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March 5, 2013

MEMORANDUM

AGENDA ITEM

To: The Commission

Through: Alec Palmer *AP*
Staff Director

For Meeting of 4-11-13

From: Patricia C. Orrock *PCO*
Chief Compliance Officer

Tom Hintermister *[Signature]*
Assistant Staff Director
Audit Division

Kendrick Smith *[Signature]*
Audit Manager

By: Brenda E. Wheeler *[Signature]*
Lead Auditor

Subject: Audit Division Recommendation Memorandum on the California
Republican Party/V8 (CRP) (A09-15)

Pursuant to Commission Directive No. 70 (FEC Directive on Processing Audit Reports), the Audit staff presents its recommendations below and discusses the findings in the attached Draft Final Audit Report (DFAR). The Office of General Counsel reviewed this memorandum and concurs with our recommendations.

Finding 1. Misstatement of Levin Activity

CRP filed amendments that materially complied with the Interim Audit Report recommendation. There were no new or significant issues raised in response to the DFAR.

The Audit staff recommends that the Commission find that CRP misstated its Levin fund activity for calendar year 2008.

Finding 2. Reporting of Debts and Obligations

CRP filed amendments that materially complied with the Interim Audit Report recommendation. There were no new or significant issues raised in response to the DFAR.

The Audit staff recommends that the Commission find that CRP failed to disclose debts and obligations totaling \$2,188,950 on Schedule D (Debts and Obligations) of its reports.

Finding 3. Extension of Credit by a Commercial Vendor

In response to the DFAR, Counsel for CRP (Counsel) and the Chief Financial Officer (CFO) of Strategic Fundraising, Inc. (SFI) submitted letters disputing the Audit staff's contention that CRP has not demonstrated that SFI extended credit within its ordinary course of business or that commercially reasonable attempts were made to collect the CRP debt.

CRP Response to DFAR

In CRP's response, Counsel responded to some questions raised by the Audit staff in the DFAR and the Office of General Counsel (OGC) in its DFAR legal analysis. Counsel stated:

1. "...the CRP believes that SFI did not suffer actual financial losses from the 'no risk guarantee.' "
2. "...SFI was paid nearly in full for the amounts it had initially billed for services."
3. "Based upon its additional submission, SFI believes that it made a profit, and continues to make a profit on its fundraising relationship with the CRP." Counsel asserts that the best evidence of this is that the relationship with SFI has continued for another four years.

In addition, Counsel suggested that the Commission should consider revising its debt settlement provisions for ongoing committees such as CRP since its debt situations are so different than those for terminating committees. Counsel contended that, unlike a candidate committee, a party committee is an ongoing entity that must fundraise to remain in existence, and often times, its ability to fundraise is affected by external conditions. As such, party committees must enter into contractual obligations with fundraising entities in a manner that will ensure its existence.

Counsel also included a memorandum to SFI (dated July 3, 2008) which discussed a partial payment of \$250,000 to SFI "...on a currently unresolved account payable..." The memorandum also stated that CRP is currently undertaking a comprehensive review of the SFI bills, from an accuracy and performance standpoint. In addition, the memorandum stated, "[the enclosed payment] should be viewed solely as a good faith effort on CRP's part to reduce the outstanding balances subject to the completion of the comprehensive review and a determination of what is the appropriate amount due under these contracts."

Counsel provided more details of the 2008 negotiated settlement between SFI and CRP. In one of the provisions, which was previously unknown by the Audit staff, SFI agreed to waive accrued interest on unpaid balances if CRP agreed to meet its obligations to pay the balance of amounts outstanding or that which would be accrued in the fundraising efforts that SFI and CRP undertook from the late summer of 2008 through the beginning of 2009 to extinguish the past debt. In addition, CRP and SFI were to negotiate an extension of the fundraising agreement

for the 2009-2010 cycle. Payment agreements were also made for future fundraising. However, the formal agreements were not presented to the Audit staff.

Information Provided by SFI

Counsel also provided the following information from the CFO.

1. Regarding some of the safeguards proposed by the Commission, the CFO stated that “[t]he CRP has bylaws that forbid it from entering into agreements that span across two board terms essentially limiting the contract to approximately two years.” The CFO also contended that all of its contracts, with both political and non-profit clients, contain a termination clause that either party can execute for any reason.
2. Regarding the caging of contributions by CRP, the CFO stated that SFI has control over “risk” in all of its fundraising agreements. The CFO contended that, as part of the fundraising agreement with CRP, SFI routinely audits the “caged” data to verify every donation is being accurately and timely reported to SFI. The CFO also added that “[w]hile some fundraising/donor acquisition is low margin work, it goes without saying that through our 20 years of experience we are able to avoid ‘losing money.’ ” The CFO stated that the fact that CRP was able to fundraise out of the financial situation and pay off its balance owed to SFI contradicts the DFAR conclusion and demonstrates it is without basis.
3. Regarding its commercially reasonable debt collection efforts, the CFO stated that SFI has had other clients that found themselves in similar debt situations, which were resolved under similar verbal agreements. In addition, the CFO stated that “[o]ther documentation to demonstrate SFI’s full efforts to collect the debt is difficult to come by as this occurred 4-5 years ago, the CRP staff and treasurer involved have moved on and our CEO at the time has since retired.”

The CFO maintained that the debt settlement agreement “worked as planned” and “...that the CRP paid off the debt and is a continued partner of SFI’s to this day.” The CFO further stated that “[o]ur experience tells us that ‘withholding of additional services until overdue debts are satisfied’ doesn’t work. I have been made aware of several state parties having their vendors stop doing work for them only to 1) not get paid, 2) get paid more slowly or 3) end the relationship permanently. We sought a win-win solution and achieved it.” The CFO expressed a concern regarding the provision of additional documentation to the Audit staff. He stated that “[i]t does not seem appropriate however to disclose private (to the CRP) and proprietary (to SFI) information that could/would end up on the public record. Sharing LifeTime Value data, inception donor counts, renewal rates, fundraising plans, etc [*sic*] does not appear to be in the purview of the Commission.”

