



FEDERAL ELECTION COMMISSION  
WASHINGTON, D.C. 20463

January 5, 2009

MEMORANDUM

To: Robert W. Biersack  
Press Officer

From: Wanda J. Thomas *WJ*  
Acting Assistant Staff Director  
Audit Division

Subject: Public Issuance of the Audit Report on Texans for Henry Cuellar  
Congressional Campaign

Attached please find a copy of the audit report on Texans for Henry Cuellar Congressional Campaign, which was approved by the Commission on December 18, 2008.

All parties involved have received informational copies of the report and the report may be released to the public on January 5, 2009.

Attachment as stated

cc: Office of General Counsel  
Office of Public Disclosure  
Reports Analysis Division  
FEC Library  
DSDD Website



# Report of the Audit Division on Texans for Henry Cuellar Congressional Campaign

January 1, 2005 – 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)

Texans for Henry Cuellar Congressional Campaign is the principal campaign committee for Henry Cuellar, Democratic candidate for the U.S. House of Representatives from the state of Texas, 28<sup>th</sup> District and is headquartered in Laredo, Texas. For more information, see the chart on the Campaign Organization, p. 2.

## Financial Activity (p. 2)

- **Receipts**
  - From Individuals \$1,217,986
  - From Other Political Committees 580,288
  - **Total Receipts** **\$1,798,274**
- **Disbursements**
  - Operating Expenditures & Other Disbursements \$1,776,668
  - **Total Disbursements** **\$1,776,668**

## Findings and Recommendations (p. 3)

- Receipt of Contributions that Exceed Limits (Finding 1)
- Receipt of Contributions from Prohibited Sources (Finding 2)
- Misstatement of Financial Activity (Finding 3)

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<sup>1</sup> 2 U.S.C. §438(b).

# **Report of the Audit Division on Texans for Henry Cuellar Congressional Campaign**

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January 1, 2005 – December 31, 2006



# Table of Contents

	<b>Page</b>
<b>Part I. Background</b>	
Authority for Audit	1
Scope of Audit	1
<b>Part II. Overview of Campaign</b>	
Campaign Organization	2
Overview of Financial Activity	2
<b>Part III. Summaries</b>	
Findings and Recommendations	3
<b>Part IV. Findings and Recommendations</b>	
Finding 1. Receipt of Contributions that Exceed Limits	4
Finding 2. Receipt of Contributions from Prohibited Sources	7
Finding 3. Misstatement of Financial Activity	9

# **Part I**

## **Background**

### **Authority for Audit**

This report is based on an audit of Texans for Henry Cuellar Congressional Campaign (THC), 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 receipt of excessive contributions and loans.
2. The receipt of contributions from prohibited sources.
3. The disclosure of contributions received.
4. The consistency between reported figures and bank records.
5. The completeness of records.
6. Other committee operations necessary to the review.

## Part II

### Overview of Campaign

#### Campaign Organization

<b>Important Dates</b>	<b>Texans for Henry Cuellar Congressional Campaign</b>
• Date of Registration	January 10, 2002
• Audit Coverage	January 1, 2005 – December 31, 2006
<b>Headquarters</b>	Laredo, Texas
<b>Bank Information</b>	
• Bank Depositories	One
• Bank Accounts	Two checking accounts
<b>Treasurer</b>	
• Treasurer When Audit Was Conducted	Rosendo Carranco
• Treasurer During Period Covered by Audit	Rosendo Carranco
<b>Management Information</b>	
• Attended FEC Campaign Finance Seminar	Yes
• Used Commonly Available Campaign Management Software Package	Yes
• Who Handled Accounting, Recordkeeping Tasks and Other Day-to-Day Operations	Paid and volunteer staff

### Overview of Financial Activity (Audited Amounts)

<b>Cash on hand @ January 1, 2005</b>	<b>\$ (11,225)<sup>2</sup></b>
<b>Receipts</b>	
○ From Individuals	\$ 1,217,986
○ From Other Political Committees	580,288
○ <b>Total Receipts</b>	<b>\$ 1,798,274</b>
<b>Disbursements</b>	
○ Operating Expenditures & Other Disbursements	\$ 1,776,668
○ <b>Total Disbursements</b>	<b>\$ 1,776,668</b>
<b>Cash on hand @ December 31, 2006</b>	<b>\$ 10,381</b>

<sup>2</sup> THC overdrew this account and the bank charged interest on the overdrawn balance.

