



Joint Legislative Audit Committee
Office of the Auditor General



REPORT TO THE CALIFORNIA LEGISLATURE

EFFICIENCIES AND ECONOMIES OF THE
ADMINISTRATION OF THE
POLITICAL REFORM ACT OF 1974

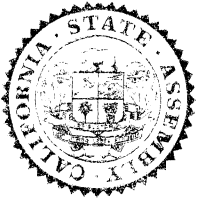
Office of the Auditor General
1955 - 1977

REPORT OF THE
OFFICE OF THE AUDITOR GENERAL
TO THE
JOINT LEGISLATIVE AUDIT COMMITTEE

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EFFICIENCIES AND ECONOMIES OF THE ADMINISTRATION OF
THE POLITICAL REFORM ACT OF 1974

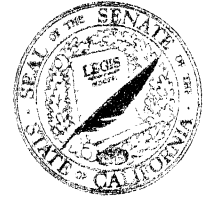
August 1977



Joint Legislative Audit Committee

OFFICE OF THE AUDITOR GENERAL

California Legislature



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August 16, 1977

The Honorable Speaker of the Assembly
The Honorable President pro Tempore of the Senate
The Honorable Members of the Senate and the
Assembly of the Legislature of California

Members of the Legislature:

Your Joint Legislative Audit Committee respectfully submits the audit report of Arthur Andersen & Co. on the administration of the Political Reform Act of 1974 by the Fair Political Practices Commission with the ministerial and technical assistance of the Secretary of State, the Attorney General and the Franchise Tax Board. This report reviews the efficiencies and economies of the operation. A fiscal audit by the Auditor General will follow.

Arthur Andersen & Co. recommends that a judgment of the effectiveness of the Act be deferred pending completion of the first four-year cycle (1978).

Although the proponents of the Political Reform Act of 1974 estimated a cost to the taxpayers of one million dollars, current costs reflect a four-fold increase with the Franchise Tax Board accounting for over \$2.5 million for its 100 percent mandatory audits. Arthur Andersen & Co. reports that a lower percentage of audits based on random selection techniques could enforce the same level of compliance with the Act.

The cavalier response of a staff member for the Franchise Tax Board ("... report is interesting, but contributes nothing new to our body of knowledge.") is mindful of an old adage of the U. S. Navy--"You can always tell an Ensign but you can't tell him much."

By copy of this letter, the Department is requested to advise the Joint Legislative Audit Committee within sixty days of the status of implementation of the recommendations of the Auditor General that are within the statutory authority of the Department.

Respectfully submitted,

MIKE CULLEN
Chairman

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The Honorable John H. Williams
Auditor General
State of California
925 L Street, Suite 750
Sacramento, California 95814

Dear Mr. Williams:

Enclosed is the final report of our independent audit of the efficiency, economy, and effectiveness of the Fair Political Practices Commission, the Office of the Secretary of State, the Office of the Attorney General, and the Franchise Tax Board in fulfilling their responsibilities specified by the Political Reform Act of 1974 as amended.

We appreciate the opportunity to perform this audit and to make our findings and recommendations known to the California Legislature. Your office has been most cooperative, as have the Fair Political Practices Commission, the Franchise Tax Board, the Office of the Secretary of State, and the Office of the Attorney General.

We believe that the current operations of these four agencies are consistent with the Political Reform Act and applicable regulations, and that their activities are being performed with reasonable efficiency and economy. The findings and recommendations presented below document those areas where we believe that improvement in efficiency and economy could be made. We believe that it would be premature to judge the effectiveness of the organizations in carrying out the provisions of the Act. This report indicates that considerable activity is in process, and the results of these activities must be evaluated before an assessment of effectiveness can be made.

We are forwarding copies of our working papers to you under separate cover.

We would be pleased to review our findings and recommendations with your office or with the members of the California Legislature.

Very truly yours,

Arthur Andersen & Co.

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I. SUMMARY

The findings and recommendations developed as a result of our independent study are presented in Section IV of this report. The table of contents of this report serves as an overall summary of these findings and recommendations.

Our findings are a description of the facts as we found them to exist. The recommendations represent our opinion of the actions that should be taken to improve the efficiency, economy, and effectiveness of the manner in which the Political Reform Act is administered.

The Commission has existed for approximately two and one-half years. Much of the Commission's effort during the first two years was devoted to the development of material describing the Act and its impact, to informing affected parties of its provisions, and to the establishment of working relationships among the Commission, the Franchise Tax Board, and the Offices of the Secretary of State and the Attorney General. Moreover, only within the past year and a half have the initial filings required by the Act become available after having been audited by the Franchise Tax Board. The first four-year election cycle under the Act will be completed when the required statements for the 1978 election are filed.

1. OVERALL ASSESSMENT

We believe that the current operations of these four agencies are consistent with the Political Reform Act and applicable regulations and that their activities are being performed with reasonable efficiency and economy. The findings and recommendations presented below document those areas where we believe that improvements in efficiency and economy could be made.

2. MAJOR FINDINGS AND RECOMMENDATIONS

Our major findings and recommendations include the following:

- 1) Early enforcement action has focused on investigations resulting from complaints and on alleged "blatant" violations. Fourteen different enforcement actions have resulted. These actions have consumed the major portion of the Commission's Enforcement Division's resources, and, as a result, investigations for 31 of the 32 audit reports

indicating substantial noncompliance have not been completed. We recommend that the Commission substantially increase its enforcement investigation and follow-up activities.