In response to the memorandum sent to SFI by CRP (previously discussed on page 2), the CFO sent a letter to Counsel dated July 9, 2008. The letter indicated that

CRP had nearly a \$900,000 balance that had accrued over the last 12-14 months. The CFO also wrote that communication between CRP and SFI never mentioned any “unresolved payables” and that during a meeting held in Minnesota between CRP and SFI, there was no mention of CRP undertaking a comprehensive review from an accuracy and performance standpoint. However, the CFO did indicate that CRP was going to provide a list of questions regarding small billing issues, but the CFO never received the list.

Audit Staff's Assessment

Initial Extension of Credit - Inadequate Safeguards

In the DFAR, the Audit staff highlighted information that should be provided to demonstrate the agreement between SFI and CRP was commercially reasonable. 11 CFR 116.4(b) and (d). However, neither provided confirmation that the terms of the credit issued to CRP are similar to the terms SFI applies when extending a similar amount of credit to a nonpolitical client of similar risk.¹ In addition, neither party provided documentation to demonstrate any particular financial value of the exclusivity clause in the SFI contract.

Without further information, questions still remain about the initial extension of credit from SFI to CRP and whether there were adequate safeguards to ensure that CRP bore a sufficient amount of the cost or the risk of the fundraising program. CRP failed to provide a valuation of the exclusivity clause as requested by the Audit staff, or other pertinent information showing that the exclusive nature of the contract was of sufficient value to offset the risk to SFI. Thus, in the absence of information regarding the value of the exclusivity clause, the Audit staff still concurs with the DFAR and does not believe the contract's term and at-will termination provisions are in the aggregate sufficient to support a conclusion that SFI's initial extension of credit to CRP was in the ordinary course of business.

The Audit staff concludes that CRP has not demonstrated that SFI's initial extension of credit to CRP was in its ordinary course of business.

Debt Collection Efforts - Waiver of Debt Not Within Commission's Debt Settlement Framework

In the DFAR, the Audit staff highlighted information that should be provided to demonstrate that SFI made commercially reasonable attempts to collect the CRP debt. However, neither SFI nor CRP provided such documentation.

The fundraising contract between CRP and SFI provided that “outstanding balances 30 days past due shall accrue interest in the amount of 1 ½ percent, compounded monthly.” However, under its debt settlement agreement, SFI agreed to waive the accrued interest, which may have been significant as CRP had

¹ The RIGHTMARCH.COM PAC INC (RMC) audit presented nearly identical issues. However, in that audit, the vendor agreement had several safeguards built in to ensure payment from RMC. In addition, RMC had its vendor submit 32 contracts from different vendors for both political and non-political clients to substantiate its position. Ultimately, the Commission did not approve the recommended finding by the required four votes, and the matter was moved to the “Additional Issues” section.

outstanding invoices for periods ranging from approximately four months to two years² (DFAR, p. 8). This waiver raises a question as to whether CRP fully paid SFI for its telemarketing services, pursuant to the terms of the fundraising contract.

Through the debt settlement agreement, CRP and SFI may have settled the debt, but it was done so without Commission approval. Further, CRP is an ongoing committee, and ongoing committees cannot settle any outstanding debts for less than the entire amount owed. 11 CFR §116.2(b). In this case, CRP continued to fundraise under its telemarketing contract with SFI and had the ability to work its way out of debt including paying the interest that had accrued pursuant to the contract. Instead, CRP settled its obligations, in part, through an agreement not to pay the accrued interest on the debt contrary to Commission regulations.

The Audit staff concludes that the waiver of accrued interest, through the debt settlement agreement, was in violation of 11 CFR §116.2(b), and CRP and SFI engaged in a debt settlement agreement that was not approved by the Commission, as required.

Audit Staff Recommendation- Finding 3

The Audit staff recommends that the Commission find that SFI's initial extension of credit to CRP was not in its ordinary course of business, and, as a result, CRP accepted a prohibited contribution from SFI totaling \$1,171,002, plus any accrued interest the Commission finds was improperly waived by SFI.

If the Commission finds that SFI's initial extension of credit to CRP was in the ordinary course of business, the Audit staff recommends that the Commission find that SFI did not engage in commercially reasonable debt collection efforts in seeking payment from CRP. As a result, CRP accepted a prohibited contribution from SFI totaling \$1,171,002, plus any accrued interest the Commission finds was improperly waived by SFI.

CRP waived the opportunity for an audit hearing before the Commission.

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

In case of an objection, 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 Brenda Wheeler or Kendrick Smith at 694-1200.

Attachments:

Draft Final Audit Report of the Audit Division on the California Republican Party/V8
Office of General Counsel's Legal Comments on Committee Response

cc: Office of General Counsel

² The Audit staff estimates the accrued interest to be approximately \$138,000.



Draft Final Audit Report of the Audit Division on the California Republican Party/V8 January 1, 2007 – December 31, 2008

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 California Republican Party/V8 is a state party committee headquartered in Burbank, California. For more information, see the chart on the Committee Organization, p. 2.

Financial Activity (p. 2)

• Receipts	
○ Contributions from Individuals	\$ 6,367,753
○ Contributions from Other Political Committees	87,646
○ Transfers from Affiliated Party Committees	7,557,282
○ Transfers from Non-Federal and Levin Accounts	3,389,660
○ Other Receipts	188,928
Total Receipts	\$ 17,591,269
• Disbursements	
○ Operating Expenditures	\$ 11,110,199
○ Transfers to Affiliated/Other Party Committees	3,968,892
○ Contributions to Federal Candidates	30,000
○ Coordinated Party Expenditures	41,660
○ Federal Election Activity	2,392,956
○ Contribution Refunds	33,688
Total Disbursements	\$ 17,577,395
• Levin Receipts	\$ 620,349
• Levin Disbursements	\$ 624,378

Findings and Recommendations (p. 3)

- Misstatement of Levin Financial Activity (Finding 1)
- Reporting of Debts & Obligations (Finding 2)
- Extension of Credit by a Commercial Vendor (Finding 3)

¹ 2 U.S.C. §438(b).

