



Interim Audit Report of the Audit Division on the Freedom's Defense Fund

(January 1, 2011 - December 31, 2012)

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 Committee (p. 2)

The Freedom's Defense Fund is a non-connected committee, headquartered in Arlington, Virginia. For more information, see the chart on Committee Organization, p.2.

Financial Activity (p. 2)

• Receipts	
○ Contributions from Individuals	\$ 3,626,052
○ Other Receipts	54,481
Total Receipts	\$ 3,680,533
• Disbursements	
○ Operating Expenditures	\$ 3,221,626
○ Contributions to Candidates/Committees	107,900
○ Independent Expenditures	376,492
○ Other Disbursements	14,728
Total Disbursements	\$ 3,720,746

Findings and Recommendations (p. 3)

- Misstatement of Financial Activity (Finding 1)
- Disclosure of Occupation and Name of Employer (Finding 2)
- Reporting of Apparent Independent Expenditures (Finding 3)
- Recordkeeping for Communications (Finding 4)

¹ 52 U.S.C. §30111(b).

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Part I

Background

Authority for Audit

This report is based on an audit of the Freedom's Defense Fund (FDF), 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 52 U.S.C. §30111(b), which permits the Commission to conduct audits and field investigations of any political committee that is required to file a report under 52 U.S.C. §30104. 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. 52 U.S.C. §30111(b).

Scope of Audit

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

1. the disclosure of individual contributors' occupation and name of employer;
2. the disclosure of debts and obligations pertaining to independent expenditures;
3. the consistency between reported figures and bank records;
4. the completeness of disbursement records;
5. the disclosure of independent expenditures; and
6. other committee operations necessary to the review.

Part II

Overview of Committee

Committee Organization

Important Dates	
• Date of Registration	June 7, 2004
• Audit Coverage	January 1, 2011 - December 31, 2012
Headquarters	Arlington, Virginia
Bank Information	
• Bank Depositories	One
• Bank Accounts	Three checking accounts
Treasurer	
• Treasurer When Audit Was Conducted	Scott Mackenzie
• Treasurer During Period Covered by Audit	Scott Mackenzie
Management Information	
• Attended Commission Campaign Finance Seminar	Yes
• Who Handled Accounting and Recordkeeping Tasks	Treasurer

Overview of Financial Activity (Audited Amounts)

Cash-on-hand @ January 1, 2011	\$ 46,043
Receipts	
○ Contributions from Individuals	3,626,052
○ Other Receipts	54,481
Total Receipts	\$ 3,680,533
Disbursements	
○ Operating Expenditures	3,221,626
○ Contributions to Candidates/Committees	107,900
○ Independent Expenditures	376,492
○ Other Disbursements	14,728
Total Disbursements	\$ 3,720,746
Cash-on-hand @ December 31, 2012	\$ 5,830

Part III

Summaries

Findings and Recommendations

Finding 1. Misstatement of Financial Activity

The Audit staff's comparison of FDF's reported financial activity with its bank records revealed that, for 2011, FDF understated its reported disbursements by \$52,357, and overstated its ending cash-on-hand balance by \$62,220. The Audit staff recommends that FDF amend its disclosure reports to correct these misstatements.

(For more detail, see p. 5.)

Finding 2. Disclosure of Occupation and Name of Employer

During audit fieldwork, a review of all contributions from individuals requiring itemization indicated that 2,911 contributions totaling \$378,639 lacked adequate disclosure of occupation and name of employer. FDF did not demonstrate "best efforts" to obtain, maintain and submit this information. The Audit staff recommends that FDF establish "best efforts" by filing amended reports to correct the disclosure of occupation and name of employer.

(For more detail, see p. 6.)

Finding 3. Reporting of Apparent Independent Expenditures

During audit fieldwork, the Audit staff reviewed disbursements to verify that the independent expenditures that FDF disclosed on Schedule E (Itemized Independent Expenditures) were reported accurately. FDF disclosed independent expenditures totaling \$385,619. The Audit staff identified additional disbursements disclosed as operating expenditures on Schedule B, Line 21b (Operating Expenditures) totaling \$868,015 which appear to be independent expenditures and for which no 24/48 hour reports were filed.

If FDF believes that the apparent independent expenditures totaling \$868,015 did not require reporting as independent expenditures, the Audit staff recommends that FDF provide evidence to support its conclusion. Absent such evidence, the Audit staff recommends that FDF amend its reports to disclose these disbursements as independent expenditures on Schedule E and submit revised procedures for reporting independent expenditures in the future. It is also recommended that FDF provide documentation to support the public dissemination for these communications to determine whether 24/48-hour reports were required to be filed.