## **Part III**

### **Summaries**

#### **Findings and Recommendations**

##### **Finding 1. Receipt of Contributions that Exceed Limits**

THC received \$36,300 in excessive contributions from twelve individuals and one partnership. Some of these excessive contributions resulted from improper election designations and/or contributor attributions. Excessive contributions totaling \$14,000 from ten contributors lacked the requisite contributor notifications of the presumptive redesignations/reattributions. The remaining \$22,300 appeared to require refunds. In response to the interim audit report, THC provided copies of seven non-negotiated refund checks totaling \$22,300 and redesignation/retribution letters sent to the contributors for the remainder. Subsequent to the final audit report's submission to the Commission, THC submitted copies of negotiated refund checks and bank statements to document that requested refunds had been made. (For more detail, see page 4.)

##### **Finding 2. Receipt of Contributions from Prohibited Sources**

A review of contributions identified two contribution checks, totaling \$13,000, which, without additional information from the contributor were treated as having been received from corporate sources. If the contributions are from permissible sources, portions of each, totaling \$10,500, would be added to the excessive contributions in Finding 1. Of the \$10,500 added to the excessive finding, \$2,100 could have been resolved provided the necessary notification letter was sent to the contributor advising of the presumptive action taken by THC. In response to the interim audit report, THC provided copies of two non-negotiated refund checks totaling \$8,800. THC failed to establish the remaining contributions were from permissible sources. Subsequent to the final audit report's submission to the Commission, THC submitted copies of negotiated refund checks and bank statements to document that requested refunds had been made. (For more detail, see page 7.)

##### **Finding 3. Misstatement of Financial Activity**

A comparison of THC's reported activity to bank records revealed a misstatement of receipts, disbursements, and cash on hand in both 2005 and 2006. For 2005, THC overstated beginning cash on hand by \$6,908, overstated receipts by \$5,523, understated disbursements by \$61,109 and overstated ending cash on hand by \$73,540. In 2006, receipts were overstated by \$85,040, disbursements were understated by \$41,322 and the ending cash on hand was overstated by \$29,821. In response to the interim audit report, THC filed amended disclosure reports which materially corrected the misstatements. (For more detail, see page 9.)

## Part IV

# Findings and Recommendations

### **Finding 1. Receipt of Contributions that Exceed Limits**

#### **Summary**

THC received \$36,300 in excessive contributions from twelve individuals and one partnership. Some of these excessive contributions resulted from improper election designations and/or contributor attributions. Excessive contributions totaling \$14,000 from ten contributors lacked the requisite contributor notifications of the presumptive redesignations/reattributions. The remaining \$22,300 appeared to require refunds. In response to the interim audit report, THC provided copies of seven non-negotiated refund checks totaling \$22,300 and redesignation/retribution letters sent to the contributors for the remainder. Subsequent to the final audit report's submission to the Commission, THC submitted copies of negotiated refund checks and bank statements to document that requested refunds had been made.

#### **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 as adjusted by the Consumer Price Index (CPI). 2 U.S.C. §441a(a)(1)(A), (c) and (f); 11 CFR §§110.1(a) and (b) and 110.9(a).

Based on the respective CPIs, the contribution limit for any one person for the 2006 election cycle was \$2,100 and \$2,300 for the 2008 election cycle.

**B. Contributions by Partnerships.** A contribution by a partnership is attributable to the partnership and proportionally to each partner. The contribution shall not exceed the limitations at 11 CFR 110.1(b), (c) and (d). 11 CFR §110.1(e).

**C. 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 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 retribution or a redesignation of the excessive portion, following the instructions provided in Commission regulations (see below for explanations of retribution and redesignation); and
  - o If the committee does not receive a proper retribution 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).



**D. Presumptive Redesignation of Excessive Contributions.** When an authorized political committee receives an excessive contribution from an individual or a non-multi-candidate committee, the committee may presumptively redesignate the excessive portion to the general election if the contribution:

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

Also, the excessive portion of an undesignated contribution made after the primary, but before the general election may be automatically applied to the primary if the campaign's net debts outstanding from the primary equal or exceed the amount redesignated.

The committee is required to notify the contributor in writing 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. For this action to be valid, the committee must retain copies of the notices sent as required. Presumptive redesignations apply only within the same election cycle. 11 CFR §110.1(b)(5)(ii)(B) & (C) and (l)(4)(ii).

