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FEDERAL ELECTION COMMISSION  
WASHINGTON, D.C. 20463

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## AGENDA ITEM

For Meeting of 07-01-10

June 30, 2010

### MEMORANDUM

**SUBMITTED LATE**

TO: The Commission

FROM: Commissioner Donald F. McGahn *DFM*

Subject: New Procedures for the Audit Process and for Legal Guidance

Attached is a proposal for new procedures for the audit process and for legal guidance. I have asked that this be made public in advance of the July 1 meeting of the Commission.

Attachment



## **New Procedures for the Audit Process and for Legal Guidance**

The Commission is adopting new procedures to enhance the transparency and efficiency of the Commission's reports analysis and audit functions. The procedures set forth in this document establish certain mechanisms to provide for Commission deliberation at earlier stages of the reports analysis and audit processes to ensure fairness and due process for persons and entities subject to the Commission's jurisdiction and to promote transparency, efficiency, and voluntary compliance with the law.

### **I. The Audit Process**

The Federal Election Campaign Act of 1971, as amended, 2 U.S.C. § 431 *et seq.*, ("the Act") provides that the Commission "may conduct audits and field investigations of any political committee required to file a report under section 434" of the Act ("Title 2 matters").<sup>1</sup> Prior to conducting such audit the Commission is required to "perform an internal review of reports filed by the committee that may be audited, to determine if the committee's reports meet the threshold requirements for substantial compliance" with the Act. The review is conducted by the Commission's Reports Analysis Division, and compliance thresholds are established by the Commission for each election cycle. Under the Presidential Election Campaign Fund Act, 26 U.S.C. § 9001 *et seq.*, the Commission is also required to conduct an audit of the qualified campaign expenses of the candidates of each political party for President and Vice President who receive public funds, as well as an audit of receipts and disbursements by presidential nominating conventions and host committees ("Title 26 matters").<sup>2</sup>

#### **A. Interim Audit Reports**

Once the Audit Division completes its fieldwork on an audit, it conducts an exit conference with representatives of the audited committee. During the exit conference, preliminary findings and recommendations are presented to the committee being audited. Based on the fieldwork and the committee's response to discussions with the Audit Division at, or following, the exit conference, the Audit Division prepares an Interim

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<sup>1</sup> 2 U.S.C. § 438(b). The Commission also has the statutory authority to conduct an audit in instances which, based on a complaint, the Commission determines by an affirmative vote of 4 of its members, that it has reason to believe that a person has committed, or is about to commit, a violation" of the Act (including chapter 95 or 96 of Title 26 of the United States Code). 2 U.S.C. § 437g.

<sup>2</sup> 26 U.S.C. §§ 9007, 9008; 11 C.F.R. Parts 9007 and 9008.

Audit Report (“IAR”) in Title 2 matters, or a Preliminary Audit Report (“PAR”) in Title 26 matters.<sup>3</sup>

All Title 26 PARs are circulated to the Commission for a vote.<sup>4</sup> For Title 2 IARs, only IARs that present complex, novel, or unsettled questions of law, as well as all audits of state party committees, are circulated to the Commission for vote on a 72-hour no-objection ballot.<sup>5</sup> The committee being audited is not provided a copy of the IAR or PAR prior to Commission consideration. Approval of an audit report at the interim or preliminary stage does not commit the Commission or individual Commissioners to that or any other position at a later stage of the audit process.<sup>6</sup>

To facilitate more thorough Commission consideration of IARs and PARs, the Commission is hereafter requiring that the circulation of all IARs and PARs to the Commission will be accompanied by notice of: (1) all prior Commission audits known to the Audit Division raising the same or substantially similar material issues to those raised in the IAR or PAR, and (2) any prior audit of the same entity. The notice of prior audits shall provide the date of the prior audit and a summary of the Commission’s findings and conclusions.

Once an IAR or PAR has completed the process described above, a copy of the report is provided to the committee being audited and the committee is provided with an opportunity to respond in writing to the report. For Title 2 IARs, committees are provided with 30 days to respond; for Title 26 PARs, committees are provided with 60 days to respond.