(For more detail, see p. 8.)

Finding 4. Recordkeeping for Communications

During audit fieldwork, the Audit staff reviewed disbursements to verify the accuracy of the information and proper classification of transactions disclosed on reports. FDF reported 13 expenditures totaling \$90,814 on Schedule B, Line 21b (Operating Expenditures) with purposes of "direct mail – creative" and "direct mail – postage." Documentation that was provided by FDF was insufficient to make a determination pertaining to the purpose for these expenditures and verification as an operating expense. The Audit staff recommends that FDF provide, in sufficient detail, the necessary information from which the reported expenditures totaling \$90,814 may be verified or explained. Such records should include the missing copies of communications, and, if the communication has already been provided, information associating each communication with an invoice(s).

(For more detail, see p. 11.)

Part IV

Findings and Recommendations

Finding 1. Misstatement of Financial Activity

Summary

The Audit staff's comparison of FDF's reported financial activity with its bank records revealed that, for 2011, FDF understated its reported disbursements by \$52,357, and overstated its ending cash-on-hand balance by \$62,220. The Audit staff recommends that FDF amend its disclosure reports to correct these 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 calendar year;
- the total amount of disbursements for the reporting period and for the calendar year; and
- certain transactions that require itemization on Schedule A (Itemized Receipts) or Schedule B (Itemized Disbursements). 52 U.S.C. §30104(b)(1), (2), (3), (4), and (5).

Facts and Analysis

A. Facts

During audit fieldwork, the Audit staff reconciled FDF's reported financial activity with its bank records for calendar years 2011 and 2012. The reconciliation determined that FDF misstated disbursements and ending cash-on-hand for 2011. The following chart outlines the discrepancies between FDF's disclosure reports and its bank records. The succeeding paragraphs explain why the discrepancies occurred.

2011 Committee Activity				
	Reported	Bank Records	Discrepancy	
Beginning Cash-on-Hand @ January 1, 2011	\$43,781	\$46,043	(\$2,262)	Understated
Receipts	\$1,324,490	\$1,312,365	\$12,125	Overstated
Disbursements	\$1,293,431	\$1,345,788	(\$52,357)	Understated
Ending Cash-on-Hand @ December 31, 2011	\$74,840	\$12,620	\$62,220	Overstated

The understatement of disbursements resulted from the following differences:

• Contributions to candidates/committees not reported	\$ 51,650
• Vendor payment not reported	2,900
• Unexplained differences	<u>(2,193)</u>
Net Understatement of Disbursements	\$ 52,357

The \$62,220 overstatement of the ending cash-on-hand balance primarily resulted from the misstatements described above.

B. Interim Audit Report & Audit Division Recommendation

At the exit conference, the Audit staff provided work papers and discussed the reporting errors that caused the misstatements. The FDF Treasurer stated that amended reports would be filed to correct the misstatements.

The Audit staff recommends that, within 30 calendar days of service of this report, FDF amend its reports to correct the misstatements for 2011 as noted above.

Finding 2. Disclosure of Occupation and Name of Employer

Summary

During audit fieldwork, a review of all contributions from individuals requiring itemization indicated that 2,911 contributions totaling \$378,639 lacked adequate disclosure of occupation and name of employer. FDF did not demonstrate "best efforts" to obtain, maintain and submit this information. The Audit staff recommends that FDF establish "best efforts" by filing amended reports to correct the disclosure of occupation and name of employer.

Legal Standard

A. Itemization Required for Contributions from Individuals. A political committee other than an authorized committee must itemize any contribution from an individual if it exceeds \$200 per calendar year, either by itself or when combined with other contributions from the same contributor. 52 U.S.C §30104(b)(3)(A).

B. Required Information for Contributions from Individuals. For each itemized contribution from an individual, the committee must provide the following information:

- the contributor's full name and address (including zip code);
- the contributor's occupation and the name of his or her employer;
- the date of receipt (the date the committee received the contribution);
- the amount of the contribution; and
- the calendar year-to-date total of all contributions from the same individual. 52 U.S.C. §30104(b)(3)(A) and 11 CFR §§ 100.12 and 104.3(a)(4)(i).

C. Best Efforts Ensures Compliance. When the treasurer of a political committee shows that the committee used best efforts (see below) to obtain, maintain, and submit the information required by the Act, the committee's reports and records will be considered in compliance with the Act. 52 U.S.C. §30102(i).

