

AGENDA DOCUMENT NO. 15-21-A



FEDERAL ELECTION COMMISSION
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April 27, 2015

MEMORANDUM

AGENDA ITEM

To: The Commission

Through: Alec Palmer
Staff Director

Handwritten signature of Alec Palmer, consisting of the letters "AP" in a stylized, cursive font.

From: Patricia C. Orrock
Chief Compliance Officer

Handwritten signature of Patricia C. Orrock, consisting of the letters "PCO" in a stylized, cursive font.

Thomas E. Hintermister
Assistant Staff Director
Audit Division

Handwritten signature of Thomas E. Hintermister, consisting of the letters "TH" in a stylized, cursive font.

Kendrick Smith
Audit Manager

Handwritten signature of Kendrick Smith, consisting of the letters "KS" in a stylized, cursive font.

By: xv Brenda Wheeler
Lead Auditor

Handwritten signature of Brenda Wheeler, consisting of the letters "BW" in a stylized, cursive font.

Subject: Audit Division Recommendation Memorandum on Kevin McCarthy for Congress (KMFC) (A13-02)

For Meeting of 5-21-15

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 has reviewed this memorandum and concurs with the recommendations.

Finding 1. Receipt of Contributions in Excess of the Limit

The Audit staff determined that KMFC received excessive contributions totaling \$77,094. These errors occurred as a result of KMFC not resolving the excessive portions of contributions by forwarding presumptive letters to the contributors or issuing refunds in a timely manner. In response to the exit conference following fieldwork, KMFC provided copies of presumptive letters that were sent to the contributors. As a result, KMFC has resolved the excessive contributions, albeit in an untimely manner. In response to the Interim Audit Report recommendation, KMFC stated that it believes presumptive letters were sent to its contributors in a timely manner; however, it cannot prove such action was taken with a degree of acceptable certainty. KMFC reiterated its position in its response to the DFAR.

The Audit staff recommends that the Commission find that KMFC received excessive contributions totaling \$77,094.

Finding 2. Misstatement of Financial Activity

The Audit staff determined that KMFC misstated its financial activity for calendar years 2011 and 2012. In 2011, beginning cash-on-hand was overstated by \$41,170, receipts were understated by \$62,407, disbursements were overstated by \$35,501, and ending cash-on-hand was understated by \$56,738. In 2012, only the beginning and ending cash-on-hand were misstated. Beginning cash-on-hand was understated by \$56,738 and ending cash-on-hand was understated by \$73,397. However, subsequent to audit notification, KMFC filed amended disclosure reports which materially corrected the misstatements identified by the Audit staff. As such, KMFC has corrected the public record. In response to the Interim Audit Report recommendation, KMFC noted that it has made organizational changes and adopted new internal procedures and safeguards to minimize future administrative issues. As part of its response to the DFAR, KMFC provided a detailed chronology of actions taken to improve its financial and reporting obligations.

The Audit staff recommends that the Commission find that KMFC misstated its financial activity for calendar years 2011 and 2012.

KMFC did not request an audit hearing.

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.

Attachment:

Draft Final Audit Report of the Audit Division on Kevin McCarthy for Congress

cc: Office of General Counsel



Draft Final Audit Report of the Audit Division on Kevin McCarthy for Congress (January 1, 2011 – December 31, 2012)

Why the Audit Was Done

Federal law permits the Commission to conduct audits and field investigations of any political committee that is required to file reports under the Federal Election Campaign Act¹ (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.² The audit determines whether the committee complied with the limitations, prohibitions and disclosure requirements of the Act.

Future Action

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

About the Campaign (p. 2)

Kevin McCarthy for Congress is the principal campaign committee for Kevin McCarthy, Republican candidate for the U.S. House of Representatives from the state of California, 23rd Congressional District, and is headquartered in Bakersfield, California. For more information, see the Campaign Organization chart, p. 2.

Financial Activity (p. 2)

• Receipts	
○ Contributions from Individuals	\$ 1,923,173
○ Contributions from Political Committees	2,422,238
○ Transfers from Authorized Committees	263,000
○ Offset to Operating Expenditures	27,616
○ Other Receipts	21,298
Total Receipts	\$ 4,657,325
• Disbursements	
○ Operating Expenditures	\$ 2,240,241
○ Contribution Refunds	41,692
○ Other Disbursements	1,710,453
Total Disbursements	\$ 3,992,386

Findings and Recommendations (p. 3)

- Receipt of Contributions in Excess of the Limit (Finding 1)
- Misstatement of Financial Activity (Finding 2)

¹ On September 1, 2014, the Federal Election Campaign Act of 1971, as amended (“the Act”), was transferred from Title 2 of the United States Code to new Title 52 of the United States Code.

² 52 U.S.C. §30111(b) (formerly 2 U.S.C. §438(b)).