**E. Reattribution of Excessive Contributions.** When an authorized committee receives an excessive contribution, the committee may ask the contributor if the contribution was intended to be a joint contribution from more than one person.

- The committee must, within 60 days of receipt of the contribution, obtain and retain a reattribution letter signed by all contributors; or
- Refund the excessive contribution. 11 CFR §§110.1(k)(3), 110.1(l)(3) and 103.3(b)(3).

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

- How the contribution was attributed; and
- The contributor may instead request a refund of the excessive amount. 11 CFR §110.1(k)(3)(ii)(B).

For this action to be valid, the committee must retain copies of the notices sent. 11 CFR §110.1(l)(4)(ii).

**F. Refund or Disgorge Questionable Contributions.** If the identity of the original contributor is known, the committee should 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**

THC received excessive contributions totaling \$36,300. Many of these excessive contributions arose from a review of the “legal defense fund<sup>3</sup>” account, which had not been reported (See Finding 3). Of this amount, there were excessive contributions from twelve individuals totaling \$35,400 and from one partnership for \$900. Excessive contributions from ten of the contributors totaling \$14,000 could have been resolved, provided the necessary notification letter was sent to the contributor advising of the presumptive reattribution or redesignation action taken by THC. The remainder of the excessive contributions, \$22,300 (\$36,300 - \$14,000), appeared to require refunds. THC did not maintain sufficient funds in its bank accounts to make the necessary refunds.

At the exit conference, the Audit staff presented to the THC representatives their finding of excessive contributions and provided a schedule detailing the contributions in question. Additional excessive contributions (included above) were identified as a result of documentation submitted subsequent to the exit conference and THC was provided an updated schedule detailing all excessive contributions.

### **Interim Audit Report Recommendation and Committee Response**

The Audit staff recommended that THC:

- Absent evidence the contributions were not excessive, send notices to those contributors that were eligible for presumptive redesignation and/or reattribution (\$14,000) to inform those contributors how the contribution was designated and/or attributed and offer a refund of the excessive portion. Absent a request for a refund by the contributors, these notices would have obviated the need for a refund or payments to the United States Treasury. For notices sent to contributors, it was also recommended that THC provide a copy of each notice and evidence that it was sent. Such notices must demonstrate that both the contributor and the individual to whom the contribution was reattributed were notified; and
- Provide evidence demonstrating that the remaining contributions totaling \$22,300 were not excessive. Such evidence could have included documentation that the contributions were reattributed and/or redesignated in a timely manner or that the excessive contributions were timely refunded; or
- Absent such evidence, refund \$22,300 to the contributors and provide evidence of such refunds (copies of the front and back of negotiated refund checks), or pay the amount to the United States Treasury; or
- If funds were not available to make the necessary refunds, disclose the contributions requiring refunds on Schedule D (Debt and Obligations) until funds became available to make such refunds.

In response to the interim audit report, THC provided copies of seven non-negotiated refund checks totaling \$22,300 and copies of the presumptive redesignation and/or reattribution letters sent to contributors.

Subsequent to the final audit report’s submission to the Commission, THC submitted copies of negotiated refund checks and bank statements to document that requested refunds had been made.

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<sup>3</sup> The legal defense fund was begun as a recount fund following the March 2004 primary election which had been subject to a recount. THC apparently maintained this fund throughout the audit period and apparently used it as a campaign account.

## **Finding 2. Receipt of Contributions from Prohibited Sources**

### **Summary**

A review of contributions identified two contribution checks, totaling \$13,000, which, without additional information from the contributor were treated as having been received from corporate sources. If the contributions are from permissible sources, portions of each, totaling \$10,500, would be added to the excessive contributions in Finding 1. Of the \$10,500 added to the excessive finding, \$2,100 could have been resolved provided the necessary notification letter was sent to the contributor advising of the presumptive action taken by THC. In response to the interim audit report, THC provided copies of two non-negotiated refund checks totaling \$8,800. THC failed to establish the remaining contributions were from permissible sources. Subsequent to the final audit report's submission to the Commission, THC submitted copies of negotiated refund checks and bank statements to document that requested refunds had been made.

### **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).<sup>4</sup>

**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:

1. **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 partnership contribution for the 2006 election may not exceed \$2,100 (as adjusted by the consumer price index) per candidate, per election, and it must be attributed to each lawful partner. 11 CFR §110.1(a), (b), (e) and (g)(2).
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).