#### B. Draft Final Audit Report & Commission Consideration of Recommendations of the Audit Division As Set Forth in the Draft Final Audit Report

Under current procedures, once the committee being audited has been given an opportunity to respond in writing to the IAR or PAR, the Audit Division prepares a Draft Final Audit Report (“DFAR”) setting forth the Audit Division’s proposed findings after the Division’s evaluation of the committee’s response to the recommendations in the IAR or PAR and any new information presented by the committee. The DFAR (and any analysis of it provided by the Office of General Counsel) is then sent to the committee being audited. Within 15 days of receiving the DFAR, the committee may respond directly to the Commission with respect to any legal or factual issues raised by the Audit

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<sup>3</sup> However, in the case of a Title 2 audit in which the Audit Division concludes that there are no material findings, no IAR is prepared and the Audit Division proceeds directly to the final stage of the audit process.

<sup>4</sup> 11 C.F.R. § 9007.1(c)(1).

<sup>5</sup> See Attachment 1 (Voting Procedures for Title 2 Audit Reports, Certification dated Dec. 17, 2009). IARs with proposed findings that do *not* present complex, novel, or unsettled questions of law are provided to the Commission on an informational basis at the time that they are sent to the committee being audited. *Id.*

<sup>6</sup> *Id.*

Division in the DFAR, by written response, may request participation in an audit hearing,<sup>7</sup> or both.<sup>8</sup>

## 1. Content and Format of the Draft Final Audit Report

To facilitate efficient Commission consideration of the proposed findings set forth by the Audit Division in the DFAR, each proposed finding to the extent possible shall be broken down into separate and severable sub-findings that can be considered by the Commission individually. Each proposed finding shall address one and only one provision of the Act or implementing regulation that is implicated. Each application of that point of law to a distinct factual situation (such as a contribution or disbursement, event, or category of activity) to the extent possible shall be a separate sub-finding.<sup>9</sup>

## 2. Report Processing

The Commission is establishing a new report processing procedure for Commission consideration of audit reports at the post-DFAR stage of the process. The Audit Division shall make its recommendations to the Commission within 30 days of any of the following events (whichever occurs later):

- (a) the Commission's receipt of an audited committee's response to a DFAR;
- (b) an audit hearing;
- (c) the end of any period the Commission provides for the submission of materials after an audit hearing; or
- (d) the audited committee's written confirmation that it declines to respond to the DFAR and does not seek a hearing.

The Audit Division shall, in consultation with the Office of General Counsel, prepare a brief cover memorandum ("Audit Division Recommendation Memorandum") presenting the Audit Division's recommendations to the Commission regarding any new legal issues or significant factual issues that were raised after the DFAR was prepared and served on the audited committee, or advising that there are none. In the event that

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<sup>7</sup> For Title 26 repayment issues, the Commission's regulations provide for a separate hearing process. See 11 C.F.R. §§ 9007.2(c)(2)(i), 3038.(c)(2)(i).

<sup>8</sup> See Procedural Rules for Audit Hearings, 74 Fed. Reg. 33140 (Jul. 10, 2009). Although this procedure provides an opportunity for the audited committee to address the Commission directly, the Office of General Counsel and the Audit Division are provided copies of any written response to the DFAR, and are represented at any audit hearing conducted by the Commission. However, the current policy does not provide a formal mechanism for the Commission to receive feedback from the Audit Division regarding its proposed findings following the audited committee's response to the DFAR or an audit hearing. As a result, the Commission is deprived of the benefit of the Audit Division's input regarding any information provided by the audited committee.

<sup>9</sup> For example, a proposed finding may raise the issue of whether a state party committee properly treated three payments (for polls, phone banks, and advertising) as allocable, or whether those disbursements were for non-allocable federal election activity: in that case, each type of payment (for polls, phone banks, and advertising) would be a separate sub-finding under the proposed finding addressing allocable versus non-allocable federal election activity. The finding would set forth the applicable legal standard, which would be applied to the facts in each sub-finding. See [Template Draft Form, to be finalized].

the Audit Division identifies any new legal issues or significant factual issues that were not addressed in the DFAR, the Audit Division Recommendation Memorandum shall identify such factual or legal issues, and make recommendations regarding the impact of such on the proposed findings in the DFAR. The Audit Division Recommendation Memorandum will be circulated to the Commission as a cover memorandum to the DFAR.<sup>10</sup>