(Recommendation 1.7)

- 2) We found that the Act requires the FTB to audit at the 100% level. We do not believe that 100% auditing is necessary to enforce compliance with the Act. A case in point is that the FTB can enforce compliance with tax laws via less than 100% auditing. We recommend that randomness be introduced into the selection process and that the statute of limitations be increased.
(Recommendations 3.7 and 3.8)
- 3) The actual audit workload has been less than estimated. We recommend an increased emphasis on the development of workload estimating techniques and an adjustment to FTB staffing based on new yearly workload estimates.
(Recommendations 4.4 through 4.7)
- 4) While less than a week is required to perform an audit, the average elapsed time for audits exceeds 8 months. We recommend several audit management techniques which are aimed at reducing the elapsed time required to complete audits.
(Recommendation 5.7)
- 5) We found that the Secretary of State's filing system for political reform statements lacks adequate controls. We recommend that this system be redesigned to improve controls over the documents filed.
(Recommendation 11.4)

3. CHANGES TO THE ACT

In making our recommendations, we did not restrict ourselves to the current wording of the Act. The implementation of several of our recommendations will require modifications to the Act. The primary recommendations that require the Act to be changed include:

- 1) Introduce randomness into the audit selection process.
(Recommendation 3.7)

-
- 2) Increase the statute of limitations.
(Recommendation 3.8)
 - 3) Audit candidates and their committees at the same time.
(Recommendation 3.9)
 - 4) Budget in accordance with the yearly workloads and allow the FTB to borrow and lend staff between years to reduce the need to smooth the audit workload.
(Recommendation 4.6)
 - 5) Change filing procedures for lobbyists from a monthly to a quarterly basis.
(Recommendation 8.3)

4. ORGANIZATION OF THE FINDINGS AND RECOMMENDATIONS

The Findings and Recommendations section addresses 12 different areas. The areas that pertain to the Commission are:

1. Commission Enforcement Policy and Practices
2. Conflict-of-Interest Procedures
6. Education of the Filers Concerning Requirements of the Act
7. Commission Audit Responsibilities
9. Campaign Analysis Reporting
10. Clerical Staffing of the Commission.

The areas that pertain to the FTB are:

3. Audit Selection
4. FTB Staffing
5. Conducting the Audit.

The area that pertains to the Secretary of State's Office is:

11. Secretary of State Activities.

The area that pertains to the Attorney General's Office is:

12. Attorney General Activities.

The area that pertains only to the Act is:

8. Lobbyist Filing Requirements.

II. SCOPE OF REPORT

This final report was prepared by Arthur Andersen & Co. in accordance with contract LCB #9769 with the Joint Legislative Audit Committee of the State of California. In response to a resolution by the Joint Legislative Audit Committee, the Auditor General of California contracted with Arthur Andersen & Co. to perform an independent audit of the efficiency, economy, and effectiveness of the Fair Political Practices Commission, the Franchise Tax Board, the Office of the Attorney General, and the Office of the Secretary of State, in fulfilling their responsibilities specified by the Political Reform Act of 1974.

This audit was not a conventional financial audit. Arthur Andersen & Co. did not audit the financial statements of these agencies.

III. BACKGROUND OF THE POLITICAL REFORM ACT

The Political Reform Act was a ballot issue passed by the voters in 1974. The Fair Political Practices Commission was established by the Act and began operations in January, 1975. The Commission is unique in its autonomy and independence from the legislative and executive branches of the State Government. We know of no other similar state or federal commission with a budget that is protected by law. The Act authorizes a budget of one million dollars, plus cost-of-living increases to the Commission.

The Commission has relationships with other state agencies as prescribed by the Act. The most significant relationship is with the Franchise Tax Board (FTB) which is responsible for auditing lobbyists, candidates, and campaign committees. The findings of these audits are summarized in written reports to the Commission and the Attorney General. The audits and field investigations encompass reports and statements filed with the Secretary of State in accordance with provisions of the Act. The proposed budget for the Political Reform Audit Division of the FTB is over 2.5 million dollars. The FTB expenses are over 50% of the total funds allocated for support of the Act.

A second important relationship is with the Office of the Secretary of State which is charged with the responsibility for collecting the various statements and reports that must be submitted by candidates, lobbyists, committees, and holders of various elective offices.

A third relationship is with the Office of the Attorney General, which prosecutes criminal violations of the Act. Civil violations of the Act are handled either through administrative hearings or civil lawsuits instigated by the Commission.

The Act authorizes budget "amounts to be appropriated to other agencies (FTB, Attorney General, and Secretary of State) to carry out their duties under this title".

The purpose of the Act is to require full disclosure of all activities dealing with candidates, committees, elected officers, lobbyists, and lobbyist employers. The purpose of the audits is to verify that filed statements make disclosures in accordance with the requirements of the Act.

The primary objectives of the Act are shown in Exhibit A. Exhibit A also shows the functions that each agency performs in carrying out the objectives of the Act.

OBJECTIVES OF THE POLITICAL REFORM ACT OF 1974

<u>Objectives of the Act</u>	<u>State Agency Activities</u>
I. Full and truthful disclosure of receipts and expenditures in election campaigns.	<ol style="list-style-type: none">1. Commission provides technical assistance and reporting forms and guidelines2. Secretary of State collects reports filed by candidates and committees, determines whether they conform on their face with the requirements of the Act, and makes them available to the public.3. FTB makes audits and field investigations with respect to filed reports and statements.4. Commission publishes reports showing expenditures and source of funds.
II. Regulate lobbyist activities and disclose finances.	<ol style="list-style-type: none">1. Secretary of State collects reports submitted by lobbyists and their employers, monitors reports submitted to detect missing statements, and makes them available to public.2. FTB audits lobbyists' reports.3. Commission rules on what are appropriate lobbyist activities.
III. Disclose assets of public officials which may represent conflicts of interest.	<ol style="list-style-type: none">1. State agencies prepare codes at the direction of the Commission.2. The Commission approves disclosure codes prepared by State agencies.3. The Commission reviews the filings of incumbents and candidates for specific state and local offices, as well as heads of the state agencies preparing codes, to determine whether they conform on their face to the requirements of the Act.