Draft Final Audit Report of the Audit Division on the California Republican Party/V8

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 California Republican Party/V8 (CRP), 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 disclosure of individual contributors' occupation and name of employer;
2. the disclosure of disbursements, debts and obligations;
3. the disclosure of expenses allocated between federal, non-federal, and Levin accounts;
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 Committee

Committee Organization

Important Dates	
• Date of Registration	March 5, 1981 ²
• Audit Coverage	January 1, 2007 – December 31, 2008
Headquarters	
Burbank, California	
Bank Information	
• Bank Depositories	One
• Bank Accounts	Four Federal, One Levin & Ten Non-federal Accounts
Treasurer	
• Treasurer When Audit Was Conducted	Keith Carlson
• Treasurer During Period Covered by Audit	Keith Carlson
Management Information	
• 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	\$ 66,827
o Contributions from Individuals	6,367,753
o Contributions from Other Political Committees	87,646
o Transfers from Affiliated Party Committees	7,557,282
o Transfers from Federal and Levin Accounts	3,389,660
o Other Receipts	188,928
Total Receipts	\$ 17,591,269
o Operating Expenditures	11,110,199
o Transfers to Affiliated/Other Party Committees	3,968,892
o Contributions to Federal Candidates	30,000
o Coordinated Party Expenditures	41,660
o Federal Election Activity	2,392,956
o Contribution Refunds	33,688
Total Disbursements	\$ 17,577,395
Cash-on-hand @ December 31, 2008	\$ 80,701
Levin Cash-on-hand @ January 1, 2007	\$ 11,321
Total Levin Receipts	\$ 620,349
Total Levin Disbursements	\$ 624,378
Levin Cash-on-hand @ December 31, 2008	\$ 7,292

² CRP originally registered with the Secretary of the Senate on August 7, 1974, as the Republican State Central Committee of California Federal Election Account, under a different identification number. This previous committee terminated on August 5, 1981, shortly after the formation of the current Committee.

Part III Summaries

Findings and Recommendations

Finding 1. Misstatement of Levin Financial Activity

During audit fieldwork, a comparison of CRP's reported Levin activity with bank records revealed a material misstatement of receipts and disbursements in 2008. CRP understated receipts and disbursements by \$50,071 and \$54,000, respectively.

In response to the Interim Audit Report recommendation, CRP filed amended reports to correct the misstatements. (For more detail, see p. 4)

Finding 2. Reporting of Debts & Obligations

Audit fieldwork indicated that CRP did not accurately disclose debts and obligations for 28 vendors totaling \$2,188,950 on Schedule D (Debts and Obligations).

In response to the Interim Audit Report recommendation, CRP filed amended reports to correct the debt reporting. (For more detail, see p. 5)

Finding 3. Extension of Credit by a Commercial Vendor

After reviewing and analyzing disbursement records during audit fieldwork, the Audit staff noted that an incorporated vendor appeared to make a prohibited contribution to CRP by extending credit beyond its normal course of business and by failing to make commercially reasonable attempts to collect \$1,071,002 for services rendered.

In response to the Interim Audit Report recommendation, CRP and the vendor presented a detailed analysis of the circumstances that led to the incurred debt, their attempts to devise payment plans to resolve the debt, and why the extension of credit was beneficial to both parties. However, neither CRP nor the vendor provided any documents or examples demonstrating that the extension of credit was in the vendor's ordinary course of business or that commercially reasonable attempts had been made to collect the debts. (For more detail, see p. 7)

Part IV

Findings and Recommendations

Finding 1. Misstatement of Levin Financial Activity

Summary

During audit fieldwork, a comparison of CRP's reported Levin activity with bank records revealed a material misstatement of receipts and disbursements in 2008. CRP understated receipts and disbursements by \$50,071 and \$54,000, respectively.

In response to the Interim Audit Report recommendation, CRP filed amended reports to correct the misstatements.

Legal Standard

A. Reporting. If a state, district or local party committee's combined annual receipts and disbursements for federal election activity (FEA) are \$5,000 or more during the calendar year, then it must disclose receipts and disbursements of Federal funds and Levin funds used for FEA. 11 CFR § 300.36(b)(2).

B. Contents of Levin Reports. Each report must disclose:

- The amount of cash-on-hand for Levin funds at the beginning and end of the reporting period;
- The total amount of Levin fund receipts and disbursements (including allocation transfers) for the reporting period and for the calendar year; and,
- Certain transactions that require itemization on Schedule L-A (Itemized Receipts of Levin Funds) or Schedule L-B (Itemized Disbursements of Levin Funds).
11 CFR § 300.36(b)(2)(B).

Facts and Analysis

A. Facts

As part of fieldwork, the Audit staff reconciled CRP's reported Levin activity with bank records for 2008. The following chart outlines the discrepancies for the beginning cash-on-hand balance, receipts, disbursements and the ending cash-on-hand balance. The succeeding paragraph addresses the reasons for the misstatements.

2008 Committee Activity			
	Reported	Bank Records	Discrepancy
Beginning Cash-on-Hand Balance @ January 1, 2008	\$14,988	\$14,443	\$545 Overstated
Receipts	\$556,470	\$606,541	\$50,071 Understated
Disbursements	\$559,692	\$613,692	\$54,000 Understated
Ending Cash-on-Hand Balance @ December 31, 2008	\$11,766	\$7,292	\$4,474 Overstated

The beginning cash-on-hand balance was overstated by \$545 and is unexplained, but likely resulted from prior period discrepancies. The \$50,071 understatement of receipts resulted mostly from contributions from individuals that were not reported, the understatement of disbursements by \$54,000 resulted from a vendor payment that was not reported, and the \$4,474 overstatement of the ending cash-on-hand balance was the result of the misstatements previously described.

B. Interim Audit Report & Audit Division Recommendation

The Audit staff discussed the reporting errors and presented relevant work papers to the CRP representative at the exit conference. The representative stated that he would review the matter.

The Interim Audit Report recommended that CRP amend its reports to correct the misstatement for 2008 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, CRP should have reconciled the cash balance of its most recent report to identify any subsequent discrepancies that may have impacted the \$4,474 adjustment recommended.

C. Committee Response to Interim Audit Report

In response to the Interim Audit Report recommendation, CRP amended its reports to correct the misstatements. Specifically, CRP amended Schedule A to disclose receipt of \$50,000 from the individuals and payment to a vendor on Schedule B for \$54,000. Prior to the issuance of this report, CRP transferred the remaining funds in its Levin account to a non-federal account, resolving the remaining discrepancies.

Finding 2. Reporting of Debts & Obligations

Summary

Audit fieldwork indicated that CRP did not accurately disclose debts and obligations for 28 vendors totaling \$2,188,950 on Schedule D (Debts and Obligations).