The DFAR and Audit Division Recommendation Memorandum will be circulated to the Commission for a tally vote. If the recommendations of the Audit Division are approved by the Commission on a tally vote, the Audit Division shall proceed to the Final Audit Report stage. If the recommendations of the Audit Division are not approved in their entirety, the matter shall be automatically placed on the next open meeting agenda, and the Audit Division Recommendation Memorandum and DFAR shall then be made public as agenda documents. The committee will be provided a copy of the Audit Division Recommendation Memorandum at least 72 hours prior to it becoming a public document. At the open meeting, the Commission will consider the issues and take appropriate action on the findings.<sup>11</sup>

### C. Final Audit Report

Under current policy, all final audit reports issued by the Commission shall reflect both (1) the conclusions of the Commission, and (2) the legal standards enunciated by the Commission and applied to the particular circumstances presented by the audit.<sup>12</sup>

Within 30 days of the Commission's vote on the DFAR, the Audit Division will revise the DFAR consistent with the vote of the Commission, and circulate the report ("the Circulated Final Audit Report") to the Commission for its approval on a 72-Hour no objection basis.

#### 1. Format and Content of the Circulated Final Audit Report<sup>13</sup>

- A. For any recommended finding that receives the affirmative vote of four or more Commissioners, the Audit Division will revise the text of the finding to reflect that it is a finding made by the Commission.
- B. For any recommended finding for which there are four or more affirmative votes to make a different finding from that which was recommended by

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<sup>10</sup> This new process will allow the Commission to benefit from the input of the Audit Division without the unnecessary and inefficient step of requiring the Audit Division to prepare a revision of the DFAR.

<sup>11</sup> In the event that the Commission votes to terminate a Title 2 audit at this stage of the process, all documents associated with the audit that have already been created and that would otherwise be made public at the conclusion will be made public on the Commission's website upon termination of the audit (including the IAR and any accompanying legal guidance), the committee's response to the IAR, the DFAR, the committee's response to the DFAR, and all vote certifications and links to open meeting agendas, meetings, and audit hearings.

<sup>12</sup> See Attachment 2 (Audit Findings Not Approved by the Commission, Certification dated May 16, 2006).

<sup>13</sup> The Commission has previously adopted some of these procedures. See Attachment 2 (Audit Findings Not Approved by the Commission, Certification dated May 16, 2006).

the Audit Division, the Audit Division will replace its recommended finding with a discussion of the finding made by the Commission. The Audit Division will move any discussion of its recommended finding to an "Additional Issues" section and will also include a footnote indicating that the Commission's finding differs from that recommended by the Division and that further discussion of the Division's recommended finding can be found in the "Additional Issues" section.

- C. For any recommended finding that does not receive four or more votes either approving or rejecting the recommendation, the Audit Division will move the discussion to an "Additional Issues" section. Each "Additional Issue" will contain a brief summary of the facts, any applicable legal standards, a brief recitation of the Audit Division's recommendation, and a statement describing the Commission's discussion of the issue and a recitation of the vote on the recommended finding.<sup>14</sup>

## 2. Approval of the Final Audit Report of the Commission

If the Circulated Final Audit Report is approved by tally vote, the title shall be changed to the "Final Audit Report of the Commission,"<sup>15</sup> and no further Commission action is required.

If the Circulated Final Audit Report is not approved by tally vote, the matter will be automatically placed on the agenda of the next open meeting of the Commission and the DFAR, the Audit Division Recommendation Memorandum, the Certification of the Vote of the Commission on the DFAR, and the Circulated Final Audit Report shall be made public as agenda documents.

### D. Public Disclosure

To further transparency and voluntary compliance, once the Commission approves a Final Audit Report of the Commission, the documents enumerated below will be placed on the public record, accessible *via* the Commission's website. Specifically, 30 days after the Commission approves a Final Audit Report of the Commission, the following documents, if available, shall be made public:

- Final Audit Report of the Commission and Vote Certification(s);
- Any written statements of any Commissioner(s);
- Audit Division Recommendation Memorandum and Vote Certification;

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<sup>14</sup> "Applicable legal standards" will generally consist of a restatement of the relevant statutory or regulatory provisions. If the Commission is unable to agree on the applicable legal standard, the report will so state.