D. Definition of Best Efforts. The treasurer and the committee will be considered to have used "best efforts" if the committee satisfied all of the following criteria.

- All written solicitations for contributions included:
 - a clear request for the contributor's full name, mailing address, occupation, and name of employer; and
 - the statement that such reporting is required by Federal law.
 - Note: The request and statement must appear in a clear and conspicuous manner on any response material included in a solicitation.
- Within 30 days of receipt of the contribution, the treasurer made at least one effort to obtain the missing information, in either a written request or a documented oral request.
- The treasurer reported any contributor information that, although not initially provided by the contributor, was obtained in a follow-up communication or was contained in the committee's records or in prior reports that the committee filed during the same two-year election cycle. 11 CFR §104.7(b).

Facts and Analysis

A. Facts

A review of all contributions from individuals requiring itemization indicated that 2,911 contributions totaling \$378,639, or 41% of total contributions from individuals required to be itemized by FDF, lacked disclosure of occupation and name of employer. The majority of the contributor entries (2,669 of 2,911) that lacked the required information were blank on the Schedules A (Itemized Receipts) filed with the Commission.

The Audit staff reviewed the contribution records provided by FDF to determine if it had utilized "best efforts" to obtain, maintain and submit the missing information.

- FDF did not provide documentation showing it made follow-up best efforts for 282 contributions totaling \$26,841 (\$378,639 - \$351,798).
- FDF had the required information for 2,629 contributions totaling \$351,798; however, this information was not disclosed on the FEC reports.

B. Interim Audit Report & Audit Division Recommendation

At the exit conference, the Audit staff provided schedules and discussed the omission of occupation and name of employer information from the disclosure reports. The FDF Treasurer commented that he had obtained some of the missing occupation and name of employer information. In its response to the exit conference, FDF provided a work paper demonstrating that FDF had obtained most of the missing occupation and name of employer information. FDF also provided copies of letters that it had sent to contributors

to obtain the missing occupation and name of employer information. This additional documentation demonstrated that FDF had obtained occupation and name of employer information for \$256,451 of the errors; however amended disclosure reports were not filed.² This amount is included in the \$351,798 noted above.

The Audit staff recommends that, within 30 calendar days of service of this report, FDF establish "best efforts" by amending its reports to disclose the missing information relating to the 2,629 contributions totaling \$351,798 (\$95,347 + \$256,451).

Finding 3. Reporting of Apparent Independent Expenditures

Summary

During audit fieldwork, the Audit staff reviewed disbursements to verify that the independent expenditures that FDF disclosed on Schedule E (Itemized Independent Expenditures) were reported accurately. FDF disclosed independent expenditures totaling \$385,619. The Audit staff identified additional disbursements disclosed as operating expenditures on Schedule B, Line 21b (Operating Expenditures) totaling \$868,015 which appear to be independent expenditures and for which no 24/48 hour reports were filed.

If FDF believes that the apparent independent expenditures totaling \$868,015 did not require reporting as independent expenditures, the Audit staff recommends that FDF provide evidence to support its conclusion. Absent such evidence, the Audit staff recommends that FDF amend its reports to disclose these disbursements as independent expenditures on Schedule E and submit revised procedures for reporting independent expenditures in the future. It is also recommended that FDF provide documentation to support the public dissemination for these communications to determine whether 24/48-hour reports were required to be filed.

Legal Standard

A. Definition of Independent Expenditures. The term "independent expenditure" means an expenditure by a person for a communication expressly advocating the election or defeat of a clearly identified candidate that is not made in coordination with any candidate or authorized committee or agent of a candidate. No expenditure shall be considered independent if the person making the expenditure allows a candidate, a candidate's authorized committee or their agents, or a political party committee or its agents to become materially involved in decisions regarding the communication as described in 11 CFR 109.21(d)(2), or shares financial responsibility for the cost of production or dissemination with any such person. 11 CFR §100.16.

² FDF's database contained the occupation and name of employer information for an additional 420 contributions totaling \$95,347.

