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MEMORANDUM

TO: The Commissioners

THROUGH: Patrina M. Clark *Just for PMC*
Staff Director

Margarita Maisonet *MM*
Chief Compliance Officer

FROM: Joseph F. Stoltz *JFS*
Assistant Staff Director
Audit Division

Tom Hintermister *TH*
Audit Manager

AGENDA ITEM
For Meeting of: 04-19-07

SUBMITTED LATE

SUBJECT: Report of the Audit Division on Gephardt for President, Inc. (GFP)

Attached for your approval is the subject report. Also attached is the legal analysis by the Office of General Counsel. The report contains the following recommendations with amounts to be paid to the U.S. Treasury.

• Finding 1	Federal Funds Received in Excess of Entitlement	\$ 378,408
• Finding 2	Receipt of Contributions that Exceed Limits	60,556
• Finding 3	Expenditures that Exceed the Iowa Spending Limit	27,746
• Finding 4	Stale-Dated Checks	12,242
Total Due		<u>\$ 478,952</u>

Regarding Finding 1, the Audit staff notes that the preliminary audit report did not contain a repayment for matching funds in excess of entitlement. This repayment obligation was determined based on GFP's financial activity through December 31, 2006 and was due to the following: 1.) winding down costs that were significantly lower than original estimates; 2.) the

amount payable for excessive contributions was reduced based on information provided by the GFP; and 3.) a reduction in the accounts payable as of the Candidate's date of ineligibility for non-qualified expenses made in excess of the spending limitation.

For Finding 2, the Audit staff notes that as a result of the Commission's decision with other audits, GFP was provided an opportunity to send notifications to contributors whose contributions would have been eligible for "presumptive reattribution" pursuant to 11 C.F.R. §110.1(k)(3)(ii)(B) or to make refunds. GFP demonstrated that notifications were sent for excessive contributors totaling \$114,000 and refunds were made for excessive amounts totaling \$37,000. As a result, the amount due to the U.S. Treasury was reduced to \$60,556.

For Finding 3, the Audit staff notes that the current recommendation to seek a repayment for expenditures in excess of the state expenditure limit is consistent with the Commission's regulation at 11 C.F.R. §9038.2(b)(2)(ii)(A). However, as stated in the legal analysis from the Office of General Counsel, the law may be unsettled in this area. Specifically, in the 1996 election cycle, the Commission found that the Dole for President Committee exceeded the overall and state expenditure limitation. *See* Audit Report on Dole for President, Inc., (Primary). The Audit Division's recommendation to seek a repayment for the Dole Committee exceeding the overall expenditure limitation failed by a 3-3 vote. *Id.* The Commission also considered, but did not seek, a repayment for exceeding the state expenditure limitation. *Id.* The Commission subsequently considered amending 11 C.F.R. §9038.2(b)(2)(ii)(A) to explicitly state whether it would seek repayment for primary expenditures in excess of the state expenditure limitation. *See* Proposed Rules, "Public Funding of Presidential Primary Candidates – Repayments," 65 *Fed. Reg.*, 15,273 (March 22, 2000) and Explanation and Justification, "Repayments Based on Expenditures in Excess of the Expenditure Limitations," 68 *Fed. Reg.*, 47,413 (August 8, 2003). The Commission did not adopt any of the proposed changes because there was no consensus in favor of changing the regulation. *Id.* The regulation, therefore, remains in effect.

It is also noted for Finding 3 that GFP has put forth an alternate calculation for the repayment for expenditures that exceed the Iowa expenditure limitation and their impact on GFP's statement of net outstanding campaign obligations (NOCO). This proposal was not included in the response to the preliminary audit report, but was made during a briefing on changes to the NOCO statement described above. The report currently includes a pro rata repayment for non-qualified Iowa expenditures paid before the point when matching funds were no longer contained in GFP's accounts. In addition, the Audit staff's figure for accounts payable on the NOCO does not include \$128,105 of Iowa allocable expenditures paid after the candidate's date of ineligibility and considered as non-qualified campaign expenses. Section 9034.5(b)(1) of the Commission's regulations specifically states that no amount owed for a non-qualified campaign expense may be included on a NOCO statement as a liability. In past calculations, the last payments made for expenses that are attributable to a spending limitation are assumed to be the ones that exceed the limitation, and if paid after the date of ineligibility, are excluded from the liabilities shown on the NOCO statement. The underlying theory is that post date of ineligibility matching fund entitlement is solely for the payment of remaining debts for qualified campaign expenses and those costs associated with winding down the campaign and not for the payment of non-qualified campaign expenses. The practical effect of this exclusion

depends on the committee's financial position. In the Gephardt case, matching funds were received in excess of the Candidate's entitlement and the exclusion of the post date of ineligibility payments for expenses in excess of the Iowa limitation are part of that calculation.

In meetings with the representatives of GFP, it was discussed whether the pro rata repayment for expenditures exceeding the Iowa limitation in conjunction with the adjustment to accounts payable on the NOCO would be considered a double count. In the past, the Commission has not considered such matters in this manner. If matching funds were used to pay non-qualified campaign expenses a repayment is due. If those same payments were used to justify the receipt of additional matching funds, it is a separate issue and not a double count.

GFP also proposed an alternative calculation whereby **all** expenditures allocated to the Iowa expenditure limit would be considered to be partially non-qualified, beginning with the first and continuing to the last. In all previous cases where a spending limitation was exceeded, the last expenditures that were made were considered to be those that exceeded a spending limitation. The assumption is that the earlier expenditures were within the limitation and that budgets are monitored to avoid accumulating excess expenses applicable to the limitation. If the limitation is exceeded, it occurs later in the campaign rather than from the very beginning.

In this case, the violation percentage (approx. 11%) that would be applied to all expenditures allocated to the Iowa limitation would equal the total amount of expenditures in excess of the Iowa limitation (\$162,943) divided by the total applicable to the Iowa spending limitation (\$1,506,700). This change would not materially affect the repayment amount for expenditures in excess of the Iowa limitation (\$27,746); however, GFP's NOCO would reflect an increase in accounts payable for qualified campaign expenses of \$114,013 and decrease the amount of matching funds in excess of entitlement by the same amount (See Finding 1). The attached report follows long standing Commission practice and the Audit staff recommends that the Commission continue that practice. Should GFP wish to pursue its argument further, it may do so in the Administrative Review process.

