entry stating, "The Transfer from the Committee's non-federal account is based on expenditures made/reported by the Committee's former treasurer, Kinde Durkee. At this time, the Committee is unable to identify or itemize on Schedule H the allocable administrative expenses comprising the transfer amount."

The Committee pays for allocable administrative expenses using its federal account, and within 60 days, makes a transfer from its non-federal account for the non-federal share of such allocable costs. The Committee discloses such reimbursements from nonfederal accounts to federal accounts on Schedule H3. After the Committee retained new counsel and a new Treasurer, the Committee was in a precarious position of having made allocable payments using its federal funds while Ms. Durkee served as treasurer, but had not yet reimbursed the federal account from its state accounts for allocable administrative expenses. Because the Committee had knowledge of the total amount of transferrable those allocable expenses, but not a list of itemized allocable expenses making up that transfer, the Committee chose to disclose the transfers on Schedule A with the explanation above. Again, the Committee's counsel consulted with RAD regarding how best to disclose the transfers. The memo text accompanying the four receipts was also provided to RAD for approval prior to filing the Year-End Report.

2. The Committee had internal controls in place at the time Ms. Durkee misappropriated the Committee's funds, and has adopted additional internal controls to reduce the Committee's exposure to such actions in the future.

The Committee had internal controls in place to provide oversight of the Committee's financial transactions. In addition to hiring the experienced campaign finance firm of Durkee & Associates, the Committee also retained an experienced law firm to oversee the Committee's activities and finances. The committee's controls included:

- a. **Approval of Expenditures.** While Ms. Durkee (and certain members of her staff) had signing authority over the Committee's bank account, payments from the Committee's accounts were only permitted if they were authorized by one of three designated Committee representatives: the Committee's Chair, Executive Director and Controller.¹ None of these representatives were employed by or had any business relationship with Ms. Durkee.

¹ Certain recurring monthly payments and payroll transactions did not require ongoing approval from a Committee representative once they were initially authorized.

- b. Separation of Tasks. The Committee was assured on numerous occasions that Ms. Durkee's office divided the financial and reporting tasks among its employees. Thus, an "account executive" was responsible for the day-to-day management of the Committee's finances, while a separate Durkee employee was responsible for preparing campaign reports. The Committee was told that account reconciliations were performed by a third Durkee & Associates employee. This division of responsibilities was apparent when the Committee's representatives dealt with different personnel in Ms. Durkee's office, depending on the task involved.
- c. Review of Financial Reports. The Committee received almost daily financial reports from Ms. Durkee's office that tracked the Committee's activities, which were generally sent to at least two officers of the Committee and its then counsel. Thus, the Committee believed that it had sufficient oversight of its finances. The Committee did not regularly receive copies of bank statements from its prior Treasurer; however, that information, on its own, may not have been sufficient to prevent the type of widespread fraud that occurred here. Given the number of accounts that the Los Angeles County Democratic Party maintains and the number of internal transfers that routinely take place among the Party's various state and federal committees, it is possible that some unauthorized activity could go unrecognized for a period of time regardless of the number of controls in place.

The safe harbor provisions issued by the FEC do not adequately address the scenario where a Committee hires a professional treasurer to manage the Committee's finances and file campaign reports. Essentially, hiring a professional treasurer substitutes for implementing some of the safeguards listed in the Commission's safe harbor policy. Generally, when a professional treasurer is hired, the treasurer makes the deposits, signs the checks and reconciles the bank accounts. Thus, it is incumbent upon the Committee to hold the treasurer accountable, but not necessarily to perform these tasks itself. This issue regarding internal controls was discussed at length with the Commission at the Committee's recent audit hearing (see below).

Nonetheless, the Committee has retained a new firm to provide compliance and legal services, and has implemented additional practices to ensure as much accountability as possible. Among other things, the Committee has adopted the following new safeguards:

- a. The Committee receives copies of its monthly bank statements and reconciliation reports from its new compliance firm.
- b. The Committee has access to its bank account so it can verify its account activity on a regular basis.
- c. The Committee representatives may not approve payments or reimbursements for themselves.

