



## Interim Report of the Audit Division on Friends for Menor

May 10, 2006 – December 31, 2006

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### Why the Audit Was Done

Federal law permits the Commission to conduct audits and field investigations of any political committee that is required to file reports under the Federal Election Campaign Act (the Act). The Commission generally conducts such audits when a committee appears not to have met the threshold requirements for substantial compliance with the Act.<sup>1</sup> The audit determines whether the committee complied with the limitations, prohibitions and disclosure requirements of the Act.

### Future Action

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

### About the Campaign (p. 2)

Friends for Menor is the principal campaign committee for Ron Menor, Democratic candidate for the U.S. House of Representatives from the state of Hawaii, 2<sup>nd</sup> District and is headquartered in Honolulu, Hawaii. For more information, see chart on the Campaign Organization, p. 2.

### Financial Activity (p. 2)

- **Receipts**

○ From Individuals	\$ 134,292
○ From the Candidate	110,000
○ From Political Committees	27,225
○ Other Receipts	48
○ <b>Total Receipts</b>	<b>\$ 271,565</b>
  
- **Disbursements**

○ Operating Expenditures & Other Disbursements	\$ 245,498
○ Repayment of Candidate Loans	25,500
○ <b>Total Disbursements</b>	<b>\$ 270,998</b>

### Findings and Recommendations (p. 3)

- Apparent Impermissible Loans (Finding 1)
- Receipt of a Contribution that Exceeds Limits (Finding 2)

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<sup>1</sup> 2 U.S.C. §438(b).

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# **Part I**

## **Background**

### **Authority for Audit**

This report is based on an audit of Friends for Menor (FFM), undertaken by the Audit Division of the Federal Election Commission (the Commission) in accordance with the Federal Election Campaign Act of 1971, as amended (the Act). The Audit Division conducted the audit pursuant to 2 U.S.C. §438(b), which permits the Commission to conduct audits and field investigations of any political committee that is required to file a report under 2 U.S.C. §434. Prior to conducting any audit under this subsection, the Commission must perform an internal review of reports filed by selected committees to determine if the reports filed by a particular committee meet the threshold requirements for substantial compliance with the Act. 2 U.S.C. §438(b).

### **Scope of Audit**

Following Commission approved procedures, the Audit staff evaluated various risk factors and, as a result, the scope of this audit was limited to the following:

1. The consistency between reported figures and bank records.
2. The disclosure of individual contributors' occupation and name of employer.
3. The receipt of loans and contributions from the Candidate.

## Part II

### Overview of Campaign

#### Campaign Organization

<b>Important Dates</b>	<b>Friends for Menor</b>
• Date of Registration	May 25, 2006
• Audit Coverage	May 10, 2006 to December 31, 2006
<b>Headquarters</b>	Honolulu, HI
<b>Bank Information</b>	
• Bank Depositories	1
• Bank Accounts	1 Checking Account
<b>Treasurer</b>	
• Treasurer When Audit Was Conducted	Amadeo P. Manuel
• Treasurer During Period Covered by Audit	Amadeo P. Manuel
<b>Management Information</b>	
• Attended FEC Campaign Finance Seminar	No
• Used Commonly Available Campaign Management Software Package	Yes
• Who Handled Accounting and Recordkeeping Tasks	Treasurer

#### Overview of Financial Activity (Audited Amounts)

<b>Cash on hand @ May 10, 2006</b>	<b>\$ 0</b>
<b>Receipts</b>	
○ From Individuals	\$ 134,292
○ From the Candidate	110,000
○ From Political Committees	27,225
○ Other Receipts	48
<b>Total Receipts</b>	<b>\$ 271,565</b>
<b>Disbursements</b>	
○ Operating Expenditures & Other Disbursements	\$ 245,498
○ Repayment of Candidate Loans	25,500
<b>Total Disbursements</b>	<b>\$ 270,998</b>
<b>Cash on hand @ December 31, 2006</b>	<b>\$ 567</b>

## **Part III**

### **Summaries**

#### **Findings and Recommendations**

##### **Finding 1. Apparent Impermissible Loans**

FFM disclosed loans and/or contributions from the Candidate totaling \$75,000 that could not be verified as coming from the Candidate's personal funds. These funds were all transferred to FFM from the Candidate's business account. Based on the review of records for the Candidate's business account, it was determined the source of funds for the Candidate loans was \$54,000 from two corporations and \$21,000 from an unknown source. The Audit staff recommends that FFM demonstrate that these loans were from the Candidate's personal funds. Absent such a demonstration, the Audit staff recommends that FFM refund the impermissible funds and properly disclose the source of the loans. (For more detail, see p. 4)