Recommendation

The Audit staff recommends that the report be approved.

It is recommended that this report be considered at the open session meeting of April 19, 2007. If you have any questions, please contact Tom Hintermister at extension 1200.

Attachments:

Report of the Audit Division on Gephardt for President, Inc.
Legal Analysis Prepared by the Office of General Counsel



Report of the Audit Division on Gephardt for President, Inc.

January 7, 2003 – April 30, 2004

Why the Audit Was Done

Federal law requires the Commission to audit every political committee established by a Presidential candidate who receives public funds for the primary campaign.¹ The audit determines whether the candidate was entitled to all of the matching funds received, whether the campaign used the matching funds in accordance with the law, whether the candidate is entitled to additional matching funds, and whether the campaign otherwise complied with the limitations, prohibitions, and disclosure requirements of the election law.

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)

Gephardt for President, Inc. is the principal campaign committee for Congressman Richard A. Gephardt, a candidate for the Democratic Party's nomination for the office of President of the United States. The Committee is headquartered in Washington, DC. For more information, see the chart on Campaign Organization, p. 2.

Financial Activity (p. 3)

- **Receipts**
 - Contributions from Individuals \$ 14,205,243
 - Matching Funds Received 4,104,320
 - Transfers from Gephardt in Congress Committee 2,403,521
 - Contributions from Political Committees 548,308
 - Offsets to Operating Expenditures 256,919
 - Interest Received 37,763
 - **Total Receipts** \$ 21,556,074
- **Disbursements**
 - Operating Expenditures \$ 20,805,873
 - Contribution Refunds 50,986
 - **Total Disbursements** \$ 20,856,859

Findings and Recommendations (p. 4)

- Net Outstanding Campaign Obligations (Finding 1)
- Receipt of Contributions that Exceed Limits (Finding 2)
- Expenditures that Exceed Iowa Spending Limit (Finding 3)
- Stale-Dated Checks (Finding 4)

¹ 26 U.S.C. §9038(a).

Report of the Audit Division on Gephardt for President, Inc.

January 7, 2003 – April 30, 2004



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Part I

Background

Authority for Audit

This report is based on an audit of Gephardt for President, Inc. (GFP), undertaken by the Audit Division of the Federal Election Commission (the Commission) as mandated by Section 9038(a) of Title 26 of the United States Code. That section states “After each matching payment period, the Commission shall conduct a thorough examination and audit of the qualified campaign expenses of every candidate and his authorized committees who received [matching] payments under section 9037.” Also, Section 9039(b) of the United States Code and Section 9038.1(a)(2) of the Commission’s Regulations state that the Commission may conduct other examinations and audits from time to time as it deems necessary.

Scope of Audit

This audit examined:

1. The receipt of excessive contributions and loans.
2. The receipt of contributions from prohibited sources.
3. The receipt of transfers from other authorized committees.
4. The disclosure of contributions and transfers received.
5. The disclosure of disbursements, debts and obligations.
6. The recordkeeping process and completeness of records.
7. The consistency between reported figures and bank records.
8. The accuracy of the Statement of Net Outstanding Campaign Obligations.
9. The campaign’s compliance with spending limitations.
10. Other campaign operations necessary to the review.

Inventory of Campaign Records

The Audit staff routinely conducts an inventory of campaign records before it begins the audit fieldwork. GFP records were materially complete and the fieldwork began immediately.

Part II

Overview of Campaign

Campaign Organization

Important Dates	Gephardt for President, Inc.
• Date of Registration	January 7, 2003
• Eligibility Period ²	December 1, 2003 – January 20, 2004
• Audit Coverage	January 7, 2003 – June 30, 2006 ³
Headquarters	Washington, DC
Bank Information	
• Bank Depositories	Seven
• Bank Accounts	Thirteen - Certificates of Deposits Six - Checking Accounts One - Money Market Account
Treasurer	S. Lee Kling (January 7, 2003 – current)
Management Information	
• Attended FEC Campaign Finance Seminar	No
• Used Commonly Available Campaign Management Software Package	Yes
• Who Handled Accounting and Recordkeeping Tasks	Paid staff and campaign consultant

² The period during which the candidate was eligible for matching funds, beginning on the date of certification for eligibility and ending on the date the candidate withdrew from the campaign. See 11 CFR §9033.

³ Limited reviews of receipts and expenditures were performed after April 30, 2004, to determine whether the candidate was eligible to receive additional matching funds.

Overview of Financial Activity (Audited Amounts)

Cash on hand @ January 7, 2003	\$ 0
o Contributions from Individuals	\$ 14,205,243 ⁴
o Matching Funds Received	4,104,320 ⁵
o Transfers from Gephardt in Congress Committee	2,403,521 ⁶
o Contributions from Political Committees	548,308
o Offsets to Expenditures	256,919
o Interest Received	37,763
Total Receipts	\$ 21,556,074
o Operating Expenditures	\$ 20,805,873
o Contribution Refunds	50,986
Total Disbursements	\$ 20,856,859
Cash on hand @ April 30, 2004	\$ 699,215

⁴ Approximately 63,800 contributions from more than 44,000 individuals.

⁵ GFP made 4 matching fund submissions totaling \$4,183,766 and received \$4,104,320 which represents 22% of the maximum entitlement (\$18,655,000).

⁶ This amount represents surplus funds from the Candidate's principal campaign committee for election to the U.S. House of Representatives (Missouri, Third District) following the 2002 general election. The transfer of funds between a candidate's previous Federal campaign committee and his current Federal campaign committee is permissible if certain criteria are met. 11 CFR §§110.3(c)(4) and 116.2(c)(2). The Gephardt in Congress Committee (GCC) met these criteria. GCC reported no outstanding debts and had a cash balance of \$2,442,118 as of December 31, 2002. The surplus funds were transferred to GFP during January and March 2003 and GCC was subsequently approved by the Commission for termination on October 10, 2003.

