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Thomas E. Hintermister
Assistant Staff Director
Audit Division
Federal Election Commission
999 E Street, NW
Washington, DC 20463
VIA EMAIL: SHThomas@fec.gov

Re: <u>Response to Interim Audit Report from McSally for Congress Committee</u>

Dear Mr. Hintermister:

On behalf of the McSally for Congress Committee ("Committee"), and Paul Kilgore, in his official capacity as Treasurer, we file this response to the Interim Audit Report received on May 20, 2017, in connection with the Federal Election Commission's ("FEC's" or "Commission's") audit of the Committee. The Committee will address each finding below.

Prior to addressing the findings, the Committee would like to bring to the Commission's attention the unique circumstances the Committee encountered during the 2012-2014 election cycles, and the extraordinary remedial measures the Committee has undertaken to fully comply with the Federal Election Campaign Act of 1971, as amended (the "Act") and Commission regulations. Congresswoman McSally is a second term Member of Congress from Arizona's 2nd congressional district. Rep. McSally is a retired Colonel and political newcomer who became the Republican nominee in the 2012 election for Arizona's 2nd congressional district. Over the 2012 and 2014 election cycles, the Committee raised and spent over $12.3 million dollars. The Committee received more than 45,300 contributions from over 22,600 individual contributors, the majority of this in the form of low dollar contributions. This volume of contributions for a candidate, who was not an incumbent, is not only rare, it is almost without comparison. The level of support was tremendous, but it created unique challenges for Committee staff in handling the overwhelming volume of activity. When the initial 2014 treasurer, who was employed at an accounting firm but who had no political finance experience, realized she did not have the capacity to handle the volume of activity, the Committee searched for an experienced political treasurer and a person with statewide federal treasurer experience. The Committee was not aware that she was also overwhelmed until she stepped aside right before the 2014 election.

The Committee did everything it could to ensure accurate accounting and reporting amidst the massive amount of activity.

In 2015, Rep McSally directed the Committee to undertake a comprehensive internal review of all of its accounting and FEC reports beginning with the Committee's inception in 2012. Unlike the Commission's Audit, this internal review was not a sample of the Committee's activity for the period of time being reviewed; rather, the Committee started from the very beginning and completely rebuilt its database consisting of over $12.3 million dollars of activity over the 2012-2014 election cycles. In other words, we started from scratch and researched/redocumented every single transaction, donation, and expenditure to ensure everything was documented correctly for the entire history of the committee. It is highly unusual for a political committee to undertake such an endeavor, especially one with this amount of activity. This was a herculean effort on the part of the Committee, and as a result of this unprecedented review, every report filed since the first report in 2012 through the Year-End 2014 was refiled on January 31, 2016, (prior to the Exit Conference). Moreover, it is critical to understand that the Committee's amendments are not based on the prior reports, but instead reflect what actually occurred. All of the Committee's reports and bank statements currently reconcile to the penny.

Finding 1. Misstatement of Financial Activity

The Audit staff identified a misstatement of financial activity in calendar years 2013 and 2014. At the Exit Conference, Audit staff reported that the Committee's amendments materially corrected the 2013 misstatement. In addition, Audit Staff reported that the Committee materially corrected the beginning and ending cash on hand for 2014. However, according to the Auditors, the Committee's amendments resulted in a material overstatement of receipts and disbursements for 2014.

The Auditors provided the Committee with a spreadsheet detailing the transactions the Auditors believed accounted for the 2014 misstatement. The Committee reviewed the spreadsheet the Auditors provided and compared the transactions to the Committee's amended reports. The Committee disagrees with the Audit Staff that there is a misstatement and maintains that the amendments filed on January 31, 2016, materially corrected the misstatement. The Committee's amendments were created by rebuilding the database using bank statements, credit card statements, donor forms, invoices and any other financial information available. The amendments were not based on the filed reports, and may not reflect transactions that inadvertently appeared on the original reports.

A. 2014 Receipts Overstatement

The IAR states that the Committee's 2016 amendments overstated receipts by $94,528. At the Exit Conference, Audit staff provided a list of 122 receipts they believed made up the overstatement. In other words, this list included a series of identified receipts that Audit staff contends were disclosed on the Committee's 2016 amended reports, but should not have been disclosed because Audit staff was unable to find documentation for or evidence of the transactions in the Committee's bank accounts.

In its Exit Conference response, the Committee disputed the list of receipts the Audit staff stated comprised the misstatement and disagreed with the misstated amount of $94,528. The Committee conducted its own review of this list of receipts, and of the 122 transactions, at least 33 transactions totaling $27,115 do *not* appear on any of the amended reports. Although many of these transactions appeared on the Committee's audited reports, they were not included in the amendments because they were either reported as duplicates on the audited reports or because the transaction did not actually happen in the first place. Again, the Committee rebuilt its database without reference to the prior reports. Thus, to the extent the Audit staff thinks this list of receipts should be reported as negative entries or in some other way, the Committee disagrees because doing so would be an inaccurate reflection of what actually occurred.

