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OFFICE OF GENERAL
COUNSEL

July 15, 2009

MEMORANDUM

To: Thomasenia P. Duncan
General Counsel

Through: Robert A. Hickey *[Signature]*
Staff Director

From: John D. Gibson *[Signature]*
Chief Compliance Officer

Joseph F. Stoltz *[Signature]*
Assistant Staff Director
Audit Division

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Audit Manager

By: Pamela Wilkerson *[Signature]*
Lead Auditor

Subject: Charlie Stuart for Congress (A07-09) -
Referral Matters

On June 18, 2009 the Commission approved the final audit report on the (Charlie Stuart for Congress). The final audit report includes the following matters that are referable:

Receipt of Contributions from LLCs and Corporations (Finding 1)
Receipt of Contributions that Exceed Limits (Finding 2)

All work papers and related documentation are available for review in the Audit Division. Should you have any questions regarding this matter, please contact Pamela Wilkerson or Thomas Nurthen at 694-1200.

Attachments: Finding 1- Receipt of Contributions from LLCs and Corporations
Finding 2- Receipt of Contributions that Exceed Limits

cc: Lorenzo Holloway

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Failure to Respond to the Interim Audit Report

The interim audit report was issued on March 20, 2009, advising SFC of the findings and recommendations resulting from the audit. SFC was to respond to the findings contained in the interim audit report on or before April 22, 2009. Upon request, SFC was twice granted extensions to respond to the interim audit report. The final due date to respond was May 18, 2009. To date, no response has been received and attempts to contact SFC representatives have failed.

Finding 1. Receipt of Contributions from LLCs and Corporations

Summary

SFC received 65 apparent prohibited contributions, totaling \$35,950. Seventeen contributions (\$15,650) were from limited liability companies (LLCs) and 48 contributions (\$20,300) were from apparent corporate entities. The Audit staff recommended that SFC provide evidence that the contributions were not from prohibited sources. Absent that the prohibited amounts should have been either refunded to the contributor or disgorged to the U.S. Treasury.

Legal Standard

A. Receipt of Prohibited Corporate Contributions. Political campaigns may not accept contributions made from the general treasury funds of corporations. This prohibition applies to any type of corporation including a non-stock corporation, an incorporated membership organization, and an incorporated cooperative. 2 U.S.C. §441b.

B. Definition of Limited Liability Company. A limited liability company (LLC) is a business entity recognized as an LLC under the laws of the state in which it was established. 11 CFR §110.1(g)(1).

C. Application of Limits and Prohibitions to LLC Contributions. A contribution from an LLC is subject to contribution limits and prohibitions, depending on several factors, as explained below.

- **LLC as Partnership.** The contribution is considered a contribution from a partnership if the LLC chooses to be treated as a partnership under Internal Revenue Service (IRS) tax rules, or if it makes no choice at all about its tax status. A contribution by a partnership is attributed to each partner in direct proportion to his or her share of the partnership profits. 11 CFR §§110.1(e)(1) and (g)(2).
- **LLC as Corporation.** The contribution is considered a corporate contribution—and is barred under the Act—if the LLC chooses to be treated as a corporation under IRS rules, or if its shares are traded publicly. 11 CFR §110.1(g)(3).

- **LLC with Single Member.** The contribution is considered a contribution from a single individual if the LLC is a single-member LLC that has not chosen to be treated as a corporation under IRS rules. 11 CFR §110.1(g)(4).

D. Limited Liability Company's Responsibility to Notify Recipient Committee. At the time it makes a contribution, an LLC must notify the recipient committee:

- That it is eligible to make the contribution; and
- In the case of an LLC that considers itself a partnership (for tax purposes), how the contribution should be attributed among the LLC's members. 11 CFR §110.1(g)(5).

E. Questionable Contributions. If a committee receives a contribution that appears to be prohibited (a questionable contribution), it must follow the procedures below:

1. Within 10 days after the treasurer receives the questionable contribution, the committee must either:
 - Return the contribution to the contributor without depositing it; or
 - Deposit the contribution (and follow the steps below). 11 CFR §103.3(b)(1).
2. If the committee deposits the questionable contribution, it may not spend the funds and must be prepared to refund them. It must therefore maintain sufficient funds to make the refunds or establish a separate account in a campaign depository for possibly illegal contributions. 11 CFR §103.3(b)(4).
3. The committee must keep a written record explaining why the contribution may be prohibited and must include this information when reporting the receipt of the contribution. 11 CFR §103.3(b)(5).
4. Within 30 days of the treasurer's receipt of the questionable contribution, the committee must make at least one written or oral request for evidence that the contribution is legal. Evidence of legality includes, for example, a written statement from the contributor explaining why the contribution is legal or an oral explanation that is recorded by the committee in a memorandum. 11 CFR §103.3(b)(1).
5. Within these 30 days, the committee must either:
 - Confirm the legality of the contribution; or
 - Refund the contribution to the contributor and note the refund on the report covering the period in which the refund was made. 11 CFR §103.3(b)(1).

F. Refund or Disgorge Questionable Contributions. If the identity of the original contributor is known, the committee must either refund the funds to the source of the original contribution or pay the funds to the U.S. Treasury. AO 1996-5.