Part III

Summaries

Findings and Recommendations

Finding 1. Net Outstanding Campaign Obligations

Based on its financial activity through December 31, 2006 and estimated winding down costs, GFP received matching fund payments totaling \$378,408 in excess of the Candidate's entitlement. (For more detail, see p. 6)

Finding 2. Receipt of Contributions that Exceed Limits

A review of contributions from individuals indicated that GFP failed to resolve excessive contributions totaling \$225,792. These contributions were excessive because GFP records did not include documentation to support the reattribution of the excessive portion to another individual. In response to the preliminary audit report, GFP demonstrated one contribution was not excessive and, therefore, a revised projection for excessive contributions totaling \$211,556 was calculated. GFP also demonstrated that notifications were sent to contributors eligible for presumptive reattributions totaling \$114,000 and that refunds were made to contributors for \$37,000 of the excessive amount. As a result, the revised payment payable to the U.S. Treasury is \$60,556 (\$211,556 - \$114,000 - \$37,000). (For more detail, see p. 8)

Finding 3. Expenditures that Exceed Iowa Spending Limit

A review of expenditures indicated that GFP exceeded the Iowa spending limitation by \$162,943. The Audit staff recommended that GFP provide evidence that allocable expenditures did not exceed the Iowa spending limitation. In response to the preliminary audit report, GFP explained the procedural safeguards and circumstances related to complying with the Iowa spending limit, but did not demonstrate that the limitation had not been exceeded. The Audit staff maintains that GFP expenditures exceeded the Iowa spending limit and recommends the Commission make a determination that GFP must make a pro rata repayment of \$27,746 to the U.S. Treasury.

(For more detail, see p. 12)

Finding 4. Stale-Dated Checks

The Audit staff identified stale-dated checks totaling \$12,242 issued by GFP. The Audit staff recommended that GFP provide evidence that these checks are not outstanding or make a payment to the U.S. Treasury for the amount of outstanding checks. In response to the preliminary audit report, GFP accepted the audit staff's calculation of stale-dated checks. Since no payment to the U.S. Treasury for the amount of stale-dated checks has been made, the Audit staff maintains \$12,242 is payable to the U.S. Treasury.

(For more detail, see p. 14)

Summary of Amounts Owed to the U.S. Treasury

• Finding 1	Federal Funds Received in Excess of Entitlement	\$ 378,408
• Finding 2	Receipt of Contributions that Exceed Limits	60,556
• Finding 3	Expenditures that Exceed the Iowa Spending Limit	27,746
• Finding 4	Stale-Dated Checks	12,242
Total Due U.S. Treasury		<hr/> \$ 478,952

Part IV

Findings and Recommendations

Finding 1. Net Outstanding Campaign Obligations

Summary

Based on its financial activity through December 31, 2006 and estimated winding down costs, GFP received matching fund payments totaling \$378,408 in excess of the Candidate's entitlement.

Legal Standard

Net Outstanding Campaign Obligations (NOCO). Within 15 days after the candidate's date of ineligibility (see definition below), the candidate must submit a statement of "net outstanding campaign obligations". This statement must contain, among other things:

- The total of all committee assets including cash on hand, amounts owed to the committee and capital assets listed at their fair market value;
- The total of all outstanding obligations for qualified campaign expenses; and
- An estimate of necessary winding down costs. 11 CFR §9034.5(a).

Value of Capital Assets. The fair market value of capital assets is 60% of the total original cost of the assets when acquired, except that assets that are received after the date of ineligibility must be valued at their fair market value on the date received. A candidate may claim a lower fair market value for a capital asset by listing the asset on the NOCO statement separately and demonstrating, through documentation, the lower fair market value. 11 CFR §9034.5(c)(1).

Date of Ineligibility (DOI). The date of ineligibility is whichever of the following dates occurs first:

- The day on which the candidate ceases to be active in more than one state;
- The 30th day following the second consecutive primary in which the candidate receives less than 10 percent of the popular vote;
- The end of the matching payment period, which is generally the day when the party nominates its candidate for the general election; or
- In the case of a candidate whose party does not make its selection at a national convention, the last day of the last national convention held by a major party in the calendar year. 11 CFR §§9032.6 and 9033.5.

Entitlement to Matching Payments after Date of Ineligibility. If, on the date of ineligibility (see above), a candidate has net outstanding campaign obligations as defined under 11 CFR §9034.5, that candidate may continue to receive matching payments provided that he or she still has net outstanding campaign debts on the day when the matching payments are made. 11 CFR §9034.1(b).

Repayment The Commission-approved audit report may address issues other than those in the preliminary audit report and will contain a repayment determination. 11 CFR §9038.1(b)(1).

Facts and Analysis

The Candidate's date of ineligibility was January 20, 2004. The Audit staff reviewed GFP's financial activity through December 31, 2006, analyzed estimated winding down costs, and prepared the Statement of Net Outstanding Campaign Obligations that appears below:

Gephardt for President, Inc.
Statement of Net Outstanding Campaign Obligations
 As of January 20, 2004
 Prepared on December 31, 2006

Assets

Cash on Hand	\$ 139,203	[a]
Cash in Bank	1,831,420	[b]
Accounts Receivable	223,689	
Capital Assets	21,975	
Other Assets	<u>10,753</u>	

Total Assets \$ 2,227,040

Liabilities

Accounts Payable for Qualified Campaign Expenses at 1/20/04	\$ 1,835,304	
Winding Down Costs:		
Paid Winding Down Costs (1/21/04 – 12/31/06)	\$830,693	
Estimated Winding Down Costs (1/01/07 – 6/30/07)	75,000	[c]
Contribution Refunds	38,160	943,853
Amounts Payable to U.S. Treasury for:		
Unresolved Excessive Contributions (See Finding 2)	\$ 60,556	[d]
Stale-Dated Checks (See Finding 4)	<u>12,242</u>	<u>72,798</u>

Total Liabilities 2,851,955

Net Outstanding Campaign Obligations (Deficit) as of January 20, 2004 (\$624,915)

Footnotes to NOCO Statement:

- [a] Represents contributions dated prior to DOI and deposited after DOI.
- [b] Includes stale-dated checks issued prior to DOI totaling \$10,904.
- [c] Estimate based on average monthly expenses during 2006. In addition, a \$40,000 contingency for legal and accounting costs related to complying with the post-election requirements of the Act has been included.
- [d] This figure equals the amount of unresolved excessive contributions (\$211,556) from the audit less subsequent refunds for excessive contributions totaling \$37,000 and an adjustment totaling \$114,000 for notifications sent to contributors eligible for the presumptive reattribution of the excessive portion of their contribution.

