LRA 878
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FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

February 7, 2013

MEMORANDUM

TO: Thomas Hintermister
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FROM: Lisa J. Stevenson LJS
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SUBJECT: Draft Final Audit Report – Canseco for Congress
(LRA 878)

I. INTRODUCTION

The Office of the General Counsel reviewed the proposed Draft Final Audit Report ("DFAR") on Canseco for Congress ("Committee") as well as the response to the Interim Audit Report ("IAR") submitted by the Committee. We concur with any findings not discussed herein. In this memorandum, we address the receipt of apparent prohibited contributions issue (Finding 1) and concur with the Audit Division. If you have any questions, please contact Danita C. Alberico, the attorney assigned to this audit.

II. THE SOURCE OF FUNDS FOR LOANS TO THE COMMITTEE WAS NOT THE CANDIDATE'S PERSONAL FUNDS

A. Legal and Factual Background

The DFAR examines two transactions totaling $100,000. The immediate apparent source of the funds is Inmuebles Caza, S.A., de C.V., ("Caza"), a foreign national corporation registered in Mexico. The funds were deposited in the Committee's bank account in two installments. One

deposit totaling $14,000 was made by an electronic funds transfer from a Caza account to the Committee's account on January 29, 2010. The Candidate made the second deposit to the Committee's account, totaling $86,000, using a cashier's check remitted by Caza and payable to the Candidate. The DFAR concludes that the transactions are contributions from a foreign national and therefore prohibited by 2 U.S.C. § 441e.

The Committee contends that the $100,000 deposited in the Committee's account consisted of loans made by the Candidate to the Committee from his personal funds. The Committee states that $42,000 of that sum represents the Candidate's "equitable share of assets held by Canseco Investments, Ltd. ("Canseco, Ltd."), less tax liability, which was advanced to him by the company [Canseco, Ltd., presumably]." Letter from Chris K. Gober, Counsel, Canseco for Congress, to T[o]m Hintermister dated September 12, 2012 ("Committee Response"). The Committee also indicates that the remaining $58,000 represents the proceeds of a personal loan that the Candidate received from his sister. The Committee asserts that the funds lent to him by his sister represented her share of assets held by Canseco, Ltd. and that she received the loan against her equitable interest in Canseco, Ltd. under the same conditions as the Candidate. *Id.* at 3-4. The Committee represents that the Candidate and his sister own Canseco, Ltd. along with their other siblings. *Id.* at 2. Canseco, Ltd. is registered in Texas as a domestic limited partnership. The Committee explains that Canseco, Ltd. owns Caza but that because Canseco Ltd. "does not maintain funds in its own bank account . . . all of the expenses and payments on behalf of Canseco [Ltd.] are made directly by Caza in the ordinary course of business." *Id.*

The Committee states that the partners in Canseco, Ltd. intended "to provide the Candidate with access to his equitable share of Canseco [Ltd.'s] assets less the company's projected tax liability upon distribution." Committee Response at 2. The Committee asserts, however, that "due to various tax concerns, the company ultimately made two separate loans to the Candidate with funds maintained in Caza's bank account." *Id.* at 3. The Committee contends that "the funds 'derive from' an asset over which the Candidate had a legal ownership share and equitable interest in [and therefore] they should be treated as personal funds." *Id.* The Committee stated that the loans the Candidate received were secured by his ownership interest in Canseco, Ltd. and that Canseco, Ltd. earned "10-14 [percent] on funds that they otherwise could not distribute." *Id.* The Committee submitted an Internal Revenue Service Schedule K-1 (Partner's Share of Income, Deductions, Credits, etc.) which identified the Candidate as a partner of Canseco, Ltd., listed his ownership percentage and reflected his ending capital balance in Canseco, Ltd. totaling $56,772. *Id.* at Attachment A. The K-1 line item ordinarily reflecting a distribution was redacted, and thus we are unable to determine whether Canseco, Ltd. made any distributions to the Candidate. *Id.*

The K-1 did not include any information on Caza. The Committee submitted an affidavit from the President of Caza, Jorge Canseco (the Candidate's brother). The affidavit states that the Candidate owns 12.125% of Canseco Ltd. and that Canseco Ltd. owns 99% of Caza. Affidavit of Jorge Canseco dated September 25, 2012 ("Affidavit"). The Affidavit also states that "loan proceeds were paid [to the Candidate] from Caza's bank account because Canseco [Ltd.] did not maintain the funds in its own bank account." Affidavit at 1. Jorge Canseco attests that the

Candidate was obligated to repay the loan and if he did not do so he would "forfeit his ownership interest in Canseco [Ltd.]." *Id.* at 2. The Affidavit said that Caza made a similar loan payout to the Candidate's sister on behalf of Canseco, Ltd. *Id.*

The issue presented here is whether the actual source of the loan from the Candidate and his sister to the Committee is the Candidate's personal funds when the funds were paid directly by a foreign national corporation, Caza, an asset of a U.S. limited partnership (Canseco, Ltd.) of which the Candidate and his sister are partners. We conclude that the $100,000 in funds was not a loan from the Candidate to the Committee using his personal funds. Rather, the funds are either foreign national contributions or partnership contributions.