In addition, the Committee separately reported $21,100 in contribution refunds and $45,015.45 in offsets to operating expenditures that Audit staff contends the Committee reported incorrectly and that contributes to the alleged misstatement of receipts. As explained in further detail below, the Committee believes the way it reported these transactions is consistent with the statute and Commission regulations.

B. 2014 Disbursements Overstatement

The IAR states the Committee overstated disbursements by $85,472, and provided a list of disbursements they believe make up the overstatement. In other words, it is a list of disbursements the Auditors believe were disclosed on the Committee's 2016 amended reports, but for which the Auditors were unable to find documentation for or evidence of in the bank accounts, and therefore, should not have appeared on the Committee's amended reports. The Committee has reviewed the list and at least 23 of the transactions totaling approximately $16,908 were *not* disclosed on the Committee's amended reports. Again, many of these transactions appeared on the Committee's audited reports, but they were not included in the amendments because they were either reported as duplicates on the audited reports or because the transaction did not actually happen in the first place, and the Committee believes its 2016 amended reports are an accurate reflection of what actually occurred at the time.

Moreover, as referenced above, Audit staff contends the Committee misreported $21,100 in contribution refunds and $45,015.45 in offsets to operating expenditures. As explained in further detail below, the Committee believes the way it reported these transactions is consistent with the statute and Commission regulations, and that there is no material misstatement.

C. Reporting of Contribution Refunds and Offsets to Operating Expenditures

It appears the main point of contention is with respect to the $21,100 the Committee reported as contribution refunds and $45,157 the Committee reported as offsets to operating expenditures. The Committee believes the way it reported these transactions is consistent with the statute and Commission regulations.

Contribution Refunds: The Committee reported $21,100 in contributions that were later refunded to the contributors. It is our understanding that the Audit staff's position is that these contributions were not "received" by the Committee and that the Committee did not actually issue refunds. As such, Audit staff contends these transactions were "chargebacks" and should have been reported as negative entries on Schedule A rather than as refunds on Schedule B. However, these contributions were not bounced checks or the electronic equivalent. As such, the Committee believes that of the $21,100 in refunds, $15,500 were properly reported as receipts and disbursements. The remaining $5,600 constitute funds that were actually received into the Committee's accounts, and under the regulations the Committee is required to show this as a receipt on Schedule A. A refund of that money is supposed to be shown as a disbursement under Schedule B. Although the credit card merchant provider may have reduced the amount forwarded to the Committee in a later set of transactions instead of pulling a disbursement from the bank account, the Committee believes this transaction should be shown as a Schedule B disbursement.

Commission regulations do not specifically address how chargebacks must be treated for reporting purposes. The Committee recognizes that the Commission has provided guidance regarding when a Committee should report a transaction as a negative entry in the Campaign Guide for Congressional Candidates and Committees. These instances include when (1) a contribution is redesignated or reattributed during a different reporting period; (2) checks returned due to insufficient funds; (3) checks that are never cashed; and (4) investment losses. The Reports Analysis Division has issued guidance stating that, with respect to contributions, "Negative entries on Schedule A should only be used to disclose returned or bounced contribution checks and not for refunds by the Committee." However, the Commission has not provided clear guidance regarding how a Committee must report a chargeback, and there is no reason why the Committee cannot choose to report a transaction in a different way if it appears to the Committee that it is a more accurate reflection of what occurred at the time.

Offsets to Operating Expenditures: The Committee also reported $45,015.45 in offsets to operating expenditures on the amended 2014 Year-End Report filed on January 31, 2016. These offsets represent disbursements from the Committee that were made and reported during 2014, but that never cleared the bank. Because the transactions never cleared, they were reported as offsets on Schedule A (*i.e.*, receipts) to maintain an accurate cash on hand. Audit staff contends that these transactions should be reported as negative entries on Schedule B, Disbursements.

The Committee notes that Commission guidance provides that uncleared checks written by the Committee should be reported as negative entries rather than offsets to operating expenditures. Nonetheless, the Committee does not believe its decision to report this amounts as offsets is inconsistent with the statute or Commission regulations. The Committee reported the uncleared checks as offsets (receipts) in order to ensure the cash on hand was accurate. This did not distort the public record or overstate *contributions* received by the Committee. The Detailed Summary pages of the reports clearly delineate between contributions the Committee has received from contributors and other types of receipts, such as interest, loans, refunds or rebates.

The amended reports disclose the disbursements totaling $45,015.45, but because those checks did not clear, those funds were treated as offsets. This was a reasonable way to account for these transactions even if it was not the preferred way.

D. Audit Staff Recommendation

Audit staff has recommended that the Committee file a Form 99 within 30 days of receipt of the IAR to "explain its reporting methodology" for the public record. The Committee believes that filing a Form 99 referencing activity that occurred almost three years ago will create needless confusion. The Commission's Audit is a just a sample. The Committee's own internal review (or audit, if you will) was not based on a sample. It was a complete recreation of its database, and the Committee's amendments reconcile with every bank statement down to the penny. Even if this could be considered a misstatement, it barely represents 1.5% of the Committee's receipts and disbursements and is not material. Nonetheless, the Committee does not believe it misstated its receipts or its disbursements, and furthermore, does not understand how the Audit staff came up with the amounts they contend make up the alleged misstatement.