Objectives of the Act

IV. Improve the format and content of the state ballot pamphlet.

V. Abolish laws and practices that unfairly favor incumbents in elections.

VI. Enforce the Act.

State Agency Activities

1. Secretary of State prepares a comprehensive and explanatory ballot pamphlet for every voter in California.
1. Order of names on ballots is now determined without regard to incumbency in California elections.
2. Mass mailings at public expense have been prohibited for candidates who have filed a declaration of candidacy.
1. FTB performs mandatory audits of candidate, committee, and lobbyist filings.
2. Both FTB and the Commission have the authority to audit records supporting filings made under the Act.
3. Commission has brought enforcement proceedings against alleged civil violators.
4. Secretary of State reviews filings for conformance on their face and imposes fines on late filers and nonfilers.
5. Attorney General investigates and prosecutes criminal violations of the Act.

IV. FINDINGS AND RECOMMENDATIONS

1. COMMISSION ENFORCEMENT POLICY AND PRACTICES

Findings:

- 1.1 The Commission's early efforts were devoted to educating affected parties about the provisions of the Act and to enforcing alleged violations uncovered through complaints.

The Commission began operations with a strong emphasis on educating affected parties concerning the provisions of the Act. The Technical Assistance & Analysis Division of the Commission's staff has developed a substantial amount of material that describes the Act.

The Enforcement Division of the staff received a full-time director less than a year ago. Early enforcement efforts were in response to complaints or related to alleged "blatant" violations.

- 1.2 No formal guidelines have been established for determining the degree of compliance evidenced by an audit report.

The Enforcement Division of the Commission has developed procedures for receiving audit reports from the FTB and systematically and routinely evaluating them. After dating and logging audit reports, an index card file system is updated to show the number of reports which have been received for a particular auditee and the audit periods covered by those reports.

After being logged, the audit reports are reviewed by a Division investigator and the degree of compliance indicated by the report is determined. Audit findings are evaluated as evidencing either substantial compliance, minor violations, marginal compliance or substantial noncompliance. However, no formal guidelines have been established for determining when an audit falls in one category as opposed to another.

Audit reports are considered to reflect minor violations of the Act when the discrepancy can be reconciled with a phone call or a follow-up letter. Reports are determined to indicate marginal compliance when it appears uncertain as to whether the violations are minor or whether they constitute substantial noncompliance. Further staff investigation is required to finalize the category. Substantial noncompliance is evidenced when numerous or

repetitive violations are reported; such cases usually require extensive staff time for investigation and follow-up.

The Division Chief and Division attorneys participate in the review process for cases suspected to be in substantial noncompliance. Otherwise, investigators and attorneys assume the responsibility of following up on reports indicating marginal compliance or minor violations. A liaison is maintained with the FTB when some form of action is being taken.

1.3 The Commission records and responds to complaints received regarding violations of the Act within the 14-day time limit specified in the Political Reform Act.

The Commission is required to respond to written complaints within fourteen days. In order to accomplish this, the Enforcement Division has developed procedures for logging, evaluating, and responding to written complaints.

Two types of complaints, formal and informal, are received. Complaints are logged and copied for distribution by the Division staff secretary. Copies of all formal complaints are made available to the public as required by the Act. Informal complaints are similarly logged but are held in strict confidence and made available only to the Commission's Executive Officer, General Counsel and Enforcement Division Chief.

Complaints are assigned to Enforcement Division attorneys and investigators and a response is developed within fourteen days. Responses are prepared for all complaints and reviewed and approved by the Division Chief and Executive Officer of the Commission. Complaints may be dismissed, referred to another agency or investigated. In instances where complaints lead to legal action or administrative hearings, enforcement action may result in civil violation proceedings, a negotiated settlement or imposition of a fine.

Considerable care is taken to ensure that the Commissioners are not provided with information that could prejudice their views before they are asked to make a decision on a case in an administrative hearings.

The Enforcement Division has responded to many complaints of noncompliance since the Act went into effect. Thirty-three formal complaints and 19 informal complaints were received in 1975, the first year of the program. Forty-six formal complaints and 67 informal complaints were received the following year (the first election year), although 23 of the formal complaints addressed a similar grievance. So far this year, eight formal complaints and 13 informal complaints have been received, and it is anticipated that slightly more than this will be received during the latter half of the year. It is anticipated that in 1978, the state election year, there will be a significant increase in the number of formal and informal complaints received.

1.4 Twenty-six percent of the FTB audit reports indicate some degree of noncompliance with the Political Reform Act.

From a Commission study of 481 audit reports received from the FTB as a result of the first audit cycle, approximately 127 (26%) of these required some follow-up activity. This sample, which represents over one-half of the 1975 audit workload, showed that while 73% of the audits indicated substantial compliance, 3% indicated minor violations and will require following up with letters or phone calls, 7% indicated substantial noncompliance, requiring extensive Division investigation, and 17% showed marginal compliance, indicating that continued investigation would be required in order to determine if substantial noncompliance occurred instead of a minor violation.

1.5 While the Commission has taken civil enforcement action on 14 separate cases, limited staffing resources have prevented the Commission from completing investigations on 31 of the 32 audit reports indicating substantial noncompliance.

Since the Commission has been operating, it has instigated fourteen enforcement cases. Nine of these took place in the first year and were resolved by administrative action resulting in fines being levied. In the last two years, the Enforcement Division has taken or is taking civil enforcement action on five different cases. One of these actions arose from a formal complaint while two of them were initiated by staff investigations and two were initiated by FTB audit reports. Of these five cases, three have been resolved by administrative hearings, while two are being pursued in the courts by the Commission.