- B. Disclosure Requirements – General Guidelines.** An independent expenditure shall be reported on Schedule E if, when added to other independent expenditures made to the same payee during the same calendar year, it exceeds \$200. Independent expenditures made (i.e., publicly disseminated) prior to payment should be disclosed as memo entries on Schedule E and as a debt on Schedule D. Independent expenditures of \$200 or less need not be itemized, though the committee must report the total of those expenditures on line (b) of Schedule E. 11 CFR §§104.3(b)(3)(vii), 104.4(a) and 104.11.
- C. Last-Minute Independent Expenditure Reports (24-Hour Reports).** Any independent expenditures aggregating \$1,000 or more, with respect to any given election, and made after the 20th day but more than 24 hours before the day of an election, must be reported and the report must be received by the Commission within 24 hours after the expenditure is made. A 24-hour report is required each time additional independent expenditures aggregate \$1,000 or more. The date that a communication is publicly disseminated serves as the date that the committee must use to determine whether the total amount of independent expenditures has, in the aggregate, reached or exceeded the threshold reporting amount of \$1,000. 11 CFR §§104.4(f) and 104.5(g)(2).
- D. Independent Expenditure Reports (48-Hour Reports).** Any independent expenditures aggregating \$10,000 or more for an election in any calendar year, up to and including the 20th day before an election, must be disclosed within 48 hours each time the expenditures aggregate \$10,000 or more. The reports must be filed with the Commission within 48 hours after the expenditure is made. A 48-hour report is required each time additional independent expenditures aggregate \$10,000 or more. The date that a communication is publicly disseminated serves as the date that the committee must use to determine whether the total amount of independent expenditures has, in the aggregate, reached or exceeded the threshold reporting amount of \$10,000. 11 CFR §§104.4(f) and 104.5(g)(1).
- E. Definition of Expressly Advocating.** The term “expressly advocating” means any communication that:
- Uses phrases such as “vote for the President,” “re-elect your Congressman,” “defeat” accompanied by a picture of one or more candidate(s), “reject the incumbent,” or communications of campaign slogan(s) or individual word(s), which in context can have no other reasonable meaning than to urge the election or defeat of one or more clearly identified candidate(s), such as posters, bumper stickers, advertisements; or
 - When taken as a whole and with limited reference to external events, such as the proximity to the election, could only be interpreted by a reasonable person as containing advocacy of the election or defeat of one or more clearly identified candidate(s) because:
 - the electoral portion of the communication is unmistakable, unambiguous, and suggestive of only one meaning; and

- o reasonable minds could not differ as to whether it encourages actions to elect or defeat one or more clearly identified candidate(s) or encourages some other kind of reaction. 11 CFR §100.22(a) and (b).

F. Formal Requirements Regarding Reports and Statements. Each political committee shall maintain records with respect to the matters required to be reported which shall provide in sufficient detail the necessary information and data from which the filed reports may be verified, explained, clarified, and check for accuracy and completeness. 11 CFR §104.14(b)(1).

Facts and Analysis

A. Reporting of Apparent Independent Expenditures

1. Facts

During audit fieldwork, the Audit staff reviewed disbursements to ensure that independent expenditures were disclosed correctly on Schedule E. FDF disclosed independent expenditures totaling \$385,619 on Schedule E. However, FDF also made media-related expenditures totaling \$868,015 and disclosed them as operating expenditures on Schedule B, Line 21b (Operating Expenditures), when it appears that they should have been reported as independent expenditures on Schedule E.

According to vendor invoices, FDF was billed \$868,015 for mailers. The invoices contained the mailer identification codes, the quantity of pieces mailed, the date that the pieces were mailed, and the cost of each mailing. A review of the mailers that were made available indicated that they contained language expressly advocating the election or defeat of a clearly identified candidate, which is Federal Election Activity that is required to be reported on Schedule E as defined under 11CFR §100.22(a).

A breakdown of the analysis for these expenditures is as follows:

Apparent Independent Expenditures Reported as Operating Expenditures (Copy of Communication Made Available)

FDF made 137 apparent independent expenditures totaling \$868,015 for which it provided supporting documentation such as invoices and the associated mailers for each invoice. All of these communications contained language expressly advocating the election or defeat of a clearly identified candidate, as defined under 11 CFR §.100.22(a).

The majority of the mailers advocated the defeat of Barack Obama in the 2012 general election. Some of the mailers included statements directly advocating defeat such as, "Barack Obama must be defeated," and "It's going to take a Herculean effort to defeat Barack Obama...this bully must be exposed and defeated." Other mailers contained language such as, "we conservatives need to start attacking Barack Obama's re-elect efforts NOW...if we're going to...do what's necessary to make Barack Hussein Obama a one-term president." and "It goes without saying that Barack Obama must be defeated...Together, you and I

must take Barack Obama and his liberal-progressive hacks head-on. This is the only way that they will be defeated!"