Draft Final Audit Report of the Audit Division on Kevin McCarthy for Congress

(January 1, 2011 – December 31, 2012)

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Part I

Background

Authority for Audit

This report is based on an audit of Kevin McCarthy for Congress (KMFC), undertaken by the Audit Division of the Federal Election Commission (the Commission) in accordance with the Federal Election Campaign Act of 1971, as amended (the Act). The Audit Division conducted the audit pursuant to 52 U.S.C. §30111(b) (formerly 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 52 U.S.C. §30104 (formerly 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. 52 U.S.C. §30111(b) (formerly 2 U.S.C. §438(b)).

Scope of Audit

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

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

Part II

Overview of Campaign

Campaign Organization

Important Dates	
• Date of Registration	March 10, 2006
• Audit Coverage	January 1, 2011 – December 31, 2012
Headquarters	
Bakersfield, California	
Bank Information	
• Bank Depositories	Six
• Bank Accounts	Two checking, Four savings
Treasurer	
• Treasurer When Audit Was Conducted	Jill Thomson (October 12, 2012 – present)
• Treasurer During Period Covered by Audit	Raymond Karp (August 1, 2007 – October 11, 2012) Jill Thomson (October 12, 2012 – present)
Management Information	
• Attended Commission Campaign Finance Seminar	
• Who Handled Accounting and Recordkeeping Tasks	Paid Staff

Overview of Financial Activity (Audited Amounts)

Cash-on-hand @ January 1, 2011	\$ 1,159,230
Receipts	
○ Contributions from Individuals	1,923,173
○ Contributions from Political Committees	2,422,238
○ Transfers from Authorized Committees	263,000
○ Offsets to Operating Expenditures	27,616
○ Other Receipts	21,298
Total Receipts	\$ 4,657,325
Disbursements	
○ Operating Expenditures	2,240,241
○ Contribution Refunds	41,692
○ Other Disbursements	1,710,453
Total Disbursements	\$ 3,992,386
Cash-on-hand @ December 31, 2012	\$ 1,824,169

Part III Summaries

Findings and Recommendations

Finding 1. Receipt of Contributions in Excess of the Limit

During audit fieldwork, the Audit staff reviewed contributions from individuals to determine if any exceeded the contribution limit. This review indicated that KMFC received apparent excessive contributions totaling \$77,094. These errors occurred as a result of KMFC not resolving the excessive portions of contributions by forwarding a presumptive letter to the contributor or issuing a refund in a timely manner. In response to the exit conference following fieldwork, KMFC provided copies of presumptive letters that were sent to the contributors. As a result, KMFC has resolved the excessive contributions, albeit in an untimely manner. In response to the Interim Audit Report recommendation, KMFC stated that it believes that presumptive letters were sent to its contributors in a timely manner; however, it cannot prove such action was taken with a degree of acceptable certainty. (For more detail, see page 10.)

Finding 2. Misstatement of Financial Activity

During audit fieldwork, a comparison of KMFC's reported activity with its bank records identified misstatements in 2011 and 2012. In 2011, beginning cash-on-hand was overstated by \$41,170, receipts were understated by \$62,577, disbursements were overstated by \$35,501, and ending cash-on-hand was understated by \$56,738. In 2012, only the beginning and ending cash-on-hand were misstated. Beginning cash-on-hand was understated by \$56,738 and ending cash-on-hand was understated by \$73,397. However, subsequent to audit completion, KMFC filed amended disclosure reports which materially corrected the misstatements identified by the Audit staff. As such, KMFC has corrected the public record. In response to the Interim Audit Report recommendation, KMFC noted that it has made organizational changes and adopted new internal procedures and safeguards to minimize future administrative issues. (For more detail, see page 11.)

Part IV

Findings and Recommendations

Finding 1. Receipt of Contributions in Excess of the Limit

Summary

During audit fieldwork, the Audit staff reviewed contributions from individuals to determine if any exceeded the contribution limit. This review indicated that KMFC received apparent excessive contributions totaling \$77,094. These errors occurred as a result of KMFC not resolving the excessive portions of contributions by forwarding a presumptive letter to the contributor or issuing a refund in a timely manner. In response to the exit conference following fieldwork, KMFC provided copies of presumptive letters that were sent to the contributors. As a result, KMFC has resolved the excessive contributions, albeit in an untimely manner. In response to the Interim Audit Report recommendation, KMFC stated that it believes that presumptive letters were sent to its contributors in a timely manner; however, it cannot prove such action was taken with a degree of acceptable certainty.