To expedite the enforcement process, the Commission is currently pursuing the changing of regulations to give respondents the option of having a hearing of probable cause before the Executive Officer of the Commission as opposed to an administrative law judge.

The Enforcement Division is currently backlogged with audit reports and does not have the staffing required to meet projected workloads. The Enforcement Division has taken action on several of the cases evidencing substantial noncompliance. However, investigative follow-up is still required on about 31 of the substantial noncompliance cases. Because of manpower limitations within the Division, no follow-up action has been taken on any of the cases evidencing marginal compliance or minor violations.

The 1976 audit reports have just begun to arrive at the Commission. The Enforcement Division expects to receive 2,200 reports from audits resulting from 1976 election year campaign activity.

This volume of reports will overwhelm the Enforcement Division. Because the Division was less experienced when evaluating the first cycle of audit reports and because of the newness of the program, the Division estimates that the percentages of audits falling into each compliance category will change slightly. Current estimates are that 65% of future audit reports will be evaluated as showing substantial compliance, 15% showing marginal compliance, 15% showing minor violations, and 5% showing substantial noncompliance. Consequently, 770 (35% of 2200) audit reports will indicate some form of noncompliance and will require further Division action. This represents an anticipated increase in the investigative workload related to audit reports for the Enforcement Division of over 600% from last year. Future investigative effort related to complaints is difficult to estimate.

1.6 The Commission could simplify procedures for dealing with minor campaign disclosure violations reported by the FTB audits.

The Enforcement Division is planning to use "personalized" form letters in its attempts to correct situations where recurring minor violations have occurred in campaign disclosure statements. The Division has plans to develop various form letters to cover the majority of the minor violations. The objective of this effort is to educate people who inadvertently violate the Act. Because of the current enforcement action workload, these letters have not yet been developed.

Recommendations:

1.7 Increase enforcement investigation and follow-up of audit reports where there are indications of substantial noncompliance.

The Commission should put more emphasis into its enforcement activity. The Enforcement Division appears to be understaffed. The current workload will soon run into statute of limitation problems with cases where its investigations have not been finished. Future investigation requirements are estimated to be substantially greater than current workloads.

The Commission should reevaluate the staffing requirements for its enforcement activity and adjust its staffing as required to meet projected workloads. The backlog that currently exists in following up on complaints and audit report cases should be eliminated. Workload controls should be implemented so that backlogs do not develop and so that all cases are monitored and completed in a timely manner.

The Commission should also be encouraged to use the administrative hearing process in lieu of civil prosecution as the means to remedy most violations of the Act. An administrative hearing can expedite the enforcement proceedings by many months.

Follow-up action should be taken with minor violations. Immediate enforcement follow-up of violations would contribute, in a cost-effective manner, to eliminating the violations and reducing future workloads.

We believe that to be able to sufficiently address investigative workloads it will be necessary to increase the Commission's staffing resources. It does not appear that staffing allocated to other efforts can be utilized for investigative effort.

1.8 Develop form letters to follow up on minor political reform violations.

The Commission should complete the development of form letters to be sent in response to minor political reform violations of the Act. With the anticipated six-fold increase in the number of violations expected from the current audit cycle, this project must be given high priority.

Once the form letters are finalized, the Commission should develop a system for determining the proper letter or paragraph that applies to a violation, sending out the letter, and recording the fact that it was sent. An effective means of composing letters could be through the use of word-processing equipment. The Secretary of State's office is using word-processing equipment for its form letter mailings to late filers and nonfilers. This system could be reviewed for adoption by the Commission.

We understand that the Commission has developed form letters pertaining to late Statement of Economic Interest filings, but the Commission has developed only a few rough drafts of letters that would be sent to candidates, committees and lobbyists in response to contribution and expenditure reporting violations.

1.9 Provide feedback to the FTB regarding the use and disposition of audit reports.

Once an auditor releases his report, he loses track of it. Auditors are motivated by the impact of their reports, and often their reports have an impact on the Commission but the auditor is not aware of it.

The Commission should regularly provide a status sheet to the FTB that would allow the individual auditors to track the status of their reports. A concise worksheet that lists all reports and identifies which ones were involved in all of the various stages of investigation, review or enforcement would be sufficient to provide this feedback to the auditors.

2. CONFLICT-OF-INTEREST PROCEDURES

Findings:

2.1 The Commission is carrying out the conflict-of-interest functions specified in the Act.

Since its inception, the Commission has been concerned with informing the public on how to comply with the conflict-of-interest reporting requirements of the Act. The Commission has established a Conflict-of-Interest Division to assist state agencies in developing conflict-of-interest codes. This Division performs the following major functions:

- 1) Drafts regulations and opinions to interpret conflict-of-interest provisions.
- 2) Determines which state and local agencies are required to develop conflict-of-interests codes, schedules deadlines for submission of codes to the Commission and, where necessary, recommends to the Commission agencies which should be granted exemption from developing codes.
- 3) Drafts models of conflict-of-interest codes, assists agencies in developing codes and identifying "designated employees" who must file in accordance with the codes, monitors the status of code development by state and local agencies and recommends code approvals to the Commission.
- 4) Reviews progress of local code reviewing bodies regarding local code development.
- 5) Monitors Statements of Economic Interests filed by state, county and city office holders in accordance with conflict-of-interest codes. This monitoring function addresses only the filing of statements and does not address the content of the filings. (This function originated in the Conflict-of-Interest Division, but is currently under the responsibility of the Technical Assistance & Analysis Division.)
- 6) Handles inquiries, gives advice, and drafts formal opinions concerning actions which may be in conflict of interest.