##### **Finding 2. Receipt of a Contribution that Exceeds Limits**

The Candidate made a \$9,000 loan to FFM with funds from a trust. A \$10,000 check was drawn on a trust and made payable to the Candidate's spouse. These funds were deposited into a personal account of the Candidate and his spouse. On the same day, a \$9,000 check signed by the Candidate's spouse was made payable to FFM. The memo line of this check identified the purpose as a loan to FFM. Depending on who established the trust and the terms thereof, a possible excessive contribution was made by the Candidate's spouse, the beneficiaries of the trust, or the person(s) who established the trust. The Audit staff recommends that FFM provide evidence demonstrating that the Candidate was legally entitled to the funds received from the trust including information regarding the establishment and terms of the trust. Absent such evidence, FFM likely received an excessive contribution and should refund the excessive portion. (For more detail, see p. 7)

## Part IV

# Finding and Recommendation

### Finding 1. Apparent Impermissible Loans

#### Summary

FFM disclosed loans and/or contributions from the Candidate totaling \$75,000 that could not be verified as coming from the Candidate's personal funds. These funds were all transferred to FFM from the Candidate's business account. Based on the review of records for the Candidate's business account, it was determined the source of funds for the Candidate loans was \$54,000 from two corporations and \$21,000 from an unknown source. The Audit staff recommends that FFM demonstrate that these loans were from the Candidate's personal funds. Absent such a demonstration, the Audit staff recommends that FFM refund the impermissible funds and properly disclose the source of the loans.

#### Legal Standard

**A. Contents of Reports.** Each report must disclose for the reporting period and election cycle, the total amount of loans made by or guaranteed by the candidate and the identification of each person who makes, endorses or guarantees a loan to the committee. 2 U.S.C. §434(b)(2)(G) and (3)(E).

**B. Contribution Defined.** A gift, subscription, loan (except when made in accordance with 11 CFR §§100.72 and 100.73), advance, or deposit of money or anything of value made by any person for the purpose of influencing any election for Federal office is a contribution. The term *loan* includes a guarantee, endorsement, and any other form of security. A loan is a contribution at the time it is made and is a contribution to the extent that it remains unpaid. The aggregate amount loaned to a candidate or committee by a contributor, when added to other contributions from that individual to that candidate or committee, shall not exceed the contribution limitations set forth at 11 CFR part 110. A loan, to the extent it is repaid, is no longer a contribution. 11 CFR §100.52(a), (b)(1) and (b)(2).

**C. Expenditures by Candidates.** Candidates for Federal office may make unlimited expenditures from personal funds. 11 CFR §110.10.

**D. Definition of Personal Funds.** *Personal funds* of the candidate means the sum of all of the following:

(a) *Assets.* Amounts derived from any asset that, under applicable State law, at the time the individual became a candidate, the candidate had legal right of access to or control over, and with respect to which the candidate had legal and rightful title or an equitable interest;

(b) *Income*. Income received during the current election cycle, as defined in 11 CFR §400.2, of the candidate, including:

- (1) A salary and other earned income that the candidate earns from bona fide employment;
- (2) Income from the candidate's stocks or other investments;
- (3) Bequests to the candidate;
- (4) Income from trusts established before the beginning of the election cycle as defined in 11 CFR §400.2;
- (5) Income from trusts established by bequest after the beginning of the election cycle of which the candidate is the beneficiary;
- (6) Gifts of a personal nature that had been customarily received by the candidate prior to the beginning of the election cycle, as defined in 11 CFR §400.2; and
- (7) Proceeds from lotteries and similar legal games of chance. 11 CFR §100.33

**E. Receipt of Prohibited Contributions – General Prohibition.** Candidates and committees may not accept contributions (in the form of money, in-kind contributions or loans):

1. In the name of another; or
2. From the treasury funds of the following prohibited sources:
  - Corporations (this means any incorporated organization, including a non-stock corporation, an incorporated membership organization, and an incorporated cooperative);
  - Labor Organizations;
  - National Banks;
  - Federal Government Contractors (including partnerships, individuals, and sole proprietors who have contracts with the federal government); and
  - Foreign Nationals (including individuals who are not U.S. citizens and not lawfully admitted for permanent residence; foreign governments and foreign political parties; and groups organized under the laws of a foreign country or groups whose principal place of business is in a foreign country, as defined in 22 U.S.C. §611(b)). 2 U.S.C. §§441b, 441c, 441e, and 441f.