Legal Standard

- A. Authorized Committee Limits.** During the election cycle for which this audit is being completed, the relevant contribution limits were \$2,500 per election from any one person or \$5,000 per election from a multiple candidate political committee. 52 U.S.C. §30116(a)(1)(A), (2)(A) and (f) (formerly 2 U.S.C. §441a(a)(1)(A), (2)(A) and (f)); 11 CFR §§110.1(a)(1)(b) and 110.1(a).
- B. Handling Contributions That Appear Excessive.** If a committee receives a contribution that appears to be excessive, the committee must either:
- Return a questionary check to the donor; or
 - Deposit the credit into its federal account and:
 - Keep enough money in the account to cover all potential refunds;
 - Keep a written record explaining why the contribution may be illegal;
 - Include this explanation on Schedule A if the contribution has to be itemized before its legality is established;
 - Send a reattribution or a redesignation of the excessive portion, following the instructions provided in the Commission regulations (see below for explanations of reattribution and redesignation); and
 - If the committee does not receive a proper reattribution or redesignation within 60 days after receiving the excessive contribution, refund the excessive portion to the donor. 11 CFR §§103.3(b)(3), (4) and (5) and 110.1(k)(3)(ii)(B).
- C. Joint Contributions.** Any contribution made by more than one person (except for a contribution made by a partnership must include the signature of each contributor on the check, money order, or other negotiable instrument or in a separate writing. A joint contribution is attributed equally to each donor unless a statement indicates that the funds should be divided differently. 11 CFR §110.1(k)(1) and (2).

D. Reattribution of Excessive Contributions. The Commission regulations permit committees to ask donors of excessive contributions (or contributions that exceed the committee's net debts outstanding) whether they had intended their contribution to be a joint contribution from more than one person and whether they would like to reattribute the excess amount to the other contributor. The committee must inform the contributor that:

- The reattribution must be signed by both contributors;
 - The reattribution must be received by the committee within 60 days after the committee received the original contribution; and
 - The contributor may instead request a refund of the excessive amount.
- 11 CFR §110.1(k)(3).

Within 60 days after receiving the excessive contribution, the committee must either receive the proper reattribution or refund the excessive portion to the donor. 11 CFR §§103.3(b)(3) and 110.1(k)(3)(ii)(B). Further, a political committee must retain written records concerning the reattribution in order for it to be effective. 11 CFR §110.1(l)(5).

Notwithstanding the above, any excessive contribution that was made on a written instrument that is imprinted with the names of more than one individual may be attributed among the individuals listed unless instructed otherwise by the contributor(s). The committee must inform each contributor:

- How the contribution was attributed; and
- The contributor may instead request a refund of the excessive amount.

E. Redesignation of Excessive Contributions. When an authorized candidate committee receives an excessive contribution (or a contribution that exceeds the committee's net debts outstanding), the committee may ask the contributor to redesignate the excess portion of the contribution for use in another election. The committee must inform the contributor that:

- The redesignation must be signed by the contributor;
- The redesignation must be received by the committee within 60 days after the committee received the original contribution; and
- The contributor may instead request a refund of the excessive amount.

Within 60 days after receiving the excessive contribution, the committee must either receive the proper redesignation or refund the excessive portion to the donor. 11 CFR §§103.3(b)(3) and 110.1(b)(5)(ii)(A). Further, a political committee must retain written records concerning the redesignation in order for it to be effective. 11 CFR §110.1(l)(5).

When an individual makes an excessive contribution to a candidate's authorized committee, the campaign may presumptively redesignate the excessive portion to the general election if the contribution:

- Is made before that candidate's primary election;
- Is not designated in writing for a particular election;
- Would be excessive if treated as a primary election contribution; and

- As redesignated, does not cause the contributor to exceed any other contribution limit. 11 CFR §110.1(b)(5)(ii)(B)(1)-(4).

The committee is required to notify the contributor of the redesignation within 60 days of the treasurer's receipt of the contribution, and must offer the contributor the option to receive a refund instead.

Facts and Analysis

A. Facts

During audit fieldwork, the Audit staff utilized a combination of sample testing and focused reviews to identify apparent excessive contributions from individuals totaling \$77,094.³ All the excessive contributions (\$77,094) were the result of KMFC not resolving the excessive portion of contributions by timely forwarding a presumptive letter to its contributors informing them how their contribution had been redesignated and/or reattributed, or refunding the excessive contribution.

B. Interim Audit Report & Audit Division Recommendation

The Audit staff discussed this matter during the exit conference at the conclusion of fieldwork and provided KMFC representatives with a schedule of the apparent excessive contributions. The representatives asked questions regarding the presumptive reattribution and/or redesignation letters that could be issued based on the sample projection.

In response to the exit conference, the representatives submitted presumptive reattribution and redesignation letters that were sent to the contributors relative to the apparent excessive contributions. In total, the representatives provided evidence that it had sent more presumptive letters to its contributors than identified in the sample projection. As a result, KMFC has resolved the excessive contributions, albeit untimely.

The Interim Audit Report recommended that KMFC provide any comments it deemed relevant to this matter.