Statements of Economic Interest are filed either at the Commission or at the offices of city or county clerks. The Commission currently receives approximately 5,000 Statements of Economic Interest for all elected state officers, judges, members of state and regional commissions, members of boards of supervisors, city councils, mayors, district attorneys, city managers and other local officers and approximately 3,000 statements from all heads of state and local agencies which act as code reviewing bodies.

Statements filed at the Commission are monitored to the extent of determining late filings and the amount of fines to be assessed. Statements are reviewed by the Commission for completeness.

2.2 Conflict-of-interest provisions have increased the awareness of potential conflicts among government officials.

Many people who have filed a Statement of Economic Interest have requested advice from the Conflict-of-Interest Division regarding whether participation in certain governmental decisions would be construed as being in conflict of interest. Several such requests are received monthly, the majority coming from city and county officers.

The news media have publicized several examples of situations where government officials have removed themselves from participating in specific decisions where they had a conflict of interest and in some cases have even relinquished their offices. This type of publicity by the media is an important aspect of conflict-of-interest enforcement.

Several complaints have been received from the public regarding conflict-of-interest violations. These complaints are typically handled by the Enforcement Division of the Commission. Of the thirty formal and informal complaints received dealing with conflict of interest, approximately half have been referred to other state or local agencies, and half were considered unsubstantiated.

While the Commission has investigated complaints related to conflict of interest, there has been no administrative hearing or civil action conducted by the Commission regarding conflict-of-interest violations. Investigations regarding conflict-of-interest violations have been delegated to district attorneys at local levels.

Recommendations:

- 2.3 Make state and local officials aware of any potential conflict of interest their employees may have and encourage them to prevent officials from acting in situations where they have a conflict of interest.

Besides heightening awareness of potential conflicts, the conflict of interest filings also provide a public record that identifies potential conflicts that could arise as the public official performs his duties. Local officials should be aware of any interests that agency employees have which might represent a conflict of interest in regard to the performance of their duties. The most appropriate individual to review an employee's filings would be the employee's immediate superior. The employee's superior should review the filing for content and should be required to certify to the fact that he has reviewed his subordinate's filings and that he will be responsible for advising him of any potential conflicts which he believes may exist or arise.

By regulation or amendment the Act should be modified to require this certification and the Commission should monitor the adherence to these certification requirements. One practical way to implement certification procedures would be to provide a statement and signature space at the bottom of conflict-of-interest forms. Upon reviewing the filed form for content, the filer's superior would attest to his review by signing the form.

- 2.4 Require local reviews of Statements of Economic Interest.

The Commission currently monitors the Statement of Economic Interest filings of elected state office holders and local officials. However, statements filed at the local level by management level employees of state agencies are not reviewed by the Commission. Awareness of potential conflicts would be substantially increased at the local level if these local filings were monitored.

The Commission should assure itself that local filings are being monitored. A description of local procedures for monitoring filings could be requested by the Commission from local agencies. Once monitoring procedures are established, assurance could be sought from local authorities that a responsible party at the local level is monitoring filings. We understand that the Commission plans to do this.

3. AUDIT SELECTION

Findings:

3.1 Virtually all mandatory audits specified in the Act are being performed.

The Act explicitly states the selection criteria for determining mandatory audits. The basis of audit selection depends on whether 15% or more of the vote was received by a candidate in a special or general election; whether \$25,000 or more was expended by or on behalf of a candidate in a primary, special or general election; whether a Committee supported a candidate who falls into one of the above mandatory audit categories; or whether a committee spent more than \$10,000 during any calendar year. All lobbyists and committees spending more than \$10,000 a year must be audited annually. Candidates and other committees must be audited after the last filing date of an election. The selection criteria are unbiased in the sense that they do not differentiate between winners and losers.

Besides specifying mandatory audits, the Act authorizes further optional audits at the discretion of the FTB or the Commission. Audits of lobbyists' employers are discretionary and not mandatory.

All audits performed to date have been conducted by the FTB. The FTB has only performed audits of individuals and committees that met the Act's mandatory selection criteria. Virtually 100% of all mandatory audits have been performed. (Independent committees spending less than \$10,000 have been given the lowest priority and have occasionally not been audited within the two-year statute of limitations allowed by the Act.) Interim statements, filed by candidates and committees during nonelection years are currently being audited.

3.2 Mandatory audits are being conducted in situations where there may be no activity reported.

Very often a candidate will use a controlled committee as the only means of accepting contributions or administering expenditures. In this situation, committee filings would reflect all financial activity while statements filed by the candidate could show no activity. When candidates who use this technique fall into a mandatory audit category,

an audit is performed on them concurrently with the committee. This means that all statements filed by the candidate, though mostly blank, are still developed into an audit package and sent to field offices of the FTB. An audit report is generated, reviewed, and issued. Concurrently, the candidate's committee is also being audited. Separate reports are developed for each of the candidate's controlled committees.

The Act is currently worded to require this auditing approach.

3.3 Subsequent audits for lobbyists have taken less time than initial audits.

After the initial lobbyist audits were completed, lobbyist bookkeeping records improved considerably. Since the condition of the bookkeeping records is one of the most important determinants of the length of time required for an audit, subsequent audits of lobbyist took substantially less time.

3.4 The reporting of only material items has significantly reduced audit time.

At the outset of the audit program, the Act was interpreted to require that all filing irregularities, no matter how minor, should be reported. Consequently, such items as omitting an address from a filed form were noted and reported.

Representatives of both the FTB and the Commission wanted audit reports to more readily identify those irregularities which warrant enforcement investigation. As a result, a regulation supported by both the FTB and the Commission gave the auditor the discretion to identify and report only material irregularities. This introduction of materiality has contributed substantially to a reduction in audit time.

3.5 100% auditing is not necessary to enforce compliance with the Act.