Shown below are adjustments for funds received after January 20, 2004 through April 1, 2004, the date GFP received its last matching fund payment. As indicated, the Candidate received federal matching funds in excess of entitlement.

Net Outstanding Campaign Obligations (Deficit) as of 1/20/04		(624,915)
Private Contributions and Other Receipts Received (1/21/04 - 3/15/04)	30,791	
Matching Funds Received (1/21/04 – 3/14/04)	<u>383,687</u>	<u>414,478</u>
Remaining Entitlement as of 3/15/04		(210,437)
Matching Funds Received (3/15/04 & 4/1/04)		<u>588,845</u>
Total Matching Funds in Excess of Entitlement		<u>\$378,408</u>

The preliminary audit report did not contain a repayment for matching funds received in excess of entitlement. The difference is due primarily to an estimate of winding down costs that was substantially higher than the actual amount spent. The NOCO that appears on the previous page replaces the estimate of winding down costs presented in the preliminary audit report with a much lower total based on actual winding down disbursements through December 31, 2006. Also, a lower estimate for winding down costs was calculated based on an average of actual winding down disbursements over the past year, plus a \$40,000 reserve for legal and accounting expenses. Furthermore, the Audit staff reduced the amount payable for unresolved excessive contributions as a result of GFP's response to the preliminary audit report (Finding 2) and reduced the amount of accounts payable on the NOCO for non-qualified expenditures made in excess of the Iowa spending limit (Finding 3).

Recommendation

The Audit staff recommends that the Commission make a determination that GFP repay \$378,408 to the U.S. Treasury pursuant to 11 CFR §9038.2(b)(1)(i).

Finding 2. Receipt of Contributions that Exceed Limits

Summary

A review of contributions from individuals indicated that GFP failed to resolve excessive contributions totaling \$225,792. These contributions were excessive because GFP records did not include documentation to support the reattribution of the excessive portion to another individual. In response to the preliminary audit report, GFP demonstrated one contribution was not excessive and, therefore, a revised projection for excessive contributions totaling \$211,556 was calculated. GFP also demonstrated that notifications were sent to contributors eligible for presumptive reattributions totaling \$114,000 and that refunds were made to contributors for \$37,000 of the excessive amount. As a result, the revised payment payable to the U.S. Treasury is \$60,556 (\$211,556 - \$114,000 - \$37,000).

Legal Standard

Authorized Committee Limits. An authorized committee may not receive more than a total of \$2,000 per election from any one person. 2 U.S.C. §441a(a)(1)(A) and (f); 11 CFR §§110.1(a) and (b) and 110.9(a).

Handling Contributions That Appear Excessive. If a committee receives a contribution that appears to be excessive, the committee must either:

- Return the questionable check to the donor; or
- Deposit the check into its federal account and:
 - o Keep enough money in the account to cover all potential refunds;
 - o Keep a written record explaining why the contribution may be illegal;
 - o Include this explanation on Schedule A-P if the contribution has to be itemized before its legality is established;
 - o Seek a reattribution of the excessive portion, following the instructions provided in FEC regulations (see below for an explanation of reattribution); and
 - o If the committee does not receive a proper reattribution 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).

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 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).

Reattribution of Excessive Contributions. Commission regulations permit committees to ask donors of excessive contributions 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:

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

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). Within 60 days of receipt of the contribution the committee must inform each contributor:

1. How the contribution was attributed; and

2. The contributor may instead request a refund of the excessive amount. 11 CFR §110.1(k)(3)(B).

Sampling. In conducting an audit of contributions, the Commission uses generally accepted statistical sampling techniques to quantify the dollar value of related audit findings. Apparent violations (sample errors) identified in a sample are used to project the total amount of violations. If a committee demonstrates that any apparent sample errors are not errors, the Commission will make a new projection based on the reduced number of errors in the sample. Within 30 days of service of the final audit report, the committee must submit a check to the United States Treasury for the total amount of any excessive contributions not refunded, reattributed, or redesignated in a timely manner. 11 CFR § 9038.1(f).

Facts and Analysis

A review of contributions from individuals indicated that, at the time of the Preliminary Audit Report, GFP failed to resolve excessive contributions totaling \$225,792.⁸ The contributions identified are excessive for one of the following reasons:

Contribution by check with two names imprinted- Eleven contributions were identified as excessive because they were made by checks imprinted with two names and signed by only one of the individuals. GFP attributed these contributions to both individuals whose names were imprinted on the checks. Such action required that within 60 days of the contribution, GFP either obtain a signed reattribution from the contributors or simply inform the individuals of how the contribution was attributed and offer a refund of the excessive portion. GFP did neither. As a result, the entire amount of the contribution was attributed by the Audit staff to the individual that signed the check.

Contribution by check with one name imprinted- Seven contributions were identified as excessive because they were made by checks imprinted with one name and attributed by GFP to two individuals. GFP records did not include a signature from the second individual acknowledging them as an accountholder. As a result, the entire amount of each contribution was attributed by the Audit staff to the individual who signed the check.