Facts and Analysis

Our review of contributions identified 65 apparent prohibited contributions, totaling \$35,950. Seventeen contributions, totaling \$15,650, were from LLCs and 48 contributions, totaling \$20,300, were from apparent corporate entities. SFC's records lacked the necessary documentation to determine whether these entities filed taxes as partnerships or corporations. With respect to the contributions from apparent corporate entities, the Audit staff contacted the appropriate Secretary of State's office and

confirmed that each entity was incorporated at the time the contributions were made to SFC.

This matter was discussed at the exit conference. An SFC representative inquired about the relevant regulations and agreed to review the contributions in question.

Interim Audit Report Recommendation

The Audit staff recommended that SFC provide evidence that demonstrates that the contributions were not from prohibited sources.

For contributions from LLCs, such evidence should have included documentation from each entity that demonstrated it elected under Internal Revenue Service tax rules not to be treated as a corporation. For contributions from apparent corporate entities, such evidence should have included documentation that demonstrated the entities were not corporations at the time the contribution was made.

Absent such evidence, it was recommended that SFC refund \$35,950 to the contributors and provide copies (front and back) of all negotiated refund checks; or disgorge this amount to the U.S. Treasury.

If funds were not available to make the necessary refunds, SFC should have disclosed the entities requiring refunds on Schedule D (Debts and Obligations) until funds became available to make such refunds.

Finding 2. Receipt of Contributions that Exceed Limits

Summary

Our review identified contributions from eight individuals, totaling \$13,000, which exceeded the limitation. Two excessive contributions, totaling \$2,300, could be cured by sending presumptive redesignation/retribution notifications. The remaining excessive contributions (\$10,700) can only be cured by refund or disgorgement to the U.S. Treasury. The Audit staff recommended that SFC provide evidence demonstrating that the contributions were not excessive or send the notices to the contributors that were eligible for presumptive redesignation/retribution. Absent those actions, the excessive amounts should have been refunded to the contributor or disgorged to the U.S. Treasury.

Legal Standard

A. Authorized Committee Limits. An authorized committee may not receive more than a total of \$2,100 per election from any one person. 2 U.S.C. §441a(a)(1)(A) and (f); 11 CFR §110.1(a) and (b), §110.9(a) and §110.17(b).

B. 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 if the contribution has to be itemized before its legality is established;
- o Seek a reattribution or a redesignation of the excessive portion, following the instructions provided in FEC regulations (see below for explanations of reattribution and redesignation); and
- o 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 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:

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).

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:

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).

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

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the excess portion of the contribution for use in another election. The committee must inform the contributor that:

1. The redesignation must be signed by the contributor;
2. The redesignation 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(b)(5).

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:

1. Is made before that candidate's primary election;
2. Is not designated in writing for a particular election;
3. Would be excessive if treated as a primary election contribution; and
4. As redesignated, does not cause the contributor to exceed any other contribution limit. 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.

F. Contributions to Retire Debts. If an authorized candidate committee has net debts outstanding after an election is over, a campaign may accept contributions after the election to retire the debts provided that:

- The contribution is designated for that election (since an undesignated contribution made after an election counts toward the limit for the candidate's upcoming election);
- The contribution does not exceed the contributor's limit for the designated election; and,
- The campaign has net debts outstanding for the designated election on the day it receives the contribution. 11 CFR §110.1(b)(3)(i) and (iii).

G. Refund or Disgorge Questionable Contributions. If the identity of the original contributor is known, the committee must either refund the funds to the source of the original contribution or pay the funds to the U.S. Treasury. AO 1996-5.

Facts and Analysis

Our review identified contributions from eight individuals, totaling \$13,000, which exceeded the limitation. Of this amount, excessive contributions totaling \$11,100 were made to the general election and \$1,900 was made to the primary election.

The primary election excessive contribution (\$1,900) can be cured by sending the contributor a presumptive redesignation notification. Only \$400 of the general election

excessive contributions can be cured by sending the contributor a presumptive reattribution notification.

The remaining excessive contributions (\$10,700) must be refunded to the contributor or disgorged to the U.S. Treasury. These contributions were received after the election for which they are designated. However, at the time of receipt there were no debts related to the relevant election. Based on the contribution records, none were eligible for reattribution to another contributor. As a result, excessive contributions, totaling \$10,700, should be refunded to the contributors or disgorged to the U.S. Treasury.

This matter was discussed at the exit conference. An SFC representative was provided a schedule of the excessive contributions, who agreed to review this matter.

Interim Audit Report Recommendation

The Audit staff recommended that SFC provide evidence that the contributions were not excessive. Such evidence should include, but not be limited to, documentation that the contributions were reattributed or redesignated in a timely manner or that the excessive contributions were timely refunded.

Absent such evidence, SFC should have sent notices to the contributors whose contributions were eligible for presumptive redesignation/retribution (\$2,300) to inform them how the contributions were attributed and offering each contributor an option of receiving a refund. SFC should have provided a copy of the notices and evidence that they were sent. Absent a request for a refund by the contributors, the notices obviate the need for a refund or payment to the U.S. Treasury; and,

For the remaining excessive contributions (\$10,700), SFC should have refunded the excessive portions to the contributors or pay that amount to the U.S. Treasury and provided evidence of the refunds or payment to the U.S. Treasury (copies of the front and back of negotiated check(s)).

If funds were not available to make the necessary refunds, SFC should have disclose the contributions requiring refund as debts owed on Schedule D until funds become available to make such refunds.