While these efforts may not completely prevent fraudulent activities from occurring, the Committee believes these additional steps will reduce the Committee's exposure to such actions in the future.

3. Although the Committee did not make a formal *sua sponte* submission, the Committee self-reported Ms. Durkee's misconduct to the Commission on several occasions, including an audit hearing presentation and multiple written submissions to the Commissioners and Commission staff in the context of the audit.

According to the Commission's policy regarding self-reporting of campaign finance violations, the Commission will generally offer penalties between 25% and 75% lower than the Commission would otherwise have sought in identical matters arising by external complaints, referrals from other government agencies, "in order to encourage the self-reporting of violations about which the Commission would not otherwise have learned." (See FEC Policy Regarding *Sua Sponte* Submissions, 72 Fed. Reg. 65, p. 16695 (emphasis added).) Although the Committee did not submit a formal *sua sponte* submission to the Office of the General Counsel prior to your notice, the Committee has on several occasions, put the Commission on notice and discussed in great detail, the fraudulent actions of Ms. Durkee and the Committee's cash-on-hand and other discrepancies resulting from Ms. Durkee's misconduct.

At an audit hearing held on December 14, 2011, the Committee's new counsel and Chair provided details relating to Ms. Durkee's embezzlement, comingling of Committee funds, and subsequent cover-up scheme, that continued until the time of Ms. Durkee's arrest on September 2, 2011. The Committee also provided written submissions before and after the audit hearing, including an itemization of the internal controls in place at the time of Ms. Durkee's misconduct, as well as additional controls put in place immediately following the discovery of her actions. (See Letters to the Audit Division, dated Oct. 6, 2011 and Feb. 21, 2012.) While the Committee did not submit a formal *sua sponte* submission to the Office of the General Counsel, the Committee's disclosure of possible violations "about which the Commission would not otherwise have learned," was achieved by the hearing and written submissions to the Commission.

At the audit hearing, the Commissioners agreed that the Committee has been the true victim in this matter. Further, at its June 7, 2012 meeting, the Commission voted 6-0 to direct staff to bring back a Final Audit Report that accurately and clearly described the misstatements of financial information at issue in the audit as completely unauthorized by the Committee. Additionally, the Commission requested that the report suggest, to the extent legally possible, that the transactions in question fit the pattern of embezzlement and cover-up for which Ms. Durkee pleaded guilty earlier this year.

As stated in the Commission's policy regarding *sua sponte* submissions, the Commission may take into account various factors in considering how to proceed regarding self-reported violations. (See FEC Policy Regarding *Sua Sponte* Submissions, 72 Fed. Reg. at 16696.) In general, "more expedited processing and a more favorable outcome will result" when a committee can show that: (1) there was an immediate end to the activity giving rise to the

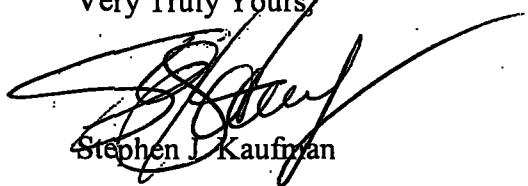
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violation; (2) the respondent makes a timely and complete disclosure to the Commission and fully cooperates in the disposition of the matter; and (3) the respondent implements appropriate and timely corrective measures. Here, the Committee (1) immediately terminated Ms. Durkee as soon as it was made aware of her embezzlement and other misconduct, and retained a new firm to provide compliance and legal services; (2) provided extensive details to the Commission and to the public relating to Ms. Durkee's misconduct, and will continue to fully cooperate in the disposition of the matter; and (3) implemented appropriate and timely corrective measures, including the adoption of additional internal controls, described above, to reduce the Committee's exposure to such actions in the future.

Based on the foregoing, we urge the Commission to take no further action against the Committee and its current Treasurer in connection with this referral. For your reference, I am enclosing copies of our written submissions detailing Ms. Durkee's misconduct and the Committee's subsequent remedial actions. Please contact me should your office require additional information in connection with this referral.

Thank you for your consideration of our response.

Very Truly Yours,



Stephen J. Kaufman

SJK:sjs

Enclosure