Contribution by credit card- Five contributions were identified as excessive because they were made by credit cards and attributed to more than one individual. The documentation provided in support of these contributions were credit card authorizations that resulted from telemarketing or direct mail solicitations from one individual in amounts exceeding the \$2,000 limit. The excessive portion was reattributed to another individual without obtaining the signature of the second individual acknowledging both the contribution and joint liability for the credit card used to make the contribution.

Although GFP's receipts database indicated that for a few of the excessive contributions a reattribution letter may have been sent to the contributor, no documentation to support these actions was maintained in GFP's records.

⁸ Represents the projected amount of excessive contributions in the sample population (\$218,292) as well as additional excessive contributions (\$7,500) identified by the Audit staff from a separate review.

Subsequent to fieldwork, a schedule of excessive contributors was provided to GFP. In response, GFP stated that contribution refunds were issued to some of the identified contributors in February and March of 2005.⁹

Preliminary Audit Report Recommendation

The Audit staff recommended that GFP provide documentation that the contributions identified as errors were not excessive. Such documentations should have included copies of timely negotiated refund checks or timely signed and dated reattribution letters. Also, for those contributions made by a check with more than one name imprinted, it was recommended that GFP provide timely notifications to the contributors of the presumptive action taken by GFP. Absent such documentation, the Audit staff recommended that GFP make a payment of \$225,792 to the U.S. Treasury.

Committee Response to Preliminary Audit Report & Audit Staff's Assessment

For the eleven excessive contributions that were made by checks with two names imprinted, GFP stated that these contributions represented 62.7% of the excessive amount in the sample and could be presumptively attributed among both spouses and should not be regarded as excessive contributions. According to GFP, the Commission removed the requirement to obtain written authorization prior to attributing contributions between two individuals whose names were imprinted on the check. To demonstrate that five of these contributions were intended to be joint contributions, GFP provided copies of letters sent for matching fund purposes that instructed the individual who did not sign the contribution check to verify the amount of their contribution. These letters were not considered valid reattributions because GFP did not obtain the requisite signatures. Further, these letters were not considered valid notifications of presumptive reattributions by GFP because the letters fail to adequately inform the individuals of how their contribution was attributed and offer a refund of the excessive portion. GFP did not provide any new documentation for the remaining six excessive contributions made by checks with two names imprinted.

For two of the contributions that were made by checks with only one name imprinted, GFP provided copies of letters sent to contributors for matching fund purposes that instructed the individual whose name was not imprinted on the contribution check to verify the amount of their contribution and that the account contained their personal funds. For one of these contributions, GFP provided a copy of a personal statement signed by both contributors which authorized the spouse to write a check to GFP on her behalf. Since it appears that GFP received a timely reattribution of the excessive amount to the spouse, the Audit staff accepted the corrective action taken by GFP for this contribution.¹⁰ The Audit staff maintains that the other contribution made by a check with only one name imprinted is excessive because the requisite signature to validate a reattribution was not obtained.

⁹ The audit notification letter dated May 12, 2004 explained that untimely refunds for impermissible contributions were not recognized by the Commission and payment to the U.S. Treasury may be required for such refunds identified as a result of the audit. Subsequent to the preliminary audit report, the Commission provided GFP the opportunity to make such refunds to identified individuals instead of the U.S. Treasury.

¹⁰ The Audit staff notes that the letter sent to the contributor did not include the offer of a refund in accordance with 11 CFR §110.1(k)(3)(A).

GFP also disputed an excessive contribution that resulted from the same person signing contribution checks from two different accounts; one account in the contributor's name and another from a personal expense account of her spouse. GFP argued that unless the spouse did not have access to his own bank records, it would seem improbable that funds from his account would have been contributed without his consent. The Audit staff maintains this contribution is excessive in accordance with 11 CFR §104.8(c) which states that absent evidence to the contrary, any contribution made by check, money order, or other written instrument shall be reported as a contribution by the last person signing the instrument prior to delivery to the candidate or committee.

For the five excessive contributions that were made by credit cards, GFP questioned whether the sample projection accurately reflected the level of possible excessive contributions made with a credit card. According to GFP, credit card transactions by paper represented only 8.4% of the total amount given to GFP yet they represented 16.9% of the sampling. The generally accepted statistical sampling technique used by the Audit staff to project the violation amount in this finding is based solely on the dollar value, not the transaction count, of contributions and makes no distinction as to the method by which the contribution was made.

In summary, GFP's response to the preliminary audit report resolved one excessive contribution identified in the sample. As a result, the projection for excessive contributions was revised to \$211,556.

Subsequently, as a result of Commission decisions in other audits, GFP was provided an opportunity to send notifications to contributors whose contributions would have been eligible for "presumptive reattribution" pursuant to 11 CFR §110.1(k)(3)(B) (See Legal Standard above), or to make refunds. These actions would obviate the need to make a payment to the U.S. Treasury for such contributions. In response, GFP demonstrated that notifications of presumptive reattribution were sent for excessive contributions totaling \$114,000 and provided evidence of untimely contribution refunds for excessive contributions totaling \$37,000. Therefore, the remaining amount due to the U.S. Treasury is \$60,556 ($\$211,556 - \$114,000 - \$37,000$).

Recommendation

The Audit staff recommends that, within 30 days of service of this report, GFP pay \$60,556 to the U.S. Treasury.

Finding 3. Expenditures that Exceed Iowa Spending Limit

Summary

A review of expenditures indicated that GFP exceeded the Iowa spending limitation by \$162,943. The Audit staff recommended that GFP provide evidence that allocable expenditures did not exceed the Iowa spending limitation. In response to the preliminary audit report, GFP explained the procedural safeguards and circumstances related to complying with the Iowa spending limit, but did not demonstrate that the limitation had not been exceeded. The Audit staff maintains that GFP expenditures exceeded the Iowa

spending limit and recommends the Commission make a determination that GFP must make a pro rata repayment of \$27,746 to the U.S. Treasury.

Legal Standard

State Expenditure Limits. No candidate for the office of President of the United States who is eligible to receive Matching Funds may make expenditures in any one state aggregating in excess of the greater of 16 cents multiplied by the voting age population of the state, or \$200,000 as adjusted by the Consumer Price Index. 2 U.S.C. §441a(b)(1)(A).

