



Interim Audit Report of the Audit Division on Smoot for Congress

(March 11, 2009 - December 31, 2010)

Why the Audit Was Done

Federal law permits the Commission to conduct audits and field investigations of any political committee that is required to file reports under the Federal Election Campaign Act (the Act). The Commission generally conducts such audits when a committee appears not to have met the threshold requirements for substantial compliance with the Act.¹ The audit determines whether the committee complied with the limitations, prohibitions and disclosure requirements of the Act.

Future Action

The Commission may initiate an enforcement action, at a later time, with respect to any of the matters discussed in this report.

About the Campaign (p. 2)

Smoot for Congress is the congressional campaign committee for Sheila Smoot, Democratic candidate for the U.S. House of Representatives from the State of Alabama, 7th District, and is headquartered in Birmingham, Alabama. For more information, see the chart on the campaign organization, p.2.

Financial Activity (p. 2)

- **Receipts**
 - Contributions from Individuals \$ 151,083
 - Contributions from Other Political Committees 98,750
 - Total Receipts \$ 249,833**

- **Disbursements**
 - Operating Disbursements \$ 250,380
 - Other Disbursements 1,030
 - Total Disbursements \$ 251,410**

Findings and Recommendations (p. 3)

- Misstatement of Financial Activity (Finding 1)
- Receipt of Apparent Prohibited Contributions (Finding 2)

¹ 2 U.S.C. §438(b).

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Part I

Background

Authority for Audit

This report is based on an audit of Smoot for Congress (SFC), undertaken by the Audit Division of the Federal Election Commission (the Commission) in accordance with the Federal Election Campaign Act of 1971, as amended (the Act). The Audit Division conducted the audit pursuant to 2 U.S.C. §438(b), which permits the Commission to conduct audits and field investigations of any political committee that is required to file a report under 2 U.S.C. §434. Prior to conducting any audit under this subsection, the Commission must perform an internal review of reports filed by selected committees to determine if the reports filed by a particular committee meet the threshold requirements for substantial compliance with the Act. 2 U.S.C. §438(b).

Scope of Audit

Following Commission-approved procedures, the Audit staff evaluated various risk factors and as a result, this audit examined:

1. the receipt of excessive contributions and loans;
2. the receipt of contributions from prohibited sources;
3. the disclosure of individual contributors' occupation and name of employer;
4. the consistency between reported figures and bank records;
5. the completeness of records; and
6. other committee operations necessary to the review.

Part II

Overview of Campaign

Campaign Organization

Important Dates	
• Date of Registration	April 22, 2009
• Audit Coverage	March 11, 2009 - December 31, 2010
Headquarters	Birmingham, Alabama
Bank Information	
• Bank Depositories	Two
• Bank Accounts	Three
Treasurer	
• Treasurer When Audit Was Conducted	Adrienne Ellison
• Treasurer During Period Covered by Audit	Johanna Martin. March 11, 2009 - October 18, 2010; and Adrienne Ellison. October 18, 2010 - December 31, 2010
Management Information	
• Attended FEC Campaign Finance Seminar	No
• Who Handled Accounting and Recordkeeping Tasks	Paid Staff

Overview of Financial Activity (Audited Amounts)

Cash-on-hand @ March 11, 2009	\$ 0
Receipts	
○ Contributions from Individuals	151,083
○ Contributions from Other Political Committees	98,750
Total Receipts	\$ 249,833
Disbursements	
○ Operating Disbursements	250,380
○ Other Disbursements	1,030
Total Disbursements	\$ 251,410
Cash-on-hand @ December 31, 2010	\$ (1,577)²

² SFC overdrew a bank account in the amount of \$1,574. The bank later forgave this amount when the account was closed out. See Finding 2 for discussion of apparent prohibited contribution from the bank for this amount.

Part III Summaries

Findings and Recommendations

Finding 1. Misstatement of Financial Activity

A comparison of SFC's reported financial activity with its bank records revealed a misstatement of receipts and disbursements in calendar years 2009 and 2010. The Audit staff recommends that SFC amend its disclosure reports to correct the misstatements. (For more detail, see p. 4.)

Finding 2. Receipt of Apparent Prohibited Contributions

Based on a review of all contributions received by SFC, the Audit staff identified 15 contributions totaling \$9,994 that appear to be from prohibited sources. The Audit staff recommends that SFC demonstrate that the contributions were made with permissible funds or refund them. (For more detail, see p. 6.)

