

**AGENDA DOCUMENT NO. 12-30**



FEDERAL ELECTION COMMISSION  
WASHINGTON, D.C. 20463

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March 8, 2012

**AGENDA ITEM**

**MEMORANDUM**

To: The Commission

Through: Alec Palmer *AP*  
Staff Director

From: Patricia Carmona *PC*  
Chief Compliance Officer

Tom Hintermister *TH*  
Assistant Staff Director  
Audit Division

Alex Boniewicz *AB*  
Audit Manager

By: Paula Nurthen *PN*  
Lead Auditor *by [signature]*

Subject: Audit Division Recommendation Memorandum on The Legacy Committee  
Political Action Committee (A09-22)

For Meeting of 5-10-12

Pursuant to Commission Directive No. 70 (FEC Directive on Processing Audit Reports), the Audit staff's recommendations are presented below and the findings are discussed in the attached Draft Final Audit Report. The Office of General Counsel has reviewed this memorandum and concurs with the recommendations.

**Finding 1. Misstatement of Financial Activity**

The Audit staff recommends that the Commission find that The Legacy Committee Political Action Committee misstated receipts and disbursements for calendar year 2008.

**Finding 2. Failure to File Notices and Properly Disclose Independent Expenditures**

The Audit staff maintains that The Legacy Committee Political Action Committee did not timely file 24/48 hour notices of \$374,327 and did not file 24-hour notices for \$17,491 and did not properly disclose independent expenditures totaling \$294,570 prior to payment as "memo" entries. The Audit staff recommends that the Commission find that The Legacy Committee Political Action Committee failed to file notices and properly disclose independent expenditures.

The Committee did not request an audit hearing. The Committee's response to the Draft Final Audit Report (DFAR) did not provide any additional comments with respect to the issues presented in the two findings. However, the Committee's response did emphasize that the current cash balance is sufficiently less than the ending cash balance on December 31, 2008 as indicated on page two of the DFAR.

If this memorandum is approved, a Proposed Final Audit Report will be prepared within 30 days of the Commission's vote.

Should an objection be received, Directive No. 70 states that the Audit Division Recommendation Memorandum will be placed on the next regularly scheduled open session agenda.

Documents related to this audit report can be viewed in the Voting Ballot Matters folder. Should you have any questions, please contact Paula Nurthen or Alex Boniewicz at 694-1200.

Attachment:

- Draft Final Audit Report on The Legacy Committee Political Action Committee

cc: Office of General Counsel



# Draft Final Audit Report of the Audit Division on The Legacy Committee Political Action Committee

January 1, 2007 – December 31, 2008

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## 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.<sup>1</sup> 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 Legacy Committee Political Action Committee is a nonconnected, multi-candidate committee headquartered in Laguna Niguel, California. For more information, see the chart on Committee Organization, p. 2.

## Financial Activity (p. 2)

• <b>Receipts</b>	
○ Contributions from Individuals	\$ 1,544,747
○ Loans Received	5,000
<b>Total Receipts</b>	<b>\$ 1,549,747</b>
• <b>Disbursements</b>	
○ Independent Expenditures	\$ 1,162,464
○ Operating Expenditures	217,889
○ Contributions to Federal Candidate Committees and Other Political Committees	47,250
○ All Other Disbursements	36,992
<b>Total Disbursements</b>	<b>\$ 1,464,595</b>

## Findings and Recommendations (p. 3)

- Misstatement of Financial Activity (Finding 1)
- Failure to File Notices and Properly Disclose Independent Expenditures (Finding 2)

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<sup>1</sup> 2 U.S.C. §438(b).

# **Draft Final Audit Report of the Audit Division on The Legacy Committee Political Action Committee**

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January 1, 2007 - December 31, 2008



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## **Part I**

### **Background**

#### **Authority for Audit**

This report is based on an audit of The Legacy Committee Political Action Committee (LCP) 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 consistency between reported figures and bank records;
2. the disclosure of individual contributors' occupation/name of employer;
3. the disclosure of independent expenditures; and
4. other committee operations necessary to the review.