<sup>4</sup> In July 2008, the Commission responded to an advisory opinion request from an LLP organized under the laws of Florida, which elected corporate tax treatment for Federal tax purposes and, although taxed as a corporation in other states, would be taxed as a partnership in the states of Florida and Massachusetts. This LLP wanted to know whether the Commission considered it a corporation or partnership under the Act and Commission regulations and would it be permitted to support a separate segregated fund (SSF). The Commission determined that it would consider the LLP to be a partnership. This suggests that contributions from such entities should be treated in a manner similar to LLCs, requiring the Audit staff to determine tax filing status of an LLP with the appropriate state.

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).
4. An LLC that makes a contribution shall, at the time of the contribution, affirm that it is eligible to make the contribution. 11 CFR §110.1(g)(5).

### **Facts and Analysis**

A review of contributions from individuals identified two contribution checks, totaling \$13,000, on which was imprinted the reference L.P. or Ltd. According to the Texas Secretary of State, each entity, though not incorporated, was registered with the state of Texas as a Domestic Limited Partnership. Since such entities may elect tax treatment as corporations, pending the receipt of a written statement from each entity explaining how it elects to be taxed, the contributions were treated as being from a prohibited source.

If the contributions were from permissible sources, portions of two, totaling \$10,500, would be added to the excessive contributions in Finding 1., as follows:

- A \$10,500 contribution would be excessive by \$8,400 and appeared resolvable only by refund; and,
- A \$2,500 contribution would be excessive in its entirety; however, \$2,100 could have been resolved provided the necessary notification letter was sent to the contributor advising of the presumptive redesignation action taken by THC and the remaining \$400 appeared resolvable only by refund.

The Audit staff advised THC's representatives of this matter by phone and e-mail following the receipt of documentation from a previously undisclosed account. To address this issue, documentation was requested from each entity stating how each elects to file its taxes. THC representatives said that they would obtain the requested documentation.

### **Interim Audit Report Recommendation and Committee Response**

The Audit staff recommended that THC:

- Provide evidence demonstrating that the contributions in question were made with permissible funds (a statement from the contributing entity explaining its tax treatment or a copy of IRS Form 8832 entity classification election) and were not excessive; or
- Refund the impermissible funds and/or refund/resolve the excessive contributions as noted above and provide evidence of such refunds (copies of the front and back of the negotiated refund checks); or
- If funds were not available to make the necessary refunds, disclose the refunds due on Schedule D (Debts and Obligations) until funds became available to make the refunds.

In response to the interim audit report, THC provided copies of two non-negotiated refund checks totaling \$8,800. THC failed to establish the contributions are from permissible sources. Therefore, the entire amount should have been refunded. However, it appears that THC treated each contribution as permissible and attempted to refund the excessive portion.

Subsequent to the final audit report's submission to the Commission, THC submitted copies of negotiated refund checks and bank statements to document that requested refunds had been made.

### **Finding 3. Misstatement of Financial Activity**

#### **Summary**

A comparison of THC's reported activity to bank records revealed a misstatement of receipts, disbursements, and cash on hand in both 2005 and 2006. For 2005, THC overstated beginning cash on hand by \$6,908, overstated receipts by \$5,523, understated disbursements by \$61,109 and overstated ending cash on hand by \$73,540. In 2006, receipts were overstated by \$85,040, disbursements were understated by \$41,322 and the ending cash on hand was overstated by \$29,821. In response to the interim audit report, THC filed amended disclosure reports which materially corrected the misstatements.

#### **Legal Standard**

**Contents of Reports.** Each report must disclose:

- The amount of cash on hand at the beginning and end of the reporting period;
- The total amount of receipts for the reporting period and for the calendar year;
- The total amount of disbursements for the reporting period and for the calendar year; and
- Certain transactions that require itemization on Schedule A (Itemized Receipts) or Schedule B (Itemized Disbursements). 2 U.S.C. §434(b)(1), (2), (3), (4), and (5).

#### **Facts and Analysis**

The Audit staff reconciled reported financial activity to bank records for calendar years 2005 and 2006. The following charts outline the discrepancies for the beginning cash balance, receipts, disbursements and the ending cash balance for each year. Succeeding paragraphs address the reasons for the misstatements.