State Allocation. An authorized committee shall allocate expenditures to a particular state if the purpose is to influence the nomination of the candidate for the office of President with respect to that state. If the expenditure influences the nomination of that candidate in more than one state, then the committee shall allocate to each state on a reasonable and uniformly applied basis. Allocable expenses include media, mass mailings, overhead, special telephone programs, and polling. 11 CFR §106.2(a)(1) and (b)(1)(2)

Exempt Activity. The candidate may exclude the following expenses from the expenditure limit of a particular state:

- Fundraising exemption 11 CFR §110.8(c)(2)- Up to 50% of the candidate's total expenditures,
- Compliance exemption 11 CFR §106.2(G)(iii)- 10% of overhead expenses, and
- Mass Mailing exemption 11 CFR §110.8(c)(2)- 100% of expenses for mass mailings up to 28 days before the state's primary or caucus.

Repayment. The Commission may determine that a portion of the matching funds received by a Candidate was used for non-qualified campaign expenses. Examples of repayments determinations under this section include a determination that the Candidate has made expenditures in excess of the limitations at 11 CFR §9035. (11 CFR § 9038.2(b)(2))

Facts and Analysis

The Iowa spending limitation for Presidential candidates in the primary election was \$1,343,757. An analysis of GFP expenditures indicated \$1,506,700 should have been applied to the Iowa spending limitation. Therefore, GFP's allocable expenditures exceeded the Iowa spending limitation by \$162,943.

GFP allocation records indicated that \$1,550,250 should have been applied to the Iowa spending limitation. As noted above, the Audit staff calculation is \$1,506,700. The difference of \$43,550 reflects GFP's allocation of certain expenses for advertisement tracking and focus groups that did not require allocation to the Iowa spending limitation.

At the conclusion of fieldwork, GFP was provided a schedule comparing GFP and Audit staff calculations for amounts applicable to the Iowa spending limitation. In response, GFP demonstrated that some amounts originally applied to the Iowa spending limitation were in fact, not allocable. The figures presented above are net of those items.

Preliminary Audit Report Recommendation

The Audit staff recommended that GFP provide evidence that allocable amounts did not exceed the Iowa spending limitation. Absent such evidence, the Audit staff stated that it would recommend that the Commission make a determination that \$31,589 (\$162,943 x repayment ratio of 19.3868%¹¹) was repayable to the U.S. Treasury.

Committee Response to Preliminary Audit Report & Audit Staff's Assessment

GFP stated that it employed numerous and extensive procedures to comply with Iowa spending limitation including the use of a software system and a full-time employee to manage the review and coding of state allocable expenditures. GFP also stated that it used and enforced budgets to ensure compliance with the limit. According to GFP, two circumstances contributed to exceeding the Iowa spending limit. First, the amount of media refunds for broadcast time purchased before the Iowa caucuses were less than expected. Second, GFP stated a significant amount of allocable expenses including special telephone programs were incurred toward the end of the caucuses and only after the election did they realize that those expenses were allocable to the Iowa spending limitation.

Although we acknowledge GFP had procedures in place to comply with the Iowa spending limitation, the Audit staff maintains that GFP exceeded the Iowa spending limitation. Therefore, in accordance with 11 CFR §9038.2(b)(2), the Audit staff calculated a repayment of \$27,746 (\$154,787 x repayment ratio of 17.9250%) for non-qualified expenses paid before the point when matching funds, to which the Candidate was entitled, were no longer contained in GFP accounts.¹²

Recommendation

The Audit staff recommends that the Commission make a determination that GFP repay \$27,746 (\$154,787 x repayment ratio of 17.9250%) to the U.S. Treasury.

Finding 4. Stale-Dated Checks

Summary

The Audit staff identified stale-dated checks totaling \$12,242 issued by GFP. The Audit staff recommended that GFP provide evidence that these checks are not outstanding or make a payment to the U.S. Treasury for the amount of outstanding checks. In response to the preliminary audit report, GFP accepted the Audit staff's calculation of stale-dated checks. Since no payment to the U.S. Treasury for the amount of stale-dated checks has been made, the Audit staff maintains \$12,242 is payable to the U.S. Treasury.

¹¹ This figure (19.3868%) represents GFP's repayment ratio as calculated pursuant to 11 CFR §9038.2(b)(2)(iii). Subsequent to the preliminary report, the repayment ratio was adjusted to (17.9250%) to account for matching funds determined to be in excess of entitlement totaling \$378,408.

¹² Expenses totaling \$8,156 (\$162,943 - \$154,787) were paid after the Candidate's accounts had been purged of all matching funds. As a result, these expenses are not subject to any repayment.

Legal Standard

Handling Stale-Dated (Uncashed) Checks. If a committee has issued checks that the payees (creditors or contributors) have not cashed, the committee must notify the Commission of its efforts to locate the payees and encourage them to cash the outstanding checks. The committee must also submit a check payable to the U. S. Treasury for the total amount of the outstanding checks. 11 CFR §9038.6.

Facts and Analysis

The Audit staff's reconciliation of GFP disbursements to bank activity through March 31, 2005 identified stale-dated checks totaling \$12,242 issued by GFP. These checks were issued between April 15, 2003 and June 15, 2004 and are comprised mostly of contribution refunds. At the conclusion of fieldwork, GFP was provided a schedule of stale-dated checks.

Preliminary Audit Report Recommendation & Committee Response

The Audit staff recommended that GFP provide evidence that the checks were no longer outstanding by demonstrating the checks or replacement checks had cleared the bank or that the obligations did not exist and the checks were voided. Absent such evidence, it was stated that the Audit staff would recommend that \$12,242 be paid to the U.S. Treasury and the amount should be disclosed on Schedule D-P (Debts and Obligations) until paid.

In response to the preliminary audit report, GFP stated that it accepted the finding on stale-dated checks and would disclose the appropriate amount as a debt on Schedule D-P. However, no payment to the U.S. Treasury has been made nor has GFP disclosed the amount as a debt on Schedule D-P. The Audit staff maintains \$12,242 be paid to the U.S. Treasury.