A candidate for Federal office may make unlimited expenditures from personal funds. 11 C.F.R. § 110.10. Personal funds of a candidate consist of assets, income, or jointly owned spousal assets. 11 C.F.R. § 100.33. Assets are "[a]mounts derived from any asset that, under applicable State law, at the time the individual became a candidate, the candidate had legal right of access to or control over, and with respect to which the candidate had (1) [l]egal and rightful title; or (2) [a]n equitable interest." 11 C.F.R. § 100.33(a). Personal funds may also consist of income received by the Candidate during the current election cycle and includes, among other things, income from the candidate's stocks or other investments including interest, dividends, or proceeds from the sale or liquidation of such stocks or investments. 11 C.F.R. § 100.33(b)(2).

It is unlawful, however, for a foreign national, directly or indirectly, to make a contribution or donation of money or other value, or to make an express or implied promise to make a contribution or donation, in connection with a Federal, State or local election. 2 U.S.C. § 441e(a)(1)(A); 11 C.F.R. § 110.20(b). It is also unlawful for a person to solicit, accept, or receive a contribution or donation from a foreign national. 2 U.S.C. § 441e(b). The term "person" includes a corporation or a committee. 2 U.S.C. § 431(11). The term "foreign national" includes a "foreign principal" as defined by 22 U.S.C. § 611(b). *See* 2 U.S.C. § 441e(b)(1). Section 611(b) defines a "foreign principal" to include a partnership, association, corporation, organization, or other combination of persons organized under the laws of or having its principal place of business in a foreign country. *Id.*

A partnership may contribute to a political committee, but a contribution by a partnership shall not exceed the limitations on contributions. 11 C.F.R. § 110.1(e). A contribution by a partnership shall be attributed to the partnership and to each partner in direct proportion to his or her share of the partnership profits, according to instructions which shall be provided by the partnership to the political committee or candidate or by agreement of the partners. 11 C.F.R. § 110.1(e). Only the profits of the partners to whom the contribution is attributed are reduced (or losses increased), and these partners' profits are reduced (or losses increased) in proportion to the contribution attributed to each of them. No portion of such a contribution may be made from the profits of a corporation that is a partner. 11 C.F.R. § 110.1(e).

B. The Candidate's Personal Funds Were Not the Source of the $100,000 Contribution to the Committee

The IAR sought information from the Committee showing that all or a portion of the $100,000 deposited in the Committee's account was composed of the Candidate's personal funds consistent with 11 C.F.R. § 100.33. Specifically, the IAR sought evidence such as accounting and/or bank records demonstrating that the true source of the funds was the Candidate's capital account in Canseco, Ltd. *and* that under applicable law and the partnership agreement the Candidate's capital account met the definition of an "asset" in 11 C.F.R. § 100.33(a). Alternatively, the IAR sought evidence demonstrating that the funds paid to the Candidate represented interest, dividends, a profit-sharing distribution, or proceeds from the sale or liquidation of the *Candidate's* assets or other information demonstrating that the funds at issue were the Candidate's personal funds.

The Committee's response describes the flow of funds enabling the Candidate to make the $100,000 loan to the Committee. The Committee's response also shows that Canseco, Ltd. owns Caza. The Committee's information, however, does not establish that the funds at issue constituted the Candidate's personal funds. The Committee provided a copy of the Candidate's K-1 but did not submit any evidence showing that the payments to the Candidate were drawn from funds in his capital account at Canseco, Ltd., or that the payments represented interest, dividends, a profit-sharing distribution, or proceeds from the sale or liquidation of the Candidate's assets. 11 C.F.R. § 100.33(b)(2).