<sup>15</sup> The Audit Report of the Commission is the Commission's document and shall reflect the views of the Commission on the recommendations of the Audit Division. See 2 U.S.C. § 438(b) ("The Commission may conduct audits and field investigations of any political committee required to file a report under section 434 of this title.... The Commission may, upon an affirmative vote of 4 of its members, conduct an audit and field investigation of any committee which does meet the threshold requirements established by the Commission.").

- Draft Final Audit Report (and any legal guidance provided thereon by the Office of General Counsel);
- Committee's Response to the Draft Final Audit Report (if any);
- Preliminary or Interim Audit Report (and any legal guidance provided thereon by the Office of General Counsel);
- Committee's Response to the Preliminary or Interim Audit Report;
- Link(s) to Open Meeting Agenda(s), Meeting(s), and Audit Hearing on the website (if any); and
- Links to audio or video of any Commission meetings related to the audit as well as any transcripts of hearing related to the audit.

## II. Legal Guidance

The Commission's Office of Compliance ("OC") (which includes the Reports Analysis Division ("RAD") and the Audit Division) may seek formal or informal legal guidance from the Office of General Counsel ("OGC") regarding questions of law that arise from the review of reports filed with the Commission or in the course of an audit of a political committee. This is an important intra-agency function, because neither RAD nor the Audit Division makes legal determinations. Moreover, such legal guidance often impacts whether: (1) RAD seeks additional information from a person or entity on a particular reporting issue, (2) the Audit Division pursues an issue in a pending audit, or (3) a matter is referred to OGC for enforcement.

### A. Internally-Generated Requests for Legal Guidance

#### 1. Timing

OGC shall respond timely to any request by OC for legal guidance. Specifically, OGC shall respond to all such requests within: (a) 30 calendar days, in the case of requests for informal legal guidance from RAD and Audit; (b) 45 calendar days of the request, in the case of requests from the Audit Division for formal guidance to at either the IAR or DFAR stage of a Title 2 audit; or (c) 60 calendar days of the request, in the case of requests from the Audit Division for formal guidance at either the PAR or DFAR stage of a Title 26 audit.

#### 2. Status Reports

OGC will provide the Commission with monthly status reports on all pending internally-generated requests for legal guidance.

The status report shall include the following information:

- a. the name of the committee being audited or the name of the person or entity about whom the request is being made by OC;
- b. the date that the request was received by OGC;
- c. a brief summary of the issue; and
- d. a reasonable estimate as to the date by which OGC is expected to render the requested guidance or present the issue to the Commission for its consideration.

#### 3. Commission Consideration of Novel, Complex, or Significant Legal Questions

Certain legal issues may warrant Commission consideration early in the reports analysis or audit process. In such instances, OGC and OC may at their own discretion bring the issue before the Commission for consideration.



The types of legal issues that OGC and OC are encouraged to bring before the Commission under this process include:

- a. Relatively close questions of law and questions of law on which the Commission has discretion to decide;
- b. Questions of law which, depending on the answer, would determine whether a significant amount of Commission resources would or would not be required on the particular matter involved;
- c. Questions of law that have been expressly reserved by the Commission – including in a prior audit, enforcement matter, or advisory opinion – for subsequent consideration;
- d. Questions of law on which a majority of the Commission has not previously made an affirmative decision; and
- e. Novel or unsettled questions of law, or questions prompted by developments in the law since the Commission last considered the same issue (including legislation, court decisions, or rulemakings) or technology.

Any legal issue presented to the Commission by OGC and OC under this procedure shall be accompanied by a statement of the issue and a recommendation by OGC and OC, and shall be circulated for a vote on the OGC and OC recommendation in accordance with all applicable Commission directives.<sup>16</sup> After the OGC and OC recommendation is circulated for a Commission vote, in the event of an objection, the matter shall be automatically placed on the next meeting agenda consistent with the Sunshine Act, 5 U.S.C. § 552b(g), and applicable Commission regulations, 11 C.F.R. part 2. However, if the Commission is unable to resolve the issue or to provide guidance on how to proceed with the matter by the affirmative vote of four or more Commissioners within 60 calendar days after the legal issue has been presented to the Commission for a vote (having thus reserved judgment on the issue), OC may proceed with the matter.