In response to the Interim Audit Report recommendation, CRP filed amended reports to correct the debt reporting.

Legal Standard

A. Continuous Reporting Required. A political committee must disclose the amount and nature of outstanding debts and obligations until those debts are extinguished. 2 U.S.C §434(b)(8) and 11 CFR §§104.3(d) and 104.11(a).

B. Separate Schedules. A political committee must file separate schedules for debts owed by the committee and debts owed to the committee, together with a statement explaining the circumstances and conditions under which each debt and obligation was incurred or extinguished. 11 CFR §104.11(a).

C. Itemizing Debts and Obligations.

- A debt of \$500 or less must be reported once it has been outstanding 60 days from the date incurred (the date of the transaction); the committee reports it on the next regularly scheduled report.
- A debt exceeding \$500 must be disclosed in the report that covers the date on which the debt was incurred. 11 CFR §104.11(b)

Facts and Analysis

A. Facts

During fieldwork, the Audit staff reviewed disbursement records and disclosure reports for proper reporting of debts and obligations. This review identified debts owed to 28 vendors totaling \$2,138,950 that required disclosure. Most of the identified debts were greater than \$500, and all remained outstanding during the reporting period in which they were incurred.

B. Interim Audit Report & Audit Division Recommendation

At the exit conference, the Audit staff discussed these debts with a CRP representative and provided relevant work papers. The representative stated that he would review the matter.

The Interim Audit Report recommended that CRP amend its reports to disclose these debts and obligations on Schedule D.

C. Committee Response to Interim Audit Report

In response to the Interim Audit Report, Counsel for the CRP commented, "...Finding No. 2 does not conclude that the CRP failed to report debts and obligations; rather that the reported debts and obligations by period were inaccurate. Some of these debts and obligations were reported on a later monthly report than the one the FEC auditor found it should have been reported." Counsel for the CRP also commented, "We would like to point out that CRP's largest vendor (Strategic Fundraising (SFI)) was disclosed properly every month."

Commission regulations require continuous reporting of debt and obligations until the debt is extinguished. Our review concluded that several obligations were not continuously disclosed as required on Schedule D; while other obligations were never disclosed on Schedule D. The Audit staff agrees that SFI was not one of the vendors cited in this review.

In response to the Interim Audit Report recommendation, CRP amended its reports to correct the disclosure of debts and obligations on Schedule D.

Finding 3. Extension of Credit by a Commercial Vendor

Summary

After reviewing and analyzing disbursement records during audit fieldwork, the Audit staff noted that an incorporated vendor appeared to make a prohibited contribution to CRP by extending credit beyond its normal course of business and by failing to make commercially reasonable attempts to collect \$1,101,002 for services rendered.

In response to the Interim Audit Report recommendation, CRP and the vendor presented a detailed analysis of the circumstances that led to the incurred debt, their attempts to devise payment plans to resolve the debt, and why the extension of credit was beneficial to both parties. However, neither CRP nor the vendor provided any documents or examples demonstrating that the extension of credit was in the vendor's ordinary course of business or that commercially reasonable attempts had been made to collect the debts.

Legal Standard

A. Corporate Contributions Impermissible. A corporation is prohibited from making any contribution in connection with a federal election. 2 U.S.C. §441b(a).

B. Definition of Commercial Vendor. A commercial vendor is any person who provides goods or services to a candidate or political committee and whose usual and normal business involves the sale, rental, lease or provision of those goods or services. 11 CFR §116.1(c).

C. Extension of Credit by Commercial Vendor. A commercial vendor, whether or not it is a corporation, may extend credit to a candidate or political committee provided that:

- The credit is extended in the vendor's ordinary course of business; and
 - The terms of the credit are similar to the terms the vendor observes when extending a similar amount of credit to a nonpolitical client of similar risk.
- 11 CFR §116.3(a) and (b).

Facts and Analysis

A. Facts

During fieldwork, the Audit staff identified an incorporated vendor that appeared to make a prohibited contribution to CRP by impermissibly extending credit beyond its normal course of business and by not providing documentation demonstrating that the vendor

made commercially reasonable attempts to collect the debts. The vendor, Strategic Fundraising, Inc. (SFI), performed voter/donor file prospecting and telephone fundraising services for CRP. There are 297 invoices, totaling \$1,171,002, which were outstanding between 121 and 757 days. Several of these invoices, dated between October and December 2006, were outstanding for services rendered during the 2006 election cycle. CRP paid all invoices between March and October 2007 and also in November 2008. Other than the initial invoices, CRP made no other documentation available to demonstrate that SFI made further attempts to collect these debts.

B. Interim Audit Report & Audit Division Recommendation

At the exit conference, the Audit staff discussed this matter with a CRP representative and provided relevant work papers for review. The representative stated that he would review the matter.

The Audit staff had questions regarding SFI's billing and payment practices; therefore, a copy of the SFI vendor contract was requested. In response, CRP provided the contract and a letter from SFI addressing the extension of credit. The contract contained the following pertinent provisions:

- While SFI was responsible for planning, preparing, managing and conducting all telephone fundraising efforts directed at both previous and prospective donors, CRP was responsible for collecting, depositing and recording all contributions generated by SFI and providing CRP with regular reports identifying all individuals who contributed to the Committee as a result of SFI's efforts, along with the amount and date of each contribution.
- SFI shall invoice CRP weekly, and CRP shall pay all invoices within 30 days of the invoice date and pay all prospecting invoices upon receipt.
- Outstanding balances 30 days past due shall accrue interest of 1 ½ % compounded monthly.
- The prospective donor fundraising program included a "Break-Even Guarantee," whereby in exchange for the right to be CRP's exclusive telephone fundraising firm, SFI agreed to cover the costs of all calls to prospective contributors. As such, CRP was not expected to pay more for prospecting calls than the sum of all annual contributions generated by those calls. The Guarantee included a provision in which the parties acknowledged that SFI was "accepting significant business risk" by extending the Guarantee to CRP and provided partial mitigation of the risk by granting SFI the exclusive right to conduct CRP's fundraising programs over the course of an entire year.
- SFI would be paid for its prospecting services at "an amount equal to the gross receipts generated by each prospecting project." In addition, if the "cumulative gross proceeds from all Prospecting campaigns performed in a calendar year exceeded the total of all prospecting calls...the positive difference [would] be credited to the Committee."