Recommendation

The Audit staff recommends that GFP pay \$12,242 to the U.S. Treasury.



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

MEMORANDUM

January 26, 2007

TO: Joseph F. Stoltz
Assistant Staff Director
Audit Division

THROUGH: Patrina M. Clark *MC*
Staff Director

FROM: James A. Kahl *JK*
Deputy General Counsel

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Associate General Counsel

Lorenzo Holloway *LH*
Assistant General Counsel
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SUBJECT: Report of the Audit Division on Gephardt for President, Inc. (LRA# 637)

I. INTRODUCTION

The Office of General Counsel reviewed the Report of the Audit Division ("Proposed Report") on Gephardt for President, Inc. ("Committee") that you submitted to this Office. This memorandum discusses our comments on the Proposed Report.¹ We generally concur with the findings not discussed in this memorandum. In this memorandum, we address three findings in the Proposed Report: Finding 1 ("Net Outstanding Campaign Obligations"); Finding 2 ("Receipt of Contributions that Exceed Limits"); and Finding 3 ("Expenditures that Exceed Iowa Spending Limit"). We summarize our comments below and provide further detail under each topic heading.

¹ The Commission is required to consider the audit report in an open session agenda document, and is required to provide the candidate and the committee with copies of the agenda document (which includes the Proposed Report, the Committee's response, and this Office's comments) twenty-four hours prior to releasing the agenda document to the public. 11 C.F.R. § 9038.1(e)(1).

The first finding in the Proposed Report addresses the Committee's Statement of Net Outstanding Campaign Obligations ("NOCO"), and within that finding the auditors recommend that the Committee repay \$284,729 to the United States Treasury because the candidate received public funds in excess of his entitlement. The Preliminary Audit Report ("PAR") did not recommend a repayment for receiving public funds in excess of entitlement. The PAR only included a repayment of \$31,589 because the Committee incurred expenses in excess of the state expenditure limitation. Given this change from the PAR to the Proposed Report, our comments discuss the legal implications of a repayment increase from the PAR to the Audit Report.

In the second finding, the auditors conclude that the Committee received excessive contributions, and recommend that the Committee pay the excessive amount to the United States Treasury. The Committee contends that a payment to the Treasury is not warranted because: 1) the contributions were not excessive because they were properly attributed or reattributed and supported with documentation and/or notices to the contributors and 2) the Audit Division used a flawed sampling technique because it did not accurately reflect the level of possible excessive contributions made by credit cards. We concur with the Audit Division that the Committee did not properly support its attributions and reattributions with required documentation and/or notices to contributors and thus do not further analyze the issue below. We also concur with and comment on the auditors' conclusion that the Committee failed to show the sample projection used to determine the excessive contributions was flawed.

Finally, we concur with the auditors' conclusion in the third finding that the Committee exceeded the state expenditure limitation by \$162,943, but we address whether a repayment is warranted for exceeding the state expenditure limitation given that the Commission did not seek a repayment for exceeding the state expenditure limitation in a prior audit and the Commission addressed whether to seek a repayment in this instance in a proposed rulemaking.

II. NET OUTSTANDING CAMPAIGN OBLIGATIONS (Finding 1)

The Audit Division found that the Committee received public fund payments in excess of the Candidate's entitlement. The PAR, however, did not include a repayment for matching funds in excess of entitlement. The auditors based its PAR finding on its analysis of the Committee's financial activity and estimated winding down expenses as calculated in the NOCO through March 31, 2005. The Proposed Report adjusted the NOCO figures for financial activity through June 30, 2006. The auditors conclude the Committee has a repayment obligation because: 1) its winding down costs were significantly lower than the original estimates; 2) the amount payable for excessive contributions was reduced based on information provided by the Committee; and, 3) the auditors reduced the accounts payable for non-qualified expenses made in excess of the state expenditure limitation. The bottom-line result of these adjustments is that the Candidate has a \$284,729 increase in his repayment obligation that was not included in the PAR.

We raise the issue of whether the Commission can increase the candidate's repayment obligation from the PAR to the audit report because the Commission must notify the candidate of a repayment obligation as soon as possible. 11 C.F.R. § 9038.2(a)(2). In fact, repayment calculations are included in a preliminary audit report to give candidates "the earliest possible opportunity to respond to the Commission's thinking with respect to its future repayment determination." Explanation and Justification for 11 C.F.R. § 9038.1(c), 48 *Fed. Reg.*, 5,232 (Feb. 4, 1983). Giving candidates the earliest possible notice of a repayment is important because candidates are required to give repayments preference over all other outstanding committee obligations other than federal taxes. 11 C.F.R. § 9038.2(a)(3).

We conclude that the law allows the Commission to increase the repayment from the PAR to the Audit Report. First, the preliminary audit report gives the candidate an early opportunity to respond to the Commission's future repayment determination, but it is not the final word with respect to a candidate's repayment obligation because it does not constitute legal notice of a repayment obligation. *Simon v. FEC*, 53 F.3d 356 (D.C. Cir. 1995) (Court determined that the interim audit report² is a "progress report of a continuing audit," including only preliminary repayment calculations, and thus cannot constitute notice of a repayment obligation under 26 U.S.C. § 9038). The Commission audit report issued pursuant to 11 C.F.R. § 9038.1(d) constitutes notice of the repayment obligation. 11 C.F.R. § 9038.2(a)(2). The Committee, therefore, should anticipate the Commission might increase the repayment obligation from the preliminary audit report to the audit report. *See* 11 C.F.R. § 9038.1(d) (Audit report may contain issues other than those included in preliminary audit report).