Finding 2. Occupation/Name of Employer (OCC/NOE)

The Audit staff determined that this Finding was materially corrected by the Committee's amendments. However, the Committee would like to note for the record that it utilized "best efforts" to collect and report occupation/name of employer during the entire history of the committee including the 2014 cycle. The Committee's solicitation materials included a clear request for the name, address, occupation and employer of individuals whose contributions aggregated $200 during the election cycle, and in instances where a contributor did not provide that information, the Committee would make at least one effort to obtain that information.

Finding 3. Receipt of Contributions from Individuals in Excess of the Limits

At the Exit Conference, Audit staff informed the Committee that during fieldwork they had identified 156 contributions from individuals, totaling $332,412 that exceeded the limits. The IAR, however, states that during fieldwork Audit staff identified 153 contributions from individuals, totaling $319,212 that exceeded the limits. The Committee does not understand why the amounts changed and why there is a discrepancy between the two communications with Audit staff.

Nonetheless, the Committee has resolved the remaining $6,601 in excessive contributions. Four were resolved by issuing refunds to the contributors, and copies of the negotiated checks for three have been provided to the Audit staff.[1] The fifth was not excessive as it was from an individual who shared the same name with another individual who had

[1] The Committee recently attempted for the fourth time to issue a refund to the remaining contributor. The Committee has confirmed that the most recent refund was received and will provide a negotiated copy of the check as soon as it is available.

contributed the maximum amount. The Committee was able to show these were two different individuals and neither individual was excessive.

The Committee also notes that an overwhelming majority of the contributions it accepted were able to be resolved by redesignations and reattributions. As stated in the IAR, the Committee resolved $31,893 by issuing refunds, as well as the additional $6,601 discussed above. The Committee had approximately $138,763 on hand on Election Day 2014, which was more than enough to cover the refunded amounts, and the refunds totaled less than 1% of the amount the Committee raised.

Finding 4. Disclosure of 48-Hour Notices

The IAR states that the Committee did not file 48-hour notices for 29 contributions totaling $91,053, and untimely filed 48-hour notices for four contributions totaling $8,800. In the IAR, the total error amount for non-filed or untimely filed 48-hour notices in the IAR is 33 contributions totaling $99,853. The Committee notes, however, that these amounts differ from the amounts presented at the Exit Conference. At the Exit Conference, Audit staff stated that the Committee did not file notices for 26 contributions totaling $47,345.55, and untimely filed notices for 6 contributions totaling $14,000. Thus, at the Exit Conference, the total error amount for 48-hour notices that were not filed or were untimely filed totaled $61,345. This is a difference of $38,508, and again, the Committee does not understand why the amounts changed or why there is such a discrepancy between two communications by Audit staff on the same topic.

The Committee notes that the volume of contributions it received during the time period before the primary and general elections was, at times, overwhelming. Nonetheless, the Committee filed notices for almost 90% of the amount raised during the 48-hour time period. The Committee has implemented procedures and hired experienced FEC compliance specialists to ensure future compliance.

Finding 5. Failure to Itemize Contributions from Political Committees

The Auditors identified 14 contributions from PACs totaling $32,250 that were not itemized on Line 11c. The 14 contributions were disclosed in the Committee's amended reports and the finding has been resolved. The Committee has hired an experienced FEC compliance specialist to serve as treasurer to ensure such inadvertent errors do not happen in the future.

Finding 6. Recordkeeping and Disclosure of Receipts (Joint Fundraising Committee Transfers)

The Auditors determined that the Committee did not disclose proceeds from one joint fundraiser totaling $200, and did not itemize 127 memo entries totaling $146,094.58 for two joint fundraising events held in March 2014. The Committee materially corrected the itemization errors in its amendments, and the finding has been resolved. The Committee has implemented procedures and hired experienced FEC compliance specialists to ensure such errors do not happen in the future.

Conclusion

The Committee takes its compliance obligations very seriously and its obligation to the public to be as transparent as possible. To that end, the Committee spent an extraordinary amount of time and resources reviewing and amending its reports in an effort to ensure the public record is as complete and accurate as possible. This was an unprecedented full review of over $12.3 million in activity over two election cycles, including the audited cycle, in which the Committee received more than 45,300 contributions from over 22,600 individual contributors. Again, we believe it is critical that the Commission understand that the Committee did not engage in audit sampling when it conducted its review. The Committee went to the barebones and rebuilt its database from scratch, and therefore we believe the amended reports filed by the Committee on January 31, 2016, provide an accurate reflection of the Committee's activity at the time it occurred.

The Committee has made every effort to work with Audit staff to resolve any outstanding issues, and we appreciate the time the Audit staff took to work with the Committee during this process.

Respectfully submitted,

Elizabeth Beacham White
Counsel to McSally for Congress