The current statutory requirement that the FTB audit 100% of those entities which exceed the mandatory selection criteria results in an unnecessarily high level of auditing. A lower percentage of audits based on random selection techniques could enforce virtually the same level of compliance with the Act.

Just as performing tax audits on less than 100% of returns has ensured compliance with the tax laws, political reform audits could be performed on a less than 100% basis. It is not necessary to audit every candidate, lobbyist and committee to ensure compliance with the Act. Filers would still feel pressure to comply as long as the audit selection was based on random selection techniques.

A reduction from 100% auditing does not imply a change or relaxation in filing requirements. Filers would still be required to file the same information on the schedule as they do currently.

3.6 The two-year statute of limitations could restrict the Commission's ability to enforce the Act.

Section 91011 of the Act specifies a two-year statute of limitations for civil prosecution. This limitation pertains to violation of the Act's reporting contribution requirements and to violations of disqualification provisions of conflict-of-interest codes. These limitations pertain to campaign, lobbyist and conflict-of-interest filers.

The delays presently being experienced in auditing filings, preparing audit reports, reviewing the reports, and initiating enforcement action could result in enforcement action not being initiated within the two-year statute of limitations.

Recommendations:

3.7 Introduce randomness in the audit selection process.

The Act should be changed to allow random selection techniques to be used to select the filings to be audited. Random techniques should be applied to the selection of lobbyists, candidates, and committees for auditing. We recommend that all statewide candidates and ballot issues be audited, but that only a random sample of lobbyists and other candidates be audited. There are several random selection techniques that could be used, including:

- 1) Auditing all campaign winners and only a random sample of losers.
- 2) Auditing all winners and losers in randomly selected districts, and not auditing anyone in other districts.

Either of the above approaches to random selection could result in fair enforcement of the Act. Auditing all winners and a sample of losers would ensure that everyone elected to office was audited. Moreover, losers would be encouraged to comply with the Act because a substantial sample of losers would be audited, and, consequently, there is a strong possibility that violations of the Act by losers would be detected. With this approach there would be no possibility that a winner would not be audited. However, in some instances the winner in a campaign would be audited while one or more losers would not. This could be regarded as "unfair" to these winners.

The second approach might involve auditing all winners and losers for state offices and then selecting districts randomly. Both winners and losers in the selected assembly and senatorial districts would be audited, while no one would be audited in the districts not selected. This approach would be unbiased in that winners and losers are treated in the same manner. However, not all winners would be audited.

We know of no objective way to choose between these approaches and believe that either approach would be consistent with enforcement of the Act.

Another way to audit more economically would be to increase the audit period and, therefore, audit each individual entity less often. To use this approach it would be necessary to modify the Act. We see this only as an alternative to introducing randomness into the audit selection process.

Because state elections occur in a two-year cycle, it would be natural to adopt a two-year audit period. All incumbent candidates could be audited on a two-year basis by combining the statements filed during an interim year with the statements filed during the following election year. (For four-year offices this would imply auditing interim statements at the two-year point.)

The Act should be changed to allow the FTB to select audits randomly. The effect random sampling would have on FTB auditor staffing is discussed in the next section. Filing requirements should not be relaxed. The investigation of complaints by the Commission and the Attorney General should be continued in the present fashion.

3.8 Increase the statute of limitations.

The Act should be changed so that the statute of limitations is increased to a longer period. The current two-year statute of limitations causes audits to be scheduled that otherwise might not be required. Exhibit B, developed in a study completed in March, 1977 by the Department of Finance, depicts the audit workload that will result in the four-year period from 1976 to 1980. The workload resulting from the 1978 elections extends from mid-1978 to early 1980. Audits whose field work is concluded in early 1980 would still need to undergo the FTB review process. The FTB review process has sometimes taken up to three months. Therefore, the Commission could receive some audit reports after the statute of limitations has expired. Typically, the audits that identify the most instances of noncompliance are the ones with the longest review process.