The letter from SFI stated that credit was extended to CRP because it, as well as many of SFI's other Republican Party clients, was unable to engage in sustainable new donor acquisition, renewal and reactivation of old donors as a result of the external political climate at the time. SFI further stated that it believed at all times that this extension of

credit would further CRP's receipt of new funding, and that at no time did it intend to make a contribution by virtue of its extension of credit. SFI contended that the extension of credit was in its ordinary course of business, and that it followed its established procedures and its past practice with other telephone fundraising clients in the political arena in approving the extension of credit. SFI further added that CRP and SFI negotiated a resolution of disputed billing items by devising a payment plan that involved its continued telephone fundraising for CRP and retention against the outstanding but unpaid balances of receipts until the obligation was satisfied in 2009. SFI contended that it received reasonable, prompt payment in full from CRP based on this extension of credit.

After consideration of all the aspects of this matter, the Audit staff suggested that there were two separate and distinct issues to be considered. First, CRP should have established that SFI's extension of credit was in its ordinary course of business. Second, if the first provision was met, CRP should have demonstrated that SFI made commercially reasonable attempts to collect the debts. If CRP did not establish either provision, a prohibited contribution would have resulted.

Ordinary Course of Business

In determining whether an extension of credit was in the ordinary course of business, the Commission considers whether the vendor followed established procedures and past practices, whether the vendor received prompt payment in full on previous extensions of credit, and whether the extension of credit conformed to the usual and normal practice in the industry (11 CFR §116.3(c)).

In considering similar fundraising agreements, the Commission has sought to determine whether an extension of credit was in a vendor's ordinary course of business by considering the presence of adequate vendor safeguards. The Commission has required committees to have safeguards in place to ensure that committees, in fact, pay for all the costs of the fundraising programs. See MUR 5635 (Conservative Leadership PAC); AO 1991-18 (New York State Democratic Committee); AO 1976-36 (Committee for Family). Safeguards proposed by the Commission have included requiring advance deposits by a committee to reimburse vendors for potential shortfalls, limiting the term of the contract or allowing vendors to terminate the contract early and demand full payment as a result of poor fundraising performance.

The terms of the "Even Guarantee" and the exclusivity clause in the contract raise a question of whether SFI's extension of credit to CRP was in its ordinary course of business. The Guarantee appears very similar to the type of "no-risk" or "limited-risk" provisions that, in previous matters, the Commission has found could constitute in-kind contributions in the absence of safeguards ensuring that (1) the committee would pay for all of the costs of the fundraising programs and (2) the vendor would bear all of the financial risk of programs not paying for themselves (MUR 5635; AO 1991-18; AO 1979-36). However, unlike the previous cases, SFI was not responsible for the "caging" of contributions resulting from its fundraising activity. The contract outlines that contributions were to be sent to CRP, which was supposed to deposit them in its own account and then pay the invoiced amounts to SFI. This provision, in combination with

the Guarantee, raises questions as to whether the arrangement between CRP and SFI was one in which “the committee retain[ed] contribution proceeds while giving up little, or assum[ing] little to no risk with the vendor bearing all, or nearly all the risk.” See AO 1991-18 (New York State Democratic Party). It appears that the exclusivity clause was included to offset any risk that prospecting calls would not generate contributions sufficient to cover SFI’s costs in making them. This raises a question regarding whether this clause provided sufficient financial value to SFI such that it negated SFI’s assumption of the risk that it would lose money on the prospecting calls. However, absent additional information showing that the value of the exclusivity clause was comparable to SFI’s financial risk or that “no-risk” or “limited-risk” agreements such as the Guarantee between CRP and SFI conform to the usual and normal practices in the telemarketing industry, the Audit staff concludes that SFI did not extend credit to CRP in its ordinary course of business.

Commercially Reasonable Debt Collection

Even where an extension of credit by a commercial vendor is legally permissible when made, it may evolve into a contribution over time through the lack of commercially reasonable attempts on the part of the vendor to collect the resulting debt. The Commission determines that these attempts are commercially reasonable if the vendor has pursued its remedies as vigorously as it would pursue its remedies against a non-political debtor in similar circumstances (11 CFR §116.4(d)(2)). In this matter, it appears that many of the debt collection provisions outlined in the contract were not fulfilled.

- As previously mentioned, other than initial invoices, no other documentation was made available to demonstrate that CRP was billed weekly or that any further attempts were made to collect these debts.
- No documentation was presented to the Audit staff to demonstrate that CRP was billed the 4.2% interest compounded monthly, for its debts outstanding more than 30 days.

In regard to the items submitted by SFI, SFI admits that credit was extended to CRP and other political clients. It also mentions a negotiated repayment plan; however, this has never been discussed with the Audit staff nor presented to the Audit staff for review.

The Interim Audit Report recommended that CRP provide documentation or any other comments to demonstrate that SFI extended credit to CRP in its ordinary course of business. The documentation should have included, but not have been limited to, evidence that (1) the “Break Even Guarantee” within the SFI contract is common industry practice, (2) verification that the value of the exclusivity clause provided sufficient financial value to SFI such that it negated SFI’s assumption of the risk that it would lose money on the prospecting calls, and (3) confirmation that the terms of the credit are similar to the terms SFI observes when extending a similar amount of credit to a nonpolitical client of similar risk.

In addition, the Interim Audit Report recommended that CRP provide documentation or any other comments to demonstrate that SFI made commercially reasonable attempts to collect these debts. The documentation should have included, but not been limited to, evidence supporting the negotiated payment plan and examples of other SFI customers or

clients of similar risk for which similar services had been provided and similar billing arrangements had been utilized. CRP should have also provided documentation concerning SFI's billing policies for similar clients and work, advance payment policies, debt collection policies, and billing cycles.

Absent such a demonstration, the Audit staff would consider the \$1,171,002 an impermissible contribution from SFI.

C. Committee Response to Interim Audit Report

In response to the Interim Audit Report recommendation, CRP and the Chief Financial Officer of SFI (CFO) dispute that the extension of credit by SFI resulted in a corporate contribution.