2. Interim Audit Report & Audit Recommendation

At the exit conference, the Audit staff presented schedules of apparent independent expenditure reporting errors. In response to the exit conference, the FDF Treasurer stated that FDF's position would be that these expenditures were fundraising expenditures and not independent expenditures.

The Audit staff recommends that, within 30 calendar days of service of this report, FDF provide documentation and evidence that apparent independent expenditures totaling \$868,015 did not require reporting as independent expenditures. Absent such evidence, the Audit staff recommends that FDF amend its reports to disclose these disbursements as independent expenditures on Schedule E and submit revised procedures for reporting independent expenditures.

B. Failure to File 24/48- Hour Reports for Independent Expenditures

1. Facts

During audit fieldwork, the Audit staff reviewed independent expenditures reported by FDF, as well as the apparent independent expenditures noted above, to determine whether additional reporting of 24/48-hour reports was required.³ As noted above, the Audit staff identified apparent independent totaling \$868,015 which may also require filing of 24/48-hour reports.

2. Interim Audit Report & Audit Recommendation

At the exit conference, the Audit staff presented schedules of independent expenditure reporting errors. The FDF Treasurer stated that FDF's position would be that these expenditures were fundraising expenditures and not independent expenditures.

Absent documentation and evidence that apparent independent expenditures totaling \$868,015 did not require reporting as independent expenditures (per Part A above), the Audit staff recommends that, within 30 calendar days of service of this report, FDF provide documentation to support the date of public dissemination for the communications to determine whether a filing of a 24/48-hour report was required.

Finding 4. Recordkeeping for Communications

Summary

During audit fieldwork, the Audit staff reviewed disbursements to verify the accuracy of the information and proper classification of transactions disclosed on reports. FDF

³ The date the expenditure is publicly distributed serves as the date that the independent expenditure is made for purposes of the 24/48-hour reports. FDF provided a master list of all mailers that included the mail date for each mailer on the list.

reported 13 expenditures totaling \$90,814 on Schedule B, Line 21b (Operating Expenditures) with purposes of “direct mail – creative” and “direct mail – postage.” Documentation that was provided by FDF was insufficient to make a determination pertaining to the purpose for these expenditures and verification as an operating expense. The Audit staff recommends that FDF provide, in sufficient detail, the necessary information from which the reported expenditures totaling \$90,814 may be verified or explained. Such records should include the missing copies of communications, and, if the communication has already been provided, information associating each communication with an invoice(s).

Legal Standard

- A. Formal Requirements Regarding Reports and Statements.** Each political committee shall maintain records with respect to the matters required to be reported which shall provide in sufficient detail the necessary information and data from which the filed reports may be verified, explained, clarified, and check for accuracy and completeness. 11 CFR §104.14(b)(1).
- B. Preserving Records and Copies of Reports.** The treasurer of a political committee must preserve all records and copies of reports for 3 years after the report is filed. 52 U.S.C. §30102(d).

Facts and Analysis

A. Facts

During audit fieldwork, the Audit staff reviewed disbursements to verify the accuracy of the information and proper classification of transactions disclosed on reports. FDF reported expenditures totaling \$90,814 for which documentation was insufficient to make a determination pertaining to whether these disbursements were correctly reported on Schedule B, Line 21b (Operating Expenditures).

The Audit staff's analysis resulted in the following:

Disbursements – Invoices Provided – Not Able to Associate with Copies of Communications (\$90,814)

Disbursements totaling \$90,814 were paid to two direct mail vendors and were disclosed on Schedule B with purposes of “direct mail – creative” and “direct mail – postage.” For these disbursements, FDF provided invoices but did not provide information about the related mail communications. Without a copy of the associated communications, the Audit staff is unable to determine how FDF should have reported these disbursements. During audit fieldwork, the Audit staff requested copies of the mail communications. To date these records have not been provided.

B. Interim Audit Report & Audit Division Recommendation

At the exit conference, the Audit staff presented a schedule of the disbursements for which further records were necessary to verify the accuracy of FDF's reporting. The

Audit staff requested copies of the mail communications. The FDF Treasurer stated that he would contact the vendors to find the missing mail communications, or find out if the invoices had incorrect mailer job identifiers, and would provide the Audit staff with any documentation that was obtained.

The Audit staff recommends that, within 30 calendar days of service of this report, FDF provide, in sufficient detail, the necessary information from which the reported operating expenditures totaling \$90,814 may be verified or explained. Such records should include:

- **Copies of communications that can be associated to the vendor invoices, and**
- **If the communication has already been provided, information associating each communication with an invoice(s).**