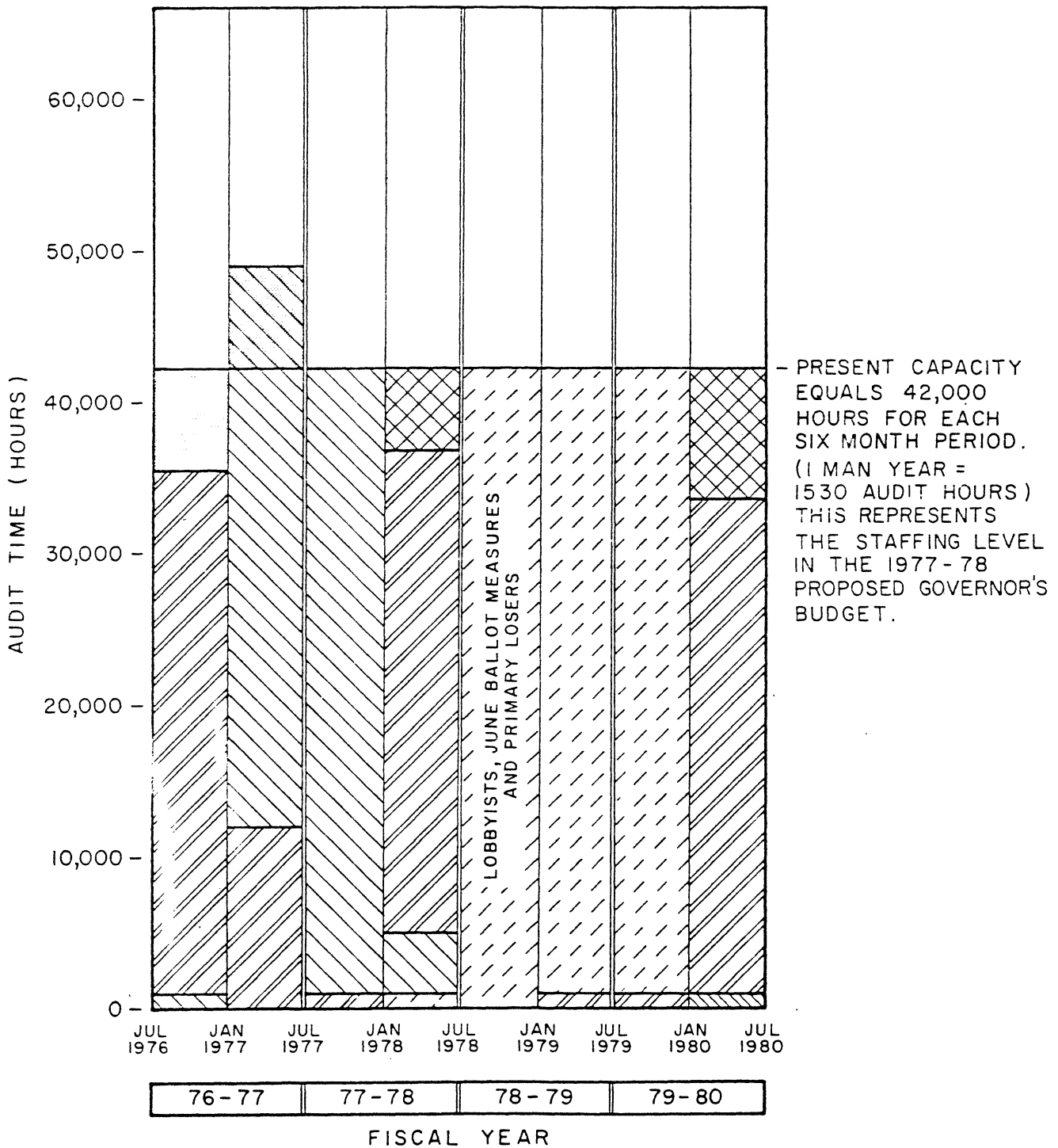
The current wording of the statute that fixed the time frame is awkward. It begins with the date of perpetration of the alleged violation rather than with the date of the filing. The statute would be more convenient to work with if its time frame were established via a filing date. This is the manner in which statute time frames are established for our tax laws and it has proven to be an effective method of establishing statute time frames.

Another problem with the two-year statute of limitations is that the current statute causes some minimal value discretionary auditing to be performed. In order to provide the Commission with timely audit reports, the FTB currently performs separate audits of interim statements filed by incumbents and ongoing committees during nonelection years. These audits are shown in Exhibit B as part of the "off-year workload from 1975, 1977, 1979".

3.9 Audit candidates and their committees at the same time.

The statute requires that audit reports be written and reviewed for candidates who have reported essentially no campaign activity. Currently, over eighty percent of all candidates use controlled committees for financial campaign activity. An economy can be gained by combining a candidate's filing with those of his committee and performing only one audit and producing only one report. The Act should be changed to allow this.

POLITICAL REFORM AUDIT PROGRAM
 ESTIMATED AUDIT WORKLOAD COMPLETION
 FOR SIX MONTH PERIODS, 1977-80
 (POLITICAL REFORM ACT AMENDED)



- LEGEND:
- WORKLOAD ARISING IN 1976
 - WORKLOAD ARISING IN 1978
 - LOAN STAFF
 - OFF YEAR WORKLOAD FROM 1975, 1977, 1979
 - WORKLOAD ARISING IN 1980
 - UNSCHEDULED AUDIT TIME

The Act has recently been modified to allow candidates to submit a form which essentially states that the candidate is using a controlled committee to control all campaign receipts and expenditures, and that all statements pertaining to the candidate will be filed by the committee. However, even in situations where this form has not been filed, economies can be gained by producing only one audit report encompassing the separate filings of candidates and their committees. The Act should be modified as necessary to give the FTB the authority to combine filings for audit purposes.

4. FTB STAFFING

Findings:

4.1 The actual audit workload has been less than estimated.

The first workload estimate was developed before the Act took effect and before any actual audit experience could be used as a basis for estimating.

In 1974, the FTB developed plans for creating the Political Reform Audit Division and described these plans in the "ASPEN" report. In this report, estimates of the number of audits to be performed and the number of auditors required were developed.

The Department of Finance completed a study in March, 1977, which also attempted to determine the correct staffing level over a four-year period. This study included revised estimates of the number of audits to be performed and the number of auditors required, based on the introduction of materiality into the audit process. Exhibit C is a tabular comparison of these estimates to actual.

4.2 Present workload estimating techniques are inadequate, and the FTB is now in the process of developing a new workload estimating technique.

The FTB has two workload estimating techniques - one developed by the Aspen Project and the other by the Department of Finance - and neither is adequate. There are two components for any workload estimating technique. The first deals with the times required to perform various types of audits (e.g., lobbyist, candidate). The second deals with the number of each type of audit to be performed.

The FTB has performed in excess of one thousand audits, and this experience provides a basis for estimating the amount of time required to perform each of the various types of audits. On the other hand, the Act has been in effect for only two and one-half years, whereas a full election cycle (from one statewide election to another) is four years. Consequently, the data needed to forecast the number of each type of audit will not be available until 1978.

The FTB is aware of these shortcomings and is in the process of developing an improved workload estimating technique.

COMPARISON OF ACTUAL AUDIT WORKLOAD
TO ESTIMATES

Source of Data	Number of Audits Per Year	Number of Auditors	Average Number of Audits Per Auditor
"ASPEN" Project Estimate	2,550	96	25.6
Department of Finance Estimate	1,800	55	34.2
Actual FTB Experience	1,178	53	22.2

4.3 The restriction of the FTB from borrowing and lending audit personnel between fiscal years inhibits staffing flexibility.