## Part II Overview of Committee

### Committee Organization

<b>Important Dates</b>	
• Date of Registration	September 19, 2006
• Audit Coverage	January 1, 2007 – December 31, 2008
<b>Headquarters</b>	
Laguna Niguel, California	
<b>Bank Information</b>	
• Bank Depositories	One
• Bank Accounts	Two Checking Accounts
<b>Treasurer</b>	
• Treasurer When Audit Was Conducted	James V. Lacy
• Treasurer During Period Covered by Audit	James V. Lacy
<b>Management Information</b>	
• Attended Commission Campaign Finance Seminar	Yes
• Who Handled Accounting and Recordkeeping Tasks	Paid Staff

### Overview of Financial Activity (Audited Amounts)

Cash-on-hand @ January 1, 2007	\$ 0
<b>Receipts</b>	
○ Contributions from Individuals	1,544,747
○ Loans Received	5,000
<b>Total Receipts</b>	<b>\$ 1,549,747</b>
<b>Disbursements</b>	
○ Independent Expenditures	1,162,464 <sup>2</sup>
○ Operating Expenditures	217,889
○ Contributions to Federal Candidate Committees and Other Political Committees	47,250
○ All Other Disbursements	36,992
<b>Total Disbursements</b>	<b>\$ 1,464,595</b>
Cash-on-hand @ December 31, 2008	\$ 85,152

<sup>2</sup> This amount, as well as the amount for operating expenditures, may change as a result of the finding on page 5.

## **Part III**

### **Summaries**

#### **Findings and Recommendations**

##### **Finding 1. Misstatement of Financial Activity**

During audit fieldwork, a comparison of LCP's reported financial activity with its bank records revealed that, for 2008, LCP understated its reported receipts and disbursements by \$32,411 and \$25,529, respectively. In response to the Interim Audit Report, LCP amended its reports to materially correct the misstatements. (For more detail, see p. 4)

##### **Finding 2. Failure to File Notices and Properly Disclose Independent Expenditures**

LCP disclosed independent expenditures totaling \$1,159,647 on Schedule E (Itemized Independent Expenditures). During audit fieldwork, the Audit staff noted that only \$412,891 of these expenditures appeared to meet the definition of independent expenditures and contained language expressly advocating the election or defeat of a clearly identified candidate. Of these independent expenditures (\$412,891):

- LCP did not timely file 24/48-hour notices for \$374,327 and did not file any 24-hour notices for \$17,491; and
- LCP did not properly disclose independent expenditures totaling \$294,570 made (i.e., publicly disseminated) prior to payment as "memo" entries on Schedule E and as a reportable debt on Schedule D (Debts and Obligations).

In response to the Interim Audit Report, LCP provided information supporting its position that the purpose of its direct-mail letters was fundraising and did not require reporting as independent expenditures. Regarding the Audit staff's recommendation that they submit and implement revised procedures for reporting independent expenditures, LCP indicated that they plan to terminate after the audit is completed. (For more detail, see p. 5)



## Part IV

# Findings and Recommendations

### Finding 1. Misstatement of Financial Activity

#### Summary

During audit fieldwork, a comparison of LCP's reported financial activity with its bank records revealed that, for 2008, LCP understated its reported receipts and disbursements by \$32,411 and \$25,529, respectively. In response to the Interim Audit Report, LCP amended its reports to materially 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 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). 2 U.S.C. §434(b)(1), (2), (3), (4) and (5).

#### Facts and Analysis

##### A. Facts

During audit fieldwork, the Audit staff reconciled reported financial activity with bank records for calendar years 2007 and 2008. A misstatement of receipts and disbursements was identified for 2008. The following chart outlines the discrepancies.

2008 Activity			
	Reported	Bank Records	Discrepancy
Opening Cash Balance @ January 1, 2008	\$19,508	\$19,365	\$143 Overstated
Receipts	\$1,066,076	\$1,098,487	\$32,411 Understated
Disbursements	\$1,007,171	\$1,032,700	\$25,529 Understated
Ending Cash Balance @ December 31, 2008	\$78,413	\$85,152	\$6,739 Understated

The understatement of receipts resulted from unidentified differences that occurred primarily in the second half of the year. Based on a limited review of available records, it appeared that all contributor information received by the vendor that processed deposits

of contributions may not have been forwarded to the vendor responsible for the data entry.