C. Committee Response to Interim Audit Report

In response to the Interim Audit Report recommendation, KMFC disagreed with the Audit staff's conclusion that the presumptive letters were issued untimely. KMFC believes that it did timely forward presumptive letters to its contributors informing them how their contributions had been redesignated and/or reattributed. KMFC further stated that, because the issuance and tracking of the presumptive letters would have been handled by its prior treasurer, it could not prove with a degree of acceptable certainty that these letters were timely sent to contributors.

³ The sample error amount was projected using a Monetary Unit Sample with a 95 percent confidence level plus the result of a focused review of contributions not included in the sample population. The sample estimate could be as low as \$53,334 and as high as \$130,427.

The Audit staff maintains that, absent records to substantiate the presumptive letters were timely sent to its contributors, the corrective action taken by KMFC is untimely.

Finding 2. Misstatement of Financial Activity

Summary

During audit fieldwork, a comparison of KMFC's reported activity with its bank records identified misstatements in 2011 and 2012. In 2011, beginning cash-on-hand was overstated by \$41,170, receipts were understated by \$62,407, disbursements were overstated by \$35,501 and ending cash-on-hand was understated by \$56,738. In 2012, only the beginning and ending cash-on-hand were misstated. Beginning cash-on-hand was understated by \$56,738 and ending cash-on-hand was understated by \$73,397. However, subsequent to audit notification, KMFC filed amended disclosure reports which materially corrected the misstatements identified by the Audit staff. As such, KMFC has corrected the public record. In response to the Interim Audit Report recommendation, KMFC noted that it has made organizational changes and adopted new internal procedures and safeguards to minimize future administrative issues.

Legal Standard

Contents of Reports.

Each report must disclose:

- The amount of cash-on-hand at the beginning and end of the reporting period;
- The total amount of receipts for the reporting period and for the election cycle;
- The total amount of disbursements for the reporting period and election cycle; and
- Certain transactions that require itemization on Schedule A (Itemized Receipts) or Schedule B (Itemized Disbursements). 52 U.S.C. §30104(b)(1), (2), (3), (4), and (5) (formerly 2 U.S.C. §134(b)(1), (2), (3), (4), and (5)).

Facts and Analysis

A. Facts

During audit fieldwork, the Audit staff reconciled KMFC's reported activity with its bank records for 2011 and 2012. The following chart outlines the discrepancies between KMFC's 2011 disclosure reports and its bank records. Succeeding paragraphs explain why the discrepancies occurred.

2011 Campaign Activity			
	Reported	Bank Records	Discrepancy
Beginning Cash-on-Hand @ January 1, 2011	\$1,200,400	\$1,159,230	\$41,170 Overstated
Receipts	\$2,670,767	\$2,733,174	\$62,407 Understated
Disbursements	\$1,355,561	\$1,320,060	\$35,501 Overstated
Ending Cash-on-Hand @ December 31, 2011	\$2,515,606	\$2,572,344	\$56,738 Understated

The \$41,170 overstatement of beginning cash-on-hand likely resulted from prior-period discrepancies.

The understatement of receipts resulted from the following.

• Contributions from individuals and PACs, not reported	\$ 41,000
• Contributions from individuals disclosed as memo entries	25,000
• Unexplained difference	<u>(3,593)</u>
Net Understatement of Receipts	\$ 62,407

The overstatement of disbursements resulted from the following.

• Operating disbursements over reported (reported twice)	\$ (46,912)
• Disbursements not reported	11,067
• Unexplained difference	<u>344</u>
Net Overstatement of Disbursements	\$ (35,501)

The misstatements described above resulted in the understatement of ending cash-on-hand by \$56,738.

For 2012, KMFC understated its beginning cash-on-hand balance by \$56,738 and its ending cash-on-hand balance by \$73,397. The understatement of its beginning cash-on-hand resulted from the discrepancies noted above during calendar year 2011. The understatement of its ending cash-on-hand primarily resulted from unreported individual and political action committee contributions.

B. Interim Audit Report & Audit Division Recommendation

The Audit staff discussed this matter during the exit conference at the conclusion of fieldwork and provided KMFC representatives with reconciliations for 2011 and 2012 based on disclosure reports filed by KMFC prior to audit notification and amended reports filed subsequently. The Audit staff informed the representatives that the amendment to the audit notification materially corrected the misstatements. As such, the representatives did not make any comments regarding this matter during the exit conference.

The Interim Audit Report recommended that KMFC provide any comments it deemed relevant to this matter.

C. Committee Response to Interim Audit Report

In response to the Interim Audit Report recommendation, KMFC conveyed that, prior to the audit notification, it had begun to undertake “corrective and prophylactic actions.” KMFC engaged a new treasurer and new representatives including an outside Counsel and a new compliance firm. In addition, KMFC stated that it had adopted internal procedures and safeguards to minimize future issues.