Second, the Committee is not deprived of due process by the change from the PAR because it will have an opportunity to argue against the basis for the increased repayment. The Commission's notice of a repayment obligation is presented in the audit report issued pursuant to 11 C.F.R. § 9038.2(d). When the Commission provides the Committee with written notice of its repayment determination in the audit report, the Committee will have ample opportunity during the administrative review process to dispute the Commission's repayment determination if it disagrees with the Commission's calculations. 11 C.F.R. § 9038.2(d)(1) and (2). Specifically, the Committee will have 60 days after service of the audit report to respond to the Commission's repayment determination in writing and the Committee may request an oral hearing to dispute the repayment. 11 C.F.R. §§ 9038.2(c)(2)(i) and (ii).

² The Commission issued "interim" rather than "preliminary" audit reports during the time period when *Simon v. FEC* was decided, but there is no legal distinction between an interim audit report and a preliminary audit report for purposes of our analysis.

III. RECEIPT OF CONTRIBUTIONS THAT EXCEED LIMITS (Finding 2)

In addition to the finding that the Committee received funds in excess of its entitlement, the auditors found that the Committee received contributions in excess of the contribution limits. In the Committee's response to the PAR, the Committee questioned whether the statistical sampling technique the auditors used to project excessive contributions made with a credit card was flawed. The Committee asserted that the projection was inaccurate because the credit card transactions authorized by a transaction slip or other writing signed by the cardholder represented 8.4% of the total amount of contributions given to the Committee, but the transactions were disproportionately represented in the sample at 16.9%.

The auditors reject the Committee's contention. According to the auditors, the sampling technique makes no distinction as to the method by which a contribution is made; it is based solely on the dollar value of the contribution. The auditors also indicate that the contributor database provided by the Committee and used in the sample did not distinguish between types of contributions. Moreover, the auditors also informed this Office that they have no basis to evaluate the Committee's challenge to the sampling projection because the Committee did not provide work papers showing how it calculated the 8.4% and 16.9% figures. As a result of the auditors rejecting the Committee's statement, the Proposed Report finds that the Committee received \$173,396 in excessive contributions.

We concur with this finding. The Commission may utilize generally accepted statistical sampling techniques to quantify, in whole or in part, the dollar value of related audit findings. 11 C.F.R. § 9038.1(f)(1). A projection of the total amount of violations based on apparent violations identified in such a sample may become the basis, in whole or in part, of any audit finding. *Id.* A committee, in responding to a sample-based finding concerning excessive or prohibited contributions, shall respond only to the specific sample items used to make the projection. 11 C.F.R. § 9038.1(f)(2). According to the auditors, the type of contribution is not a specific item in the sample because the sampling technique made no distinction based on the method of making the contribution. Consequently, the Committee has failed to show that there were apparent errors among the sample items. *Id.*

IV. EXPENDITURES THAT EXCEED IOWA SPENDING LIMIT (Finding 4)

In Finding 4, the Audit Division concludes that the Presidential Committee exceeded the state expenditure limitation by \$162,943. Accordingly, the Audit Division recommends that the Presidential Committee make a pro rata repayment of \$31,589 ($\$162,943 \times$ repayment ratio of 19.3868%) to the United States Treasury.

The Audit Division's recommendation is consistent with the Commission's regulation at 11 C.F.R. § 9038.2(b)(2)(ii)(A) because this regulation allows the Commission to seek a repayment when a committee exceeds the state expenditure

limitation, but the law may be unsettled in this area. Specifically, in the 1996 election cycle, the Commission found that the Dole for President Committee exceeded the overall and state expenditure limitations. *See* Audit Report on Dole for President, Inc., (Primary). The Audit Division's recommendation to seek a repayment for the Dole Committee exceeding the overall expenditure limitation failed by a 3-3 vote. *Id.* The Commission also considered, but did not seek, a repayment for exceeding the state expenditure limitation. *Id.* The Commission subsequently considered amending 11 C.F.R. § 9038.2(b)(2)(ii)(A) to explicitly state whether it would seek repayment for primary expenditures in excess of the state expenditure limitation. *See* Proposed Rules, "Public Funding of Presidential Primary Candidates – Repayments," 65 *Fed. Reg.*, 15,273 (March 22, 2000) and Explanation and Justification, "Repayments Based on Expenditures in Excess of the Expenditure Limitations," 68 *Fed. Reg.*, 47,413 (August 8, 2003). The Commission did not adopt any of the proposed changes because there was no consensus in favor of changing the regulation. *Id.* The regulation, therefore, remains in effect. Consequently, we concur with the Audit Division's recommendation to seek a repayment. Given the Commission's prior deliberations on this issue, however, we recommend that the Audit Division raise this issue in the cover memorandum that forwards the Proposed Report to the Commission.

If the Commission decides that a repayment is warranted for exceeding the state expenditure limitation, then the Commission should consider the Committee's explanation of the procedural safeguards it employed to comply with the limitation. The Committee presents mitigating circumstances rather than arguing that it did not exceed the state expenditure limit or that it was not required to comply with the expenditure limit. Neither the statute nor the regulations, however, allow for a waiver or adjustments of a committee's pro rata repayment obligation for exceeding a state expenditure based on mitigating factors. 2 U.S.C. § 441a(b)(1)(A) and 11 C.F.R. § 9038.2(b)(2). We, therefore, concur with the Audit Division's finding that the Committee exceeded the expenditure limitation. We also concur with the Audit Division's recommendation that the Committee must repay the United States Treasury.

CASE INDEX FORM

CASE NO. & NAME: Gephardt for President

STAFF ASSIGNED: Tom Hintermister, Audit Manager

TELEPHONE: Audit - 202-694-1200

<u>DATE</u>	<u>DOCUMENT</u>
September 30, 2005	Doc 1- Legal Analysis on Preliminary Audit Report
December 13, 2005	Doc 2- Preliminary Audit Report
March 16, 2006	Doc 3- Response to Preliminary Audit Report (Narrative Only)
January 17, 2007	Doc 4- Supplemental Letter for Excessive Contributions
September 11, 2006	Doc 5- Legal Analysis on Audit Report
March 16, 2006	Doc 6- Response to Supplemental Letter for Excessive Contributions (Narrative Only)
April 12, 2007	Doc 7- Audit Report

For more information or to request any of the documents listed above, contact Tom Hintermister at 694-1200.