CRP discussed the many factors that led to its incurrence of the debt to SFI. Specifically, CRP presented the following:

1. Fundraising is Cyclical - CRP stated that it incurred most of its SFI debt during its traditional drought period, the off-election year (2007). CRP stated "the CRP's traditional fundraising cycle has peaks and valleys, and the valley in 2007 after the big California gubernatorial election of 2006 and the decline of national Republican fortunes in the 2006 Congressional elections, was especially large and problematic."
2. CRP Organizational Changes and the Decline in Direct Mail and Tele-Fundraising Rates – CRP stated that it, like many organizations that engage in direct mail and tele-fundraising efforts, suffered a decline in fundraising receipts from these activities. CRP also discussed the turnover in key upper management positions (Chairman and Chief Operating Officer) and how this affected its ability to resolve some of its debt issues.
3. National and State Decline in Republican Fortunes – CRP stated "Like other Republican organizations that engage in direct mail and tele-fundraising, the CRP also suffered a loss of brand identification and support that was related to the declining popularity of the national administration and special conditions in California, where in 2006, Republicans had suffered a loss of all but two statewide Republican officeholders." CRP further added, "the CRP suffered a loss of larger dollar donors in part because its major statewide officeholder, Governor Schwarzenegger, had declared after his re-election in 2006 that he no longer considered himself as a partisan Republican governor, and he described his party as a damaged brand." CRP stated that, beginning in early 2007, Governor Schwarzenegger ceased to assist CRP in fundraising.

CRP contended that SFI made commercially reasonable efforts to collect the CRP debt. As evidence of these attempts, CRP stated that it engaged in good faith discussions and negotiations to resolve the debt to SFI. CRP added that many of its officers and key employees were in constant, regular communications with SFI. In addition, CRP's Board of Directors received regular briefings at each board meeting regarding the growing debt, and CRP key staff visited SFI offices in Minnesota to negotiate a strategy to resolve the debt.

As further evidence that SFI made commercially reasonable efforts to collect the CRP debt, CRP stated that it was billed monthly on all telemarketing and direct mail matters, that it had hundreds of separate communications by telephone, email and face-to-face with SFI representatives relating to the debt matter, and that SFI's invoices included finance charges.

Counsel for the CRP commented that in July 2008 a negotiated agreement with SFI "(1) resolved disputes about billing items; (2) negotiated a set aside of SFI-generated tele-fundraising receipts that were dedicated and credited to pay-down of the CRP debt; and (3) extended the SFI-CRP fundraising agreement into 2009-2010."

CRP contended that the fundraising agreement was in SFI's ordinary course of business. In response to the concern that the agreement with SFI did not provide for it to cage and sequester funds necessary to pay its bills, CRP stated that it chose to separate caging functions from all its fundraising vendors and that it had a separate caging vendor and agreement. CRP points out two critical facts: First, CRP was one of the largest, if not the largest, of SFI's client. CRP stated that this better ensured compliance with FEC and non-federal campaign reporting requirements. Second, CRP's financial situation during 2007 and 2008 resulted in delayed payments to vendors. The separate caging agreement allowed for it to balance payments to vendors with "keeping its doors open."

To supplement its Interim Audit Report response, CRP provided comments from the CFO to address that credit was extended in the normal course of business. The CFO contended that extending credit was in the best interest of CRP from a prospecting and fundraising perspective, and in the best interest of SFI from the perspective of helping a valued, long term client by working out a mutually beneficial payment plan. The CFO stated that it believed that by continuing to prospect and fundraise for CRP, in spite of the debt, not only would fundraising goals eventually be realized but its donor base would not decline in base value and CRP would possibly acquire new donors. The CFO stated that the result of extending credit to CRP would be CRP gaining new or lapsed donors and being eventually paid. Therefore, SFI extended credit to CRP. The CFO noted that at no time had SFI intended to make a contribution to the CRP by virtue of an extension of credit.

Regarding the "break even guarantee" and the exclusivity provision within the CRP and SFI agreement, the CFO stated, "Without disclosing too much of the details of our business model or explaining how fundraising works, SFI will stress that our standard fundraising agreements with all political clients call for exclusivity. As a company, we understand the need to acquire new donors for the long-term health of our partners like the CRP and we have a 20 year history which allows us to mitigate our internal 'risk'. All other tele-fundraising firms offer the exact or similar 'break-even guarantee'. As pointed out above, we issue credit to non-political clients as well in the exact same fashion."

Regarding SFI's commercially reasonable attempts to collect the CRP debt, the CFO contended that besides its normal weekly invoices, SFI also sends out via an e-mail link bi-weekly summaries and open invoice reports which contain the 'aging' for each client.

He added that this was done for all SFI clients, political and non-profit. As further evidence, the CFO stated, "SFI requested and was presented with several informal payment plans in the fall/winter of 2007. They would be adhered to for a while, and then the CRP would be unable to keep up with the payments..." The CFO concurs with Counsel that a new agreement was created in 2008 that resulted in the debt being paid off in early 2009.

Assessment by the Audit Staff

After reviewing the responses submitted by CRP and the CFO, the Audit staff made the following observations regarding CRP's adherence to the Interim Audit Report recommendation:

1. Other than providing written comments, no documentation was submitted to demonstrate that SFI extended credit to CRP in its ordinary course of business. The CFO stated that the "Break Even Guarantee" and the exclusivity clause within the SFI contract is common industry practice, but no examples of other client contracts or any supporting documentation was provided to verify this statement. The CFO cites confidentiality clauses in contracts with its non-profit clients that do not fall under the purview of the Commission. In addition, neither CRP nor the CFO provided confirmation that the terms of the credit issued to CRP are similar to the terms SFI observes when extending a similar amount of credit to a nonpolitical client of similar risk.

Further research by the Audit staff indicates that the "Break Even Guarantee" and the exclusivity clause are not unusual in the fundraising industry. SFI does not "cage" the contributions resulting from the fundraising activity. Under its contract, contributions were to be sent directly to CRP which was to deposit the contributions in its own account and then pay the invoiced amounts to SFI. This provision, in combination with the Guarantee, raises questions as to whether the arrangement between CRP and SFI was one in which CRP retained contribution proceeds while giving up little, or assuming little to no risk with the SFI bearing all, or nearly all the risk. The Audit staff's research also indicates this provision is not unusual.