Part IV

Findings and Recommendations

Finding 1. Misstatement of Financial Activity

Summary

A comparison of SFC's reported financial activity with its bank records revealed a misstatement of receipts and disbursements in calendar years 2009 and 2010. The Audit staff recommends that SFC amend its disclosure reports to correct the misstatements.

Legal Standard

Contents of Reports. Each report must disclose:

- the amount of cash-on-hand at the beginning and end of the reporting period;
- the total amount of receipts for the reporting period and for the election cycle;
- the total amount of disbursements for the reporting period and for the election cycle; and
- certain transactions that require itemization on Schedule A (Itemized Receipts) or Schedule B (Itemized Disbursements). 2 U.S.C. §434(b)(1), (2), (3), (4) and (5).

Facts and Analysis

A. Facts

The Audit staff reconciled SFC's reported activity with its bank records and identified a misstatement of receipts and disbursements for 2009 and 2010. The following charts detail the discrepancies and succeeding paragraphs explain the reasons for the misstatements, if known.

2009 Activity			
	Reported	Bank Records	Discrepancy
Beginning Cash Balance @ March 11, 2009	\$0	\$0	\$0
Receipts	\$60,008	\$60,038	\$(30) Understated
Disbursements	\$55,674	\$54,678	\$996 Overstated
Ending Cash Balance @ December 31, 2009	\$4,334	\$5,360	\$(1,026) Understated

SFC understated receipts in 2009 by \$30. However, when evaluating the identified errors, regardless of whether the errors were positive or negative (absolute values), Audit staff discovered that the committee misstated receipts by \$5,694 (\$2,862 + \$2,270 + \$562).

The misstatement of receipts resulted from the following differences:

• Receipts not reported, primarily contributions from individuals	\$2,862
• Receipts reported twice	2,270
• Reported receipts not supported by bank deposits or credits	<u>562</u>
Sum of Reporting Adjustments	<u>\$5,694</u>

SFC overstated disbursements in 2009 by \$996. However, when evaluating the identified errors, regardless of whether the errors were positive or negative (absolute values), Audit staff discovered that the committee misstated disbursements by \$4,305 (\$1,383 + 2,922).

The misstatement of disbursements resulted from the following differences:

• Disbursements not reported	\$1,383
• Disbursements reported not supported by canceled checks	<u>2,922</u>
Sum of Reporting Adjustments	<u>\$4,305</u>

2010 Activity			
	Reported	Bank Records	Discrepancy
Opening Cash Balance January 1, 2010	\$4,334	\$5,360	\$(1,026) Understated
Receipts	\$170,698	\$189,795	\$(19,097) Understated
Disbursements	\$199,604	\$196,732	\$2,872 Overstated
Ending Cash Balance December 31, 2010	\$(24,572)	\$(1,577)	\$(22,995) Understated

The understatement of receipts resulted from the following:

• Receipts not reported	\$22,417
• Receipts reported twice or incorrectly	(410)
• Reported contributor checks returned by bank for insufficient funds with no report adjustments	(700)
• Reported receipts not supported by bank deposits or credits	(1,810)
• Bank correction erroneously reported as receipt	<u>(400)</u>
Net Understatement of Receipts	<u>\$19,097</u>

SFC overstated disbursements in 2010 by \$2,872. However, when evaluating the identified errors, regardless of whether the errors were positive or negative (absolute values), Audit staff discovered that the committee misstated disbursements by \$35,357 (\$15,481 + 19,876).

The misstatement of disbursements resulted from the following differences:

• Disbursements not reported	\$15,481
• Disbursements reported not supported by canceled checks	<u>19,876</u>
Sum of Reporting Adjustments	<u>\$35,357</u>

The reporting discrepancies noted above resulted in the \$22,995 understatement of the ending cash balance.

B. Interim Audit Report & Audit Division Recommendation

Audit staff and SFC representatives discussed this matter at the exit conference held at the end of audit fieldwork. SFC representatives acknowledged the discrepancies in the reports and indicated that the committee would file corrective amendments.

The Audit staff recommends that, within 30 calendar days of receipt of this report, SFC:

- amend its reports to correct the misstatements for 2009 and 2010 as noted above; and
- amend its most recently filed report to correct the cash-on-hand balance with an explanation that the change resulted from a prior period audit adjustment.