The understatement of disbursements resulted from the following:

• Refunds of contributions not reported	\$ 18,152
• Bank and credit card fees not reported	4,560
• Independent expenditures not reported	<u>2,817</u>
<b>Understatement of disbursements</b>	<b><u>\$ 25,529</u></b>

### **B. Interim Audit Report & Audit Division Recommendation**

At the exit conference, the Audit staff explained the misstatements and provided schedules to LCP's Treasurer and Assistant Treasurer. They agreed to amend their reports as necessary.

The Audit staff recommended that LCP:

- Amend its reports to correct the misstatements 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, LCP should have reconciled the cash balance of its most recent report to identify any subsequent discrepancies that may affect the adjustment recommended by the Audit staff.

### **C. Committee Response to Interim Audit Report**

In response to the Interim Audit Report, LCP filed amended reports for 2008 that materially corrected the misstatements. In addition, LCP provided supporting documentation that demonstrated that amendments to its most recently filed report were not necessary.

## **Finding 2. Failure to File Notices and Properly Disclose Independent Expenditures**

### **Summary**

LCP disclosed independent expenditures totaling \$1,159,647 on Schedule E (Itemized Independent Expenditures). During audit fieldwork, the Audit staff noted that only \$412,891 of these expenditures appeared to meet the definition of independent expenditures and contained language expressly advocating the election or defeat of a clearly identified candidate. Of these independent expenditures (\$412,891):

- LCP did not timely file 24/48-hour notices for \$374,327 and did not file any 24-hour notices for \$17,491; and
- LCP did not properly disclose independent expenditures totaling \$294,570 made (i.e., publicly disseminated) prior to payment as "memo" entries on Schedule E and as a reportable debt on Schedule D (Debts and Obligations).

In response to the Interim Audit Report, LCP provided information supporting its position that the purpose of its direct-mail letters was fundraising and did not require

reporting as independent expenditures. Regarding the Audit staff's recommendation that they submit and implement revised procedures for reporting independent expenditures, LCP indicated that they plan to terminate after the audit is completed.

### **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. 11 CFR §100.16.

**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 reportable debt on Schedule D. Independent expenditures of \$200 or less do not need to be itemized, though the committee must report the total of those expenditures on line (b) on Schedule E. 11 CFR §§104.3(b)(3)(vii), 104.4(a) and 104.11.

**C. Last-Minute Independent Expenditure Reports (24-Hour Notices).** Any independent expenditures aggregating \$1,000 or more, with respect to any given election, and made after the 20<sup>th</sup> 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 notice 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 Notices).** Any independent expenditure aggregating \$10,000 or more with respect to any given election, at any time during a 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 notices must be filed with the Commission within 48 hours after the expenditure is made. 11 CFR §§104.4(f) and 104.5(g)(1).

### **Facts and Analysis**

#### **A. Facts**

Initially, LCP disclosed all expenditures as operating expenditures (Schedule B, Line 21(b)). During 2008, LCP received notices from the Commission's Reports Analysis Division (RAD) questioning whether any of the expenditures, e.g., "Printing," were for public communications containing express advocacy. LCP's Treasurer acknowledged that some of the communications contained express advocacy but contended that the purpose of the communication was fundraising. RAD advised LCP that if the communication contained express advocacy, LCP should amend its reports to disclose the

expenditures as independent expenditures. Subsequently, LCP filed the requested amended reports.