**B. Externally-Generated Request for Consideration of Legal Questions by the Commission**

The Commission is adopting a new procedure to provide a means for persons and entities to have a legal question considered by the Commission earlier in both the report review process and the audit process. Specifically, in the event that OGC provides legal guidance to OC recommending some type of corrective action by the person or entity about whom the guidance was sought, the appropriate Division of OC shall, within five days, provide a copy of OGC's legal guidance to the person or entity. If the person or entity disagrees with OGC's recommendation, the person or entity may, within 15 days from receipt of OGC's legal guidance, seek Commission consideration of the issue pursuant to this procedure.<sup>17</sup>

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<sup>16</sup> See, e.g., LRA #726 (Electronic Redesignation of Contributions / Date of Withdrawal) (presenting issues to the Commission, with recommendations).

<sup>17</sup> Requests should be directed to the Commission Secretary (Federal Election Commission, 999 E Street, N.W., Washington DC 20463), who will forward a copy to each Commissioner, the General Counsel, and the Staff Director.

Any request for consideration shall be limited to questions of law, when: (1) the legal issue is novel, complex, or pertains to an unsettled question of law, (2) there has been intervening legislation, rulemaking, or litigation since the Commission last considered the issue, (3) OGC is taking a position on the issue contrary to or otherwise inconsistent with prior Commission matters dealing with the same issue, or (4) if there is other good cause demonstrated. The request must specify the question of law at issue and why it is subject to Commission consideration. It should discuss, when appropriate, prior Commission matters raising the same issue, relevant court decisions, and any other analysis of the issue that may assist the Commission in its decision-making.

Within seven days of the filing of a request for consideration, OGC shall, in consultation with OC, make a recommendation to the Commission regarding the resolution of the issue. Within five working days of a legal issue being presented to the Commission by OGC, if two or more Commissioners agree that the Commission should consider the issue, the issue will then be circulated for a vote on OGC's recommendation in accordance with all applicable Commission directives.<sup>18</sup> After the recommendation is circulated for a Commission vote, in the event of an objection, the matter shall be automatically placed on the next meeting agenda consistent with the Sunshine Act, 5 U.S.C. § 552b(g), and applicable Commission regulations, 11 C.F.R. part 2. However, if within 60 calendar days of the filing of a request for consideration, the Commission has not resolved the issue or provided guidance on how to proceed with the matter by the affirmative vote of four or more Commissioners vote (having thus reserved judgment on the issue), OC may proceed with the matter.

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<sup>18</sup> See, e.g., LRA #726 (Electronic Redesignation of Contributions / Date of Withdrawal) (presenting issues to the Commission, with recommendations).

BEFORE THE FEDERAL ELECTION COMMISSION

In the Matter of )  
 )  
Voting Procedures for Title 2 Interim )  
Audit Reports )

CERTIFICATION

I, Mary W. Dove, Secretary of the Federal Election Commission, do hereby certify that on December 17, 2009, the Commission decided by a vote of 6-0 to approve the revision of the Voting Procedures for Title 2 Interim Audit Reports, as recommended in the Memorandum from the Assistant Staff Director, Audit Division, dated December 3, 2009.

Commissioners Bauerly, Hunter, McGahn II, Petersen, Walther and Weintraub voted affirmatively for the decision.

Attest:

December 17, 2009  
Date

Mary W. Dove  
Mary W. Dove  
Secretary of the Commission

Attach. 1

BEFORE THE FEDERAL ELECTION COMMISSION

In the Matter of )  
 )  
Audit Findings Not Approved By The ) Agenda Document No. X06-27  
Commission )

AMENDED CERTIFICATION

I, Darlene Harris, recording secretary for the Federal Election Commission executive session on May 16, 2006, do hereby certify that the Commission decided by a vote of 6-0 to adopt a policy that final audit reports reflect conclusions of the Commission, and the bodies of those reports reflect the legal standards as enunciated by the Commission and as applied to the particular circumstances of the audit reports.

Commissioners Lenhard, Mason, Toner, von Spakovsky, Walther, and Weintraub voted affirmatively for the decision.

Attest:

May 19, 2006  
Date

Darlene Harris  
Darlene Harris  
Deputy Secretary of the Commission