### **Facts and Analysis**

FFM disclosed loans and/or contributions from the Candidate totaling \$75,000 that could not be verified as coming from the Candidate's personal funds. These funds were all transferred to FFM from the Candidate's business account. Based on an examination of bank statements and other records relating to the Candidate's business account, the Audit staff determined the source of the funds was apparently \$54,000 from two corporations and \$21,000 from an unknown source.

During audit fieldwork, the Audit staff noted several deposits to the Candidate's business account that were made on the same day or just prior to the Candidate's transfers of the same or similar amounts to FFM. The average daily balance in the business account was only \$2,700 during the period when transfers to FFM were made.

The \$54,000 in question was from a mortgage lending company (\$29,000) and a housing construction company (\$25,000). Funds from these two corporations were part of three transfers to FFM from the Candidate's business account as described below:

- Transfer #1 for \$9,000- A check for \$10,000 from a mortgage lending company was deposited into the Candidate's business account on September 5, 2006. On the same day, a transfer of \$9,000 was made to FFM.
- Transfer #2 for \$30,000- Two checks for \$10,000 each from the same mortgage lending company were deposited into the Candidate's business account on September 8, 2006. In addition, a \$15,000 check from a housing construction company was also deposited. On the same day, a transfer of \$30,000 was made to FFM.
- Transfer #3 for \$15,000- Another check for \$15,000 from the same housing construction company was deposited into the Candidate's business account on September 15, 2005. On the same day, a transfer of \$15,000 was made to FFM.

Regarding the funds from the mortgage lending company, the Audit staff notes that the memo line for one of the company checks was redacted and the company's president who signed the checks was a contributor to FFM. It is also noted that the owner of the housing construction company contributed in-kind radio advertisements to FFM.

FFM has been unable to document the source for the \$21,000 deposited in the Candidate's business account and transferred to FFM. This amount includes a \$6,000 deposit made on August 25, 2006 for which the deposit slip has a handwritten notation stating "Cash". No source for this "Cash" deposit is identified and a \$5,000 transfer from this account to FFM was made on the same date. For the remaining \$16,000 in deposits, the Audit staff could not identify the source of the receipts based on the examination of the accompanying deposit slips.

The originating source for these Candidate loans was discussed at the exit conference. In support of his claim that the amounts were from personal funds, the Candidate provided a letter to the Audit staff which emphasizes that contributions to his campaign were never deposited into the law firm account. In addition, FFM provided a spreadsheet summarizing the income from legal services and expenses for the Candidate's law firm for the period from April 2006 to December 2006. This spreadsheet indicates the gross income from legal services for the third quarter (July thru September) and prior to the September 23, 2006 primary election to be approximately four times the income for either, the second or fourth quarters of 2006. It is noted that the income on this spreadsheet is significantly less than total receipts according to bank statements of the business for the same period.

#### **Interim Audit Report Recommendation**

The Audit staff recommends that, within 30 calendar days of service of this report, FFM provide evidence demonstrating that \$75,000 transferred to FFM came from the Candidate's personal funds. The evidence should include records to establish that the

funds deposited into the Candidate's business account meet the definition of *personal funds* in accordance with 11 CFR §110.10(a). This should include the following:

- Documentation such as copies of contracts, agreements, specific terms of service, and/or billing statements illustrating that the \$75,000 was received for services provided by the Candidate's business.
- For the \$21,000 from an unknown source, FFM should provide documentation such as copies of checks, bank credit memorandums, or any other records necessary to identify the source of amounts deposited and establish the funds as personal funds of the Candidate.
- Records to demonstrate the monthly financial position of the Candidate's business (i.e. net earnings statements, balance sheets)
- Tax returns or other documentation for calendar year 2006 to establish that the Candidate's business is a sole proprietorship for which the Candidate has legal entitlement to any assets or income.

Absent such evidence, the Audit staff recommends that FFM refund the apparent impermissible amounts (\$75,000) to the original source(s) and amend its reports to properly disclose the source of the loans. FFM should provide evidence of all repayments of these funds (legible copies of the front and back of the negotiated repayment checks).

## **Finding 2. Receipt of a Contribution that Exceeds Limits**

### **Summary**

The Candidate made a \$9,000 loan to FFM with funds from a trust. A \$10,000 check was drawn on a trust and made payable to the Candidate's spouse. These funds were deposited into a personal account of the Candidate and his spouse. On the same day, a \$9,000 check signed by the Candidate's spouse was made payable to FFM. The memo line of this check identified the purpose as a loan to FFM. Depending on who established the trust and the terms thereof, a possible excessive contribution was made by the Candidate's spouse, the beneficiaries of the trust, or the person(s) who established the trust. The Audit staff recommends that FFM provide evidence demonstrating that the Candidate was legally entitled to the funds received from the trust including information regarding the establishment and terms of the trust. Absent such evidence, FFM likely received an excessive contribution and should refund the excessive portion.