Rather, the Committee's response and Jorge Canseco's affidavit emphasized that the funds provided to the Candidate were loans. Indeed, the Committee attached promissory notes to its response, reflecting the nature of these funds as loans to the Candidate. Attachment B-E to Committee Response. A loan made by any person, including a partnership or corporation, for the purpose of influencing any election for Federal office is a contribution. 11 C.F.R. § 100.52(a). A loan is a contribution at the time it is made and is a contribution to the extent that it remains unpaid. 11 C.F.R. § 100.52(b)(2). Since the $100,000 in funds that the Candidate received was a loan from either Canseco, Ltd. or Caza, it constitutes a contribution from one of those two entities. Consequently, the funds cannot be considered the Candidate's personal funds within the meaning of 11 C.F.R. § 100.33.[1]

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[1] With respect to the funds the Candidate received from his sister, if it could be established that $58,000 loaned to the Candidate from his sister constituted her personal funds, rather than the funds of one of the two entities, our analysis might lead us to conclude that the Committee received an excessive contribution from the Candidate's sister. Although the sister's loan was structured as a personal debt owed by the Candidate to his sister, the funds were deposited directly to the Committee's account after being endorsed by the Candidate. Any candidate who receives a loan for use in connection with his or her campaign is deemed, by operation of law, to do so as an agent of the authorized committee. 2 U.S.C. § 432(e)(2). Accordingly, even if the Commission accepted that the transaction was a loan from the Candidate's sister, the Candidate would have received the loan as the Committee's agent. The loaned funds were directly deposited in the Committee's account and used in connection with the Candidate's election campaign. The funds, therefore, could not be considered the Candidate's personal funds but rather would be an excessive contribution from his sister.

C. Caza, A Foreign National Corporation, Is the Prohibited Source of the Candidate's $100,000 Contribution to the Committee

We conclude that Caza is the source of the Candidate's $100,000 loan to the Committee because the funds were, in fact, paid directly from Caza's bank account and Caza is listed as the lender (or co-lender) on the underlying promissory notes.[2] The Committee claims that the funds paid out of Caza's account are actually Canseco, Ltd. funds because: (1) Canseco, Ltd. owns 99% of Caza; and (2) Caza transacts financial business for Canseco, Ltd. because the partnership does not "maintain funds" in its bank account. The percentage of ownership by an American parent company of a foreign subsidiary and where the companies maintain their funds are not factors in determining foreign national status. *See* 2 U.S.C. § 441e(b)(1) and 22 U.S.C. §611(b). Caza is organized under the laws of Mexico, and it provided $100,000 to the Candidate and his sister in connection with the Candidate's U.S. Congressional election campaign. Since Section 441e prohibits contributions by a foreign national through any other person, and since Caza is both a person, 2 U.S.C. § 431(11), and a foreign national by application of 22 U.S.C. § 611(b)(3), it follows that funds loaned by Caza to the Candidate and his sister, directly or indirectly, constituted an impermissible contribution in connection with a Federal election. We conclude that the $100,000 in funds originating from Caza and deposited in the Committee's account did not lose their character as foreign national contributions merely because Caza is an asset held by a U.S. limited partnership. Therefore, we concur with the Audit Division that Caza, as a foreign national company, made a $100,000 contribution to the Committee in violation of 2 U.S.C. § 441e.

The Committee's response, however, contends that the source of the $100,000 was loans made to the Candidate and his sister from their partnership – Canseco, Ltd – and not Caza. Even if we accept as true that the funds constituted loans from Canseco, Ltd., we would conclude that the partnership made a prohibited excessive contribution to the Committee, as discussed in Section D, below.

D. If Canseco, Ltd. Funded the Loans then the Partnership Made an Apparent Excessive Contribution to the Committee

As discussed in Section B, above, a contribution is defined to include a loan and a loan is a contribution at the time it is made. *See* 2 U.S.C. § 431(8)(A)(1) and 11 C.F.R. § 100.52(b)(2). The Commission has consistently treated a contribution by a business owner that is funded by a loan from the business as a contribution by the business. In MUR 3191 (Christmas Farm, Inc., *et al.*), the Commission determined that there was probable cause to believe that a candidate's contribution to his campaign of $209,000 that he withdrew from a corporation, of which he was a 50% shareholder, constituted contributions by the corporation because the draws were against his

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[2] Canseco Ltd. and Caza are listed as co-lenders on a $30,000 promissory note issued to the Candidate dated January 28, 2010. Att. B to Committee Response. Caza is listed as the sole lender on a $28,000 note to the Candidate dated April 12, 2010, and on a $58,000 note to the Candidate's sister also dated April 12, 2010. Att. C-D to Committee Response. The sister, in turn, is listed as the lender on a $58,000 note from the sister to the Candidate dated April 12, 2010. Att. E to Committee Response.