During fieldwork, the Audit staff became aware of an additional bank account. The legal defense fund account (fund) began as a recount fund following the March 2004 primary election; the recount dispute ended when the opponent conceded on August 13, 2004. THC maintained this fund throughout the audit period. All but one of the expenditures from this account were made for legal services. The available documentation, though limited, indicated that the payments were made for services rendered in the audit period. About 60% of the contribution checks deposited into this fund were payable to "Texans for Henry Cuellar." Therefore, for audit purposes, the Audit staff treated this fund as a THC campaign account.

<b>2005 Activity</b>			
	<b>Reported</b>	<b>Bank Records</b>	<b>Discrepancy</b>
Beginning Cash Balance 01/01/2005	(\$4,317)	(\$11,225)	\$6,908 Overstated
Receipts	\$637,474	\$631,951	\$5,523 Overstated
Disbursements	\$330,949	\$392,058	\$61,109 Understated
Ending Cash Balance 12/31/2005	\$302,208	\$228,668	\$73,540 Overstated

The overstatement of the beginning cash balance on January 1, 2005, could not be explained but most likely occurred due to prior period errors.

The overstatement of receipts resulted from the following:

• Unreported deposit to the legal defense fund	\$ 3,640
• Receipts reported not supported by check or credit	(6,000)
• Deposit adjustments	(2,100)
• Unexplained difference	<u>(1,063)</u>

**Net overstatement of receipts** (\$ 5,523)

The understatement of disbursements resulted from the following:

• Disbursements reported not supported by check or bank debit	(\$ 5,509)
• Unreported disbursements	43,075
• Unreported disbursement – legal defense fund	25,260
• Unitemized disbursements underreported	2,194
• Unexplained difference	<u>(3,911)</u>

**Net understatement of disbursements** \$ 61,109

The \$73,540 overstatement of ending cash on hand resulted from the misstatements noted above.

<b>2006 Activity</b>			
	<b>Reported</b>	<b>Bank Records</b>	<b>Discrepancy</b>
Beginning Cash Balance 01/01/2006	\$302,208	\$228,668	\$73,540 Overstated
Receipts	\$1,081,283	\$1,166,323	\$85,040 Understated
Disbursements	\$1,343,288	\$1,384,610	\$41,322 Understated
Ending Cash Balance 12/31/2006	\$40,202	\$10,381	29,821 Overstated

The understatement of receipts resulted from the following:

• Unreported receipts – legal defense fund	\$ 56,474
• Unreported in-kind contributions	5,201
• Unexplained difference	<u>23,365</u>
<b>Understatement of receipts</b>	<b><u>\$ 85,040</u></b>

The volume and condition of THC records did not allow for the unexplained difference to be specifically identified. However, THC receipts consisted solely of contributions from individuals or contributions from other political committees. All contributions from other political committees were reviewed and all were reported. Therefore, it can be inferred that these unreported receipts were all contributions from individuals.

The understatement of disbursements resulted from the following:

• Prior period reversal reported in error	(\$ 2,100)
• Unreported disbursements	61,692
• Unreported disbursements – legal defense fund	28,388
• Adjustments to unitemized disbursements	2,449
• Disbursements reported not supported by check or debit	(27,488)
• Transactions detailed on a loan analysis reported in error	(23,493)
• Unexplained difference	<u>1,874</u>
<b>Net understatement of disbursements</b>	<b><u>\$ 41,322</u></b>

During the audit period, payments THC made on its loan had been credited to another non-campaign related loan incurred by the Candidate. The bank provided a detailed loan analysis which showed that corrections had been made. As noted above, some information from this document was incorrectly reported by TLC.

The \$29,821 overstatement of ending cash on hand resulted from the misstatements noted above.

At the exit conference, the Audit staff explained the misstatements and subsequently provided THC representatives with schedules detailing these discrepancies. They agreed to review the spreadsheets provided and expressed a willingness to file amended reports.

### **Interim Audit Report Recommendation and Committee Response**

The Audit staff recommended that THC:

- Amend its reports to correct the misstatements noted above.
- In addition, the Audit staff recommended that THC amend its most recently filed report to correct the cash on hand balance with an explanation that the change resulted from a prior period audit adjustment. Further, THC should have reconciled the cash balance of its most recent report to identify any subsequent discrepancies that may have impacted on the \$29,821 adjustment recommended by the Audit staff.

In response to the interim audit report, THC filed amended reports which materially corrected the misstatements for 2005 and 2006; and, corrected cash on hand on its most recent report.