Documentation was not provided to demonstrate any particular financial value of the exclusivity clause. If the exclusivity clause provided value to SFI sufficient to negate SFI's assumption of the risk that it would lose money on the prospecting calls, the extension of credit would result in no contribution. Further research by the Audit staff indicates that when a contract contained an exclusivity clause as a safeguard against losses by the vendor; it was not the only safeguard, as it is in CRP's contract with SFI.

2. CRP and the CFO both detail SFI's attempts at collecting the CRP debt. However, neither provided any evidence to support the various negotiated payment plans, the bi-weekly summaries or open invoice reports, the meetings between CRP and SFI officials, the hundreds of communications between the two parties, etc. In addition, neither CRP nor the CFO provided any examples of

other SFI customers or clients of similar risk for which similar services had been provided and similar billing arrangements had been utilized.

SFI's effort to convince the CRP to resume the fundraising program and SFI's continued provision of services when CRP had repeatedly failed to pay raises the question of whether SFI's debt collection efforts were commercially reasonable. Among the debt collection practices that may be regarded as evidence of commercial reasonableness is the withholding of additional services until overdue debts are satisfied. Here, it appears the opposite happened; CRP, concerned about the level of debt it had accumulated, sought to suspend delivery of services from SFI, and it was SFI that convinced CRP that the only viable way for CRP to get out of debt to SFI was for it to continue the fundraising program. If this is correct, it may be that SFI's decision to give CRP additional time to pay and SFI's decision to continue providing services was commercially reasonable. However, the Audit staff believes that additional information is necessary to reach this conclusion. SFI asserted in its response that, as part of its efforts to convince the CRP, it met with CRP and presented a detailed house file analysis which included details on historical fundraising trends and renewal rates. In addition, SFI contended that this meeting led to a better understanding of the need to prospect and fundraise to help CRP out of the situation it found itself in. Information supporting this contention by SFI would be precisely the type of information that would demonstrate the commercial reasonableness of SFI's course. In addition, the specifics of the negotiated payment plans and how the plans compare to the terms SFI has provided to similarly situated non-political clients may also demonstrate the commercial reasonableness and reasonable debt collection efforts by SFI. However, while both CRP and SFI say that SFI provided such information to CRP in 2008, neither has provided a copy of the detailed house file analysis or the specifics of the negotiated payment plans to the Audit staff.

After reviewing the responses to the Interim Audit Report submitted by CRP and the CFO, the Audit staff concludes that CRP has not demonstrated that SFI extended credit with its ordinary course of business or that commercially reasonable attempts were made to collect the CRP debt. Until further documentation is provided by CRP, the Audit staff will consider this matter an impermissible contribution of \$1,171,002 to CRP.



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

January 14, 2013

MEMORANDUM

TO: Thomas Hintermister
Assistant Staff Director
Audit Division

FROM: Lisa J. Stevenson *LJS*
Deputy General Counsel - Law

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Assistant General Counsel
Public Finance and Audit Advice

Danita C. Alberico *DCA*
Attorney

SUBJECT: Draft Final Audit Report – California Republican Party/V8
Legal Comments on Committee Response
(LRA 829)

I. INTRODUCTION

The Office of General Counsel (“OGC”) has reviewed the proposed Draft Final Audit Report (“DFAR”) on the California Republican Party/V8 (“Committee”), as well as the responses to the DFAR submitted by the Committee and Strategic Fundraising, Inc. (“SFI”). We concur with the Audit Division’s findings in the DFAR. In this memorandum, we evaluate the Committee’s contention with respect to Finding 3 (Extension of Credit by a Commercial Vendor) that its fundraising contract with SFI contained adequate safeguards. We also conclude that SFI’s waiver of the Committee’s accrued interest obligations was inconsistent with the Commission’s legal framework for debt settlement and/or forgiveness. The debt settlement issue is not addressed in the DFAR as neither the Audit Division nor OGC had sufficient information, prior to the responses of the Committee and SFI, to discern whether the debt was, in fact, settled or partially forgiven. We recommend that the auditors address the debt settlement issue in the Audit Division Recommendation Memorandum. If you have any questions, please contact Danita C. Alberico, the attorney assigned to this audit.

II. INITIAL EXTENSION OF CREDIT: SFI ASSERTS THAT THE FUNDRAISING CONTRACT CONTAINED ADEQUATE SAFEGUARDS TO ASSURE THAT ALL COSTS WERE PAID

SFI asserts that its initial extension of credit to the Committee was in the ordinary course of business because, in addition to the exclusivity clause, its contract contained two additional safeguards to ensure that the Committee paid for the costs of the fundraising program. Response to Draft Final Audit of 2007-2008 Election Cycle for California Republican Party, C#000014590, (Dec. 6, 2012) (“SFI Response”). Specifically, SFI first points to the purported “short-term” nature of its contract which was mandated by the Committee’s “bylaws forbid[ding] it [the Committee] from entering into agreements that span across two board terms [and] essentially limiting the contract to approximately two years.” *Id.* Second, SFI noted that the contract contained “a termination clause that either party could execute for any reason.” *Id.*

The safeguards that SFI highlights are examples of the potential types of protections that the Commission has focused on in the past in determining whether a fundraising program may have resulted in a prohibited in-kind contribution to a committee. *See* MUR 5635 (Commission concluded that contract resulted in contributions from fundraising firm because the arrangement was not in the ordinary course of business given the size of the disbursements and short-term nature of the program); Advisory Opinion 1991-18 (safeguards proposed by the Commission included requiring advance deposits by a committee to reimburse vendors for potential shortfalls, limiting the term of the contract, or allowing vendors to terminate the contract early and demand full payment as a result of poor fundraising performance); Advisory Opinion 1979-36 (addressing a “limited risk” fundraising contract where the committee was only required to pay three-fourths of the total amount of contributions received irrespective of the actual amount of fees and expenses). In our comments on the DFAR, we had not previously evaluated either the term of the contract or its termination clause as potential safeguards but rather focused on the exclusivity clause in evaluating whether the contract may have resulted in a contribution to the Committee.