Further, SFC should recencile the cash balance on its most recent report to identify any subsequent discrepancies that may impact the \$22,995 adjustment recommended by the Audit staff.

Finding 2. Receipt of Apparent Prohibited Contributions

Summary

Based on a review of all contributions received by SFC, the Audit staff identified 15 contributions totaling \$9,994 that appear to be from prohibited sources. The Audit staff recommends that SFC demonstrate that the contributions were made with permissible funds or refund them.

Legal Standard

A. Receipt of Prohibited Contributions – General Prohibition. Candidates and committees may not accept contributions (in the form of money, in-kind contributions or loans) from the treasury funds of the following prohibited sources:

- corporations (this means any incorporated organization, including a non-stock corporation, an incorporated membership organization, and an incorporated cooperative);
- labor organizations; or
- national banks. 2 U.S.C. §441b.

B. Definition of Limited Liability Company. A limited liability company (LLC) is a business entity recognized as an LLC under the laws of the state in which it was established. 11 CFR §110.1(g)(1).

C. Applications of Limits and Prohibitions to LLC Contributions. A contribution from an LLC is subject to contribution limits and prohibitions, depending on several factors, as explained below:

1. LLC as Partnership. The contribution is considered a contribution from a partnership if the LLC chooses to be treated as a partnership under Internal

Revenue Service (IRS) tax rules, or if it makes no choice at all about its tax status. 11 CFR §110.1(g)(2).

2. LLC as Corporation. The contribution is considered a corporate contribution—and is barred under the Act—if the LLC chooses to be treated as a corporation under IRS rules, or if its shares are traded publicly. 11 CFR §110.1(g)(3).
3. LLC with Single Member. The contribution is considered a contribution from a single individual if the LLC is a single-member LLC that has not chosen to be treated as a corporation under IRS rules. 11 CFR §110.1(g)(4).
4. At the time it makes the contribution, an LLC shall provide to the recipient committee information on how the contribution is to be attributed and affirm that it is eligible to make the contribution. 11 CFR §110.1(g)(5).

D. Questionable Contributions. If a contribution that presents genuine questions about its permissibility is received and deposited, the treasurer shall make his or her best efforts to determine whether it is from a prohibited source. If the legality of the contribution cannot be verified in 30 days of the treasurer's receipt, it shall be refunded to the contributor. 11 CFR §103.3(b)(1).

Facts and Analysis

A. Facts

Based on a review of all contributions received by SFC, the Audit staff identified 15 contributions totaling \$9,994 that appear to be from prohibited sources. This amount includes contributions from twelve LLCs, totaling \$7,720, two corporations, totaling \$700 and one national bank, totaling \$1,574.

Audit staff requested that SFC provide documentation confirming how each LLC elected to be treated under IRS rules at the time the contributions were made. To date, no such documentation has been provided from SFC. Audit staff verified the corporate status with the appropriate Secretaries of State and could not determine the status of one of the entities.

SFC incurred a negative bank account balance in November 2010, when it overdrew its account with a debit charge for a rental car. In January 2011, the account was closed when the bank posted a \$1,574 credit. No information was provided to indicate that the credit posted by the bank was the result of a deposit by the committee.

B. Interim Audit Report & Audit Division Recommendation

The Audit staff requested that SFC provide documentation from the bank explaining this transaction. The candidate stated that SFC would provide a letter from the bank. To date, no such letter has been provided. Audit staff and committee representatives discussed this matter at the exit conference held at the end of audit fieldwork. Audit staff requested that SFC provide documentation verifying that the contributions in question were permissible. To date, SFC has not submitted any additional documentation concerning this matter.

The Audit staff recommends that, within 30 calendar days of service of this report, SFC provide evidence demonstrating that the contributions in question were made with permissible funds. For contributions in question from LLCs, SFC should provide documentation from each entity explaining its tax treatment. SFC should also provide documentation from the bank explaining the \$1,574 credit posted to SFC's account.

If SFC does not provide evidence that the funds were permissible, then it should make refunds to the contributors or disgorge to the U.S. Treasury the impermissible amounts. SFC should provide evidence of any refunds by providing the front and back of the negotiated refund checks.

If funds are not available to make the necessary refunds or disgorgement, SFC should disclose the contributions requiring refunds on Schedule D (Debts and Obligations) until funds become available to make such refunds.