personal equity in the corporation (indicating that his equity served as collateral for a loan) rather than a reduction of his equity interest (which would have constituted a withdrawal of his own funds). The withdrawal thereby had the effect of a loan from a repayable drawing account and, indeed, the corporation recorded the transaction as a loan. *See* Factual and Legal Analysis, MUR 3191 (Christmas Farm, Inc., *et al.*); *see also* MUR 3119 (Edmar Corp.) (finding probable cause to believe that corporation contributed to a candidate, a shareholder of the corporation, by loaning the shareholder/candidate $266,000 that the candidate then contributed to his campaign).[3]

The Committee characterizes the funds provided to the Candidate and his sister as loans from Canseco, Ltd. to be repaid with interest. The Committee admits that the sums were not distributions and that the Candidate's and his sister's ownership interest in Canseco, Ltd. were merely held as security against the loans in the event of default. In fact, Jorge Canseco said that "the amount of the *loan* was determined by the company's accountants (Canseco, Ltd., presumably) to ensure that the value of the *loan* did not exceed the cash value of [the Candidate's] ownership interest in [Canseco, Ltd.], less the amount of taxes the company would owe *were it to make a distribution of the funds maintained in Caza's bank account.*" Affidavit at 2. (Emphasis added). Thus, even if we accept as true that the source of the loans was Canseco, Ltd., rather than Caza, based on the Commission precedent discussed above, we would nevertheless conclude that Canseco, Ltd. made an excessive contribution to the Committee in violation of 11 C.F.R. §§ 110.1(b)(1) and 110.1(e).[4]

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[3] The Commission has also consistently applied these principles in its advisory opinions. The Commission has evaluated in each case whether a proposed transaction constituted a loan from a business to the contributor to make a contribution, in which case the request was denied, or whether the proposed transaction constituted the routine and irreversible payment of income to the contributor, in which case the request was approved. *See, e.g.*, Advisory Op. 2005-20 (Pillsbury, Winthrop, Shaw, Pittman, LLP) at 3 & n.3 (systematic monthly distributions of actual or anticipated partner profits to partners based on their assigned share of the profits become the personal assets of the partners and, if used for contributions, would not constitute contributions by the partnership); Advisory Op. 1997-09 (Chicago Board of Trade) (no prohibited corporate contributions or contributions in the name of another if traders used their personal trading account to make contributions so long as the trader's firm did not extend credit or advance funds to the trader "and thus make the contribution itself"); Advisory Op. 1984-10 (Arnold & Porter LLP) (Commission denied request by law firm to pay for contributions made in the name of its partners that would subsequently be deducted from the partners' quarterly income distribution).

[4] If the $100,000 is treated as a partnership contribution, the amount attributable to the Candidate in accordance with Section 110.1(e) would not be excessive because a candidate can make unlimited expenditures from personal funds under Section 110.10. However, the amount attributable to the partnership itself would be excessive, and the amounts attributable to the other individual partners in Canseco, Ltd. would potentially be excessive depending on the total number of non-corporate partners, their respective share of the partnership profits and any other contributions they previously made, respectively, affecting their contributions limits for the Candidate. *See* 11 C.F.R. §§ 110.1(e) and 110.1(b).

FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

November 25, 2013

MEMORANDUM

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SUBJECT: Audit Division Resubmission of the Draft Final Audit Report on Canseco for Congress (LRA 878)

The Office of the General Counsel ("OGC") reviewed the resubmitted Draft Final Audit Report ("DFAR") on Canseco for Congress ("Committee"), the Committee's response to the Interim Audit Report ("IAR"), and additional documentation and information that the Committee submitted subsequent to its IAR response. The resubmitted DFAR contains the same three findings as the original DFAR: Receipt of Apparent Prohibited Contributions (Finding 1); Receipt of Apparent Excessive Contributions (Finding 2); and Misstatement of Financial Activity (Finding 3).

The Audit Division resubmitted the DFAR to OGC because the Committee's additional documentation and information caused the Audit Division to make significant changes to the amounts at issue in each of the findings as well as to the classification of some of the items at issue. The Committee did not raise any new or additional legal arguments in its subsequent submission of additional documentation and information and, despite the extent of the Audit Division's changes to the DFAR, the changes do not present any new or additional legal issues. Thus, we incorporate herein our legal analysis of February 7, 2013 on the original DFAR and concur with the resubmitted DFAR. We recommend that the Audit Division attach and forward to the Commission and the Committee this memorandum along with our prior legal analysis. If you have any questions, please contact Danita C. Alberico, the attorney assigned to this audit.