Looking at the contract as a whole, questions still remain about the initial extension of credit from SFI to the Committee and whether there were adequate safeguards to ensure that the Committee bore a sufficient amount of the cost or the risk of the fundraising program. The Committee failed to provide a valuation of the exclusivity clause as requested by the auditors, or other pertinent information, showing that the exclusive nature of the contract was of sufficient value to offset the risk to SFI. Thus, in the absence of information regarding the value of the exclusivity clause, we still concur with the DFAR and do not believe the contract’s term and at-will termination provisions are in the aggregate sufficient to support a conclusion that SFI’s initial extension of credit to the Committee was in the ordinary course of business.¹

¹ The Audit Division may need to revisit the issue of the adequacy of the safeguards in the SFI contract pending the Commission’s final decision on a similar issue in the Proposed Final Audit Report

Further, SFI's "waiver" of accrued interest on the Committee's outstanding debt resulted in some of the costs arising out of the SFI fundraising program being left unpaid by the Committee. "With respect to the payment or non-payment of an extension of credit, the Commission has made plain that in political committee fundraising, 'none of the costs of the program [may] be left unpaid by the Committee.'" General Counsel's Report #2, MUR 5635, at 8 (quoting Advisory Opinion 1990-14). As discussed in Section III below, the Committee resolved payment of its outstanding debt with SFI in a manner that is inconsistent the Commission's legal framework for addressing debts owed by committees.

III. WAIVER OF DEBT ARISING OUT OF INITIAL EXTENSION OF CREDIT: THE COMMITTEE AND SFI NEGOTIATED A WAIVER OF ACCRUED INTEREST THAT IS INCONSISTENT WITH THE COMMISSION'S LEGAL FRAMEWORK FOR RESOLVING DEBT

The other issue that must be addressed is whether SFI's waiver of interest, which was accrued pursuant to the provisions of the fundraising contract, results in a contribution. The DFAR found that the Committee failed to pay several invoices for SFI voter/donor file prospecting, caging, fundraising and mailing services for periods ranging from approximately four months to two years. DFAR at 8. The SFI invoices totaled \$1,171,002. *Id.* Initially, SFI contended that it continued to provide services to the Committee to help the Committee satisfy the debt, but neither SFI nor the Committee submitted information in response to the DFAR to indicate that such an approach was commercially reasonable. 11 C.F.R. §§ 116.4(b) and (d).

Instead, in its response to the DFAR, the Committee states that it negotiated a settlement of its debt to SFI and that "SFI [was] effectively paid in full" for its telemarketing services. Further Response to [Draft] Final Audit Report for the 2007-2008 Election Cycle for California Republican Party, C#000014590 at 2 (Dec. 9, 2012) ("Committee Response"). The Committee explains that SFI waived the accrued interest on the unpaid balances owed to SFI subject to the Committee's "agreement (a) that it would meet its obligations to pay the balance of amounts outstanding . . . and (b) the [Committee] and SFI were to negotiate an extension of the fundraising agreement for the 2009 and 2010 cycle."² *Id.* at 3.

("PFAR") on Rightmarch.com PAC. In Rightmarch, the safeguards included the right of the vendor to terminate the contract early and demand full payment and to slow the pace of fundraising if the contract was not profitable. During the Commission's consideration of the Audit Division Recommendation Memorandum in Rightmarch, the Commission split 3-3 on the issues of whether credit was extended to Rightmarch in the ordinary course of a commercial vendor's business and whether Rightmarch incurred reportable debt as a result of its fundraising contract with the commercial vendor. In accordance with Directive 70, the Audit Division will present these issues in the "Additional Issues" section in the Rightmarch PFAR.

² The contract between the Committee and SFI provides that "outstanding balances 30 days past due shall accrue interest in the amount of 1 ½ percent, compounded monthly." Fundraising Services Contract dated November 1, 2006 between Strategic Fundraising Services, Inc. and the California Republican Party.

The Committee and SFI may have settled the debt, but they did so without the Commission's approval. The Committee is an ongoing committee, and ongoing committees cannot settle any outstanding debts for less than the entire amount owed. 11 C.F.R. § 116.2(b).

Although the Committee claims that the settlement with SFI was necessary for it to "keep its doors open," the Commission has previously considered and rejected allowing debt settlements by ongoing committees. The Commission prohibits settlements by ongoing committees because "these committees have the intention to continue to solicit funds and engage in election related activity." Explanation and Justification for Debts Owed by Terminating Committees, Ongoing Committees and Authorized Committees, 55 Fed. Reg. 26,379 (June 27, 1989). Under these circumstances, "the settlement of an ongoing committee's debt cannot be considered to be commercially reasonable given that the committee is continuing to receive funds that could be used to pay its past debts." *Id.* The Commission notes that "by freeing additional funds for future electoral activity, such a practice could result in direct subsidization of a political committee's speech beyond the committee's ordinary capacity." *Id.* Here, the Committee continued to fundraise under its telemarketing contract with SFI and had the ability to work its way out of debt – including paying the interest that had accrued pursuant to the contract. Instead, the Committee settled its obligations, in part, through an agreement not to pay the accrued interest on the debt contrary to Commission regulations.³

Creditors may, in certain limited circumstances, forgive debts of ongoing committees as prescribed in 11 C.F.R. § 116.8. See 11 C.F.R. § 116.2(b). This settlement does not qualify for creditor forgiveness under section 116.8 because, among other factors, the Committee's whereabouts were known to SFI and the Committee had receipts of at least \$1,000 and disbursements of at least \$1,000 during the 24 months prior to when the debt was settled. 11 C.F.R. § 116.8(a)(1) and (2). A creditor that intends to forgive a debt must, in addition to satisfying the requirements of section 116.8, follow the procedures outlined for notifying and obtaining approval from the Commission, which also were not followed here.

Since the settlement of the Committee's obligation to pay the accrued interest is a part of the analysis of whether the Committee satisfied its debt to SFI, we recommend that the auditors address this debt settlement issue in the Audit Division Recommendation Memorandum.

³ Even if the Committee was a terminating committee and could therefore settle its debt, it did not follow the Commission's procedures for doing so. In particular, the committee must submit, and the Commission will consider, the committee's plan to terminate, its cash on hand, expenditures and receipts, the total amount of debts and number of creditors owed, the total dollar amount and percentage of debt proposed to be settled or forgiven and the length of time the debt has been overdue. 11 C.F.R. § 116.7(f). None of those steps were followed here.