### **Legal Standard**

**A. Authorized Committee Limits:** An authorized committee may not receive more than a total of \$2,000 per election from any one person.<sup>2</sup> 2 U.S.C. §441a(a)(1)(A) and 11 CFR §110.1(a) and (b). The Bipartisan Campaign Reform Act of 2002 (BCRA) includes provisions that indexes the individual contribution limit for

<sup>2</sup> Person refers to an individual, partnership, or any group of persons, not including the federal government. 11 CFR §100.10.

inflation. The limit for individuals' contributions to candidates for the 2006 election cycle was \$2,100.

- B. Handling Contributions That Appear Excessive.** If a committee receives a contribution that appears to be excessive, the committee must either:
- return the questionable contribution to the donor; or
  - deposit the contribution into a campaign depository and keep enough money on account to cover all potential refunds until the legality of the contribution is established. 11 CFR §103.3(b)(3) and (4).

**C. 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.

**D. Definition of Personal Funds.** *Personal funds* of the candidate means the sum of all of the following:

(a) *Assets.* Amounts derived from any asset that, under applicable State law, at the time the individual became a candidate, the candidate had legal right of access to or control over, and with respect to which the candidate had legal and rightful title or an equitable interest;

(b) *Income.* Income received during the current election cycle, as defined in 11 CFR §400.2, of the candidate, including:

- (1) A salary and other earned income that the candidate earns from bona fide employment;
- (2) Income from the candidate's stocks or other investments;
- (3) Bequests to the candidate;
- (4) Income from trusts established before the beginning of the election cycle as defined in 11 CFR §400.2;
- (5) Income from trusts established by bequest after the beginning of the election cycle of which the candidate is the beneficiary;
- (6) Gifts of a personal nature that had been customarily received by the candidate prior to the beginning of the election cycle, as defined in 11 CFR §400.2; and
- (7) Proceeds from lotteries and similar legal games of chance. 11 CFR §100.33

### **Facts and Analysis**

FFM reported a \$9,000 loan from the Candidate that was made with funds from a trust. A check for \$10,000 was drawn on a trust and made payable to the Candidate's spouse. This check was deposited into a joint personal account of the Candidate and his spouse. On the same day as this deposit, a \$9,000 check from this joint personal account was deposited into the FFM campaign account. The check to FFM was signed by the Candidate's spouse and included a notation "loan to campaign" on the memo line. It is noted that the balance in this joint personal account on the day prior to the deposit of funds from the trust was not sufficient to allow for the transfer of the \$9,000 to FFM. In

addition, the average daily balance of the joint personal account for the period audited was only \$2,500.

FFM has not provided documentation regarding the terms of the trust or the identity of the beneficiary of the trust or the person(s) that established the trust. It is also not known what relationship the Candidate's spouse has to the trust or the trustees. Therefore, absent evidence that the Candidate was entitled to the funds, the Audit staff considers the source of the funds for the loan to FFM to be either the Candidate's spouse or the trust. Given the above, it appears that either the Candidate's spouse or the person(s) who established the trust made an excessive or potentially prohibited contribution to FFM.<sup>3</sup>

At the exit conference, the Audit staff discussed this issue with FFM's treasurer. No additional documentation that demonstrates the Candidate was entitled to the funds from the trust has been provided.

### **Interim Audit Report Recommendation**

The Audit staff recommends that, within 30 calendar days of service of this report, FFM:

- Provide evidence demonstrating that the contribution was not excessive or prohibited. Such evidence should include documentation demonstrating the Candidate's entitlement to the funds from the trust and the purpose of the \$10,000 check issued to the Candidate's spouse from the trust account. FFM should also provide information regarding the person(s) who established the trust and the beneficiary of the trust.
- Absent such evidence, refund the excessive portion of the contribution or, if determined to be a prohibited contribution, FFM should refund the entire contribution. Alternatively, FFM may make a disgorgement to the U.S. Treasury. FFM should provide evidence of contribution refunds with copies of the front and back of negotiated refund checks.
- If funds are not available to make the necessary refunds, FFM should disclose the contributions requiring refunds on Schedule D (Debt and Obligations) until funds become available to make such refunds.

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<sup>3</sup> The amount from the trust account may be considered a prohibited contribution depending on the identification of the beneficiary.