LCP disclosed independent expenditures totaling \$1,159,647 on Schedule E. During audit fieldwork, it was noted that most of these disbursements were for the printing and postage of direct mail solicitation letters and were disclosed as either in support of John McCain for President or in opposition to Hillary Clinton or Barack Obama for President. The Audit staff reviewed these expenditures to determine if they were properly reported on Schedule E and to determine if LCP filed the required 24/48-hour notices. The review noted that only \$412,891 of these expenditures appeared to meet the definition of an independent expenditure and contained language expressly advocating the election or defeat of a clearly identified candidate. A review of the direct mail pieces and invoices for those expenditures (\$412,891) revealed the following:

- LCP did not timely file 24/48-hour notices of its independent expenditures for \$374,327. In addition, LCP did not file any 24-hour notices for \$17,491 of these expenditures.
- LCP reported the independent expenditures when the invoices were paid. However, most of these payments were weeks or months after the dissemination date of the printed material. For expenditures totaling \$294,570, LCP should have disclosed independent expenditures as memo entries on Schedule E, filed with reports covering the dates when the materials were disseminated, and included a corresponding debt on Schedule D.

#### **B. Interim Audit Report & Audit Division Recommendation**

The Audit staff addressed these matters at the exit conference and provided appropriate schedules to LCP representatives. The Audit staff indicated that, at this time, no amended reports were necessary to correct the reporting of the independent expenditures or to address the 24/48-hour notices that were not filed or not filed timely. LCP representatives stated that they would review these schedules.

The Audit staff recommended that LCP take the following action:

- Provide any documentary evidence that would demonstrate that these disbursements were not independent expenditures and therefore did not require 24/48-hour notices; and
- Submit and implement revised procedures for reporting independent expenditures, as well as for tracking dissemination dates for such expenditures, in order to allow for timely filing of 24/48-hour reporting notices.

#### **C. Committee Response to Interim Audit Report**

In response to the Interim Audit Report, LCP offered background information for why they were created and the purpose of its direct-mail fundraising letters. LCP explained that it was formed in 2007 as a non-connected Political Action Committee (PAC) that was not supported by any sponsoring organization such as a labor union or corporation. There was no permanent staff, office or office equipment. It was formed with the

intention of raising funds to allow it to participate in the 2008 General Election by making direct contributions to candidates for Federal office. LCP indicated that the committee was the epitome of a “grass roots” attempt to participate in the 2008 Federal elections.

LCP explained that its direct-mail advisors obtained lists of proven donors to Republican and conservative causes and tested various content appeals in the letters to these donors. The various tests included content with references to elected officials and Presidential candidates to clue the recipient audience that LCP was a conservative Republican PAC worthy of their support. LCP stated that the purpose of these mailings was not to intervene in any election. LCP indicated that the facts demonstrated that: the *timing* of all of its mailings had no reference to the timing of primary elections during 2008; the *content* of the letters, other than sometimes including some words considered “express advocacy” by the Commission, did not urge the recipient audience to vote for any particular candidate; and the *audience* was selected for its fundraising value, with no consideration for its electoral value. Thus the expenditures’ content, timing and distribution, and audience served a fundraising purpose but not an electoral purpose.

LCP stated that they disagreed that any of its direct-mail fundraising letters constituted independent expenditures. LCP noted that the Commission defines an independent expenditure at 11 CFR §100.16 as a communication expressly advocating the election or defeat of a clearly identified candidate. LCP acknowledged that some of its mailings did include words of express advocacy. However, LCP thought that if the Commission considered all of the facts, it should agree that LCP’s fundraising letters were not independent expenditures and that the special reporting rules applicable to independent expenditures (such as the 24/48-hour notices or memo entries) should not apply. LCP stated that they believe that direct-mail fundraising letters should be excluded from the definition of independent expenditures, and that the intent of the regulation was not to include direct mail fundraising expenditures as independent expenditures. LCP urged the Commission to reform its reporting requirements for grass-roots organizations that engage in direct-mail fundraising since they believe that these letters are not independent expenditures. LCP indicated that they have made the decision that the time requirements, coordination and record keeping are not worth the effort of continuing to participate and as such, plan to terminate the committee after the audit is completed.

The Audit staff does not dispute that LCP’s intention was to raise funds via the direct-mail letters. However, LCP acknowledges and the Audit staff agrees that some of these letters included express advocacy language such as “Vote for John McCain”. Since these expenditures meet the definition of an independent expenditure and the regulation does not exclude direct-mail fundraising letters from the definition, the Audit staff believes that the documentary evidence provided does not support LCP’s assertion that none of these expenditures are independent expenditures.