A provision of the 1976-1977 California State budget restricted the Political Reform Audit Division from borrowing and lending personnel with other FTB audit programs. While the FTB may shift personnel between the Political Reform Audit Division and other FTB divisions to meet varying monthly workload demands, it cannot incur a "personnel debt" in one fiscal year and satisfy it in another year. The borrowing and lending had been planned as a means to smooth out the extensive variation in audit workload peaks that occur from year to year in a four-year cycle.

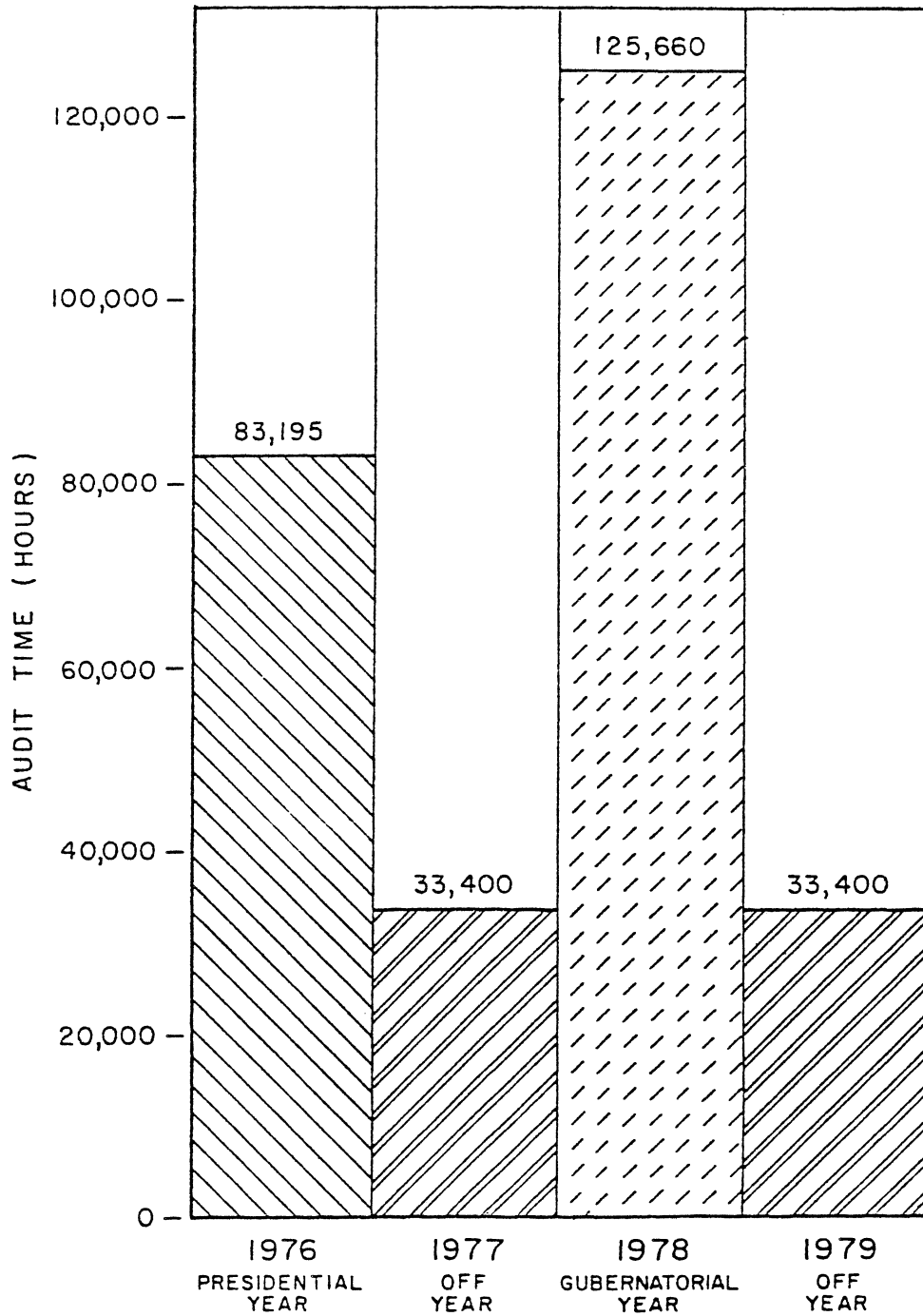
The audit workload has a four-year cycle that is dependent upon the four-year statewide election cycle. The number of elections and the subsequent audit workloads vary substantially from year to year within this cycle. Exhibit D was developed by the Department of Finance for their report issued in March, 1977, to depict the political reform audit workload of the FTB. The graph covers a standard four-year election cycle and shows the audit workload in terms of audit hours in the year the work is incurred. We can see from the graph that there are two years in which the audit workload is substantial and two years in which it is minimal. The largest audit workload is incurred during state election years followed by a second peak occurring during federal election years. Between these peaks are off-year workloads which are substantially smaller in terms of the number of audits performed and audit hours required.

Recommendations:

4.4 Finalize development of a workload estimating technique.

The FTB should develop and adopt a reliable technique for estimating the time that various types of audits will take. Once developed, the technique can be used to estimate the yearly audit workloads. Since the audit workloads vary substantially from year to year and the FTB may not lend or borrow personnel resources from year to year, planning and estimating become more important and demand more precision.

POLITICAL REFORM AUDIT PROGRAM
 NEW AUDIT WORKLOAD BY CALENDAR YEAR OF INCIDENCE
 1976 - 1979



SOURCE: Department of Finance

The FTB has had significant experience with the actual times required to perform various types of audits. However, there is considerable uncertainty about the number of each type of audit to be performed. Reference to the numbers of candidates and ballot issues in the 1970 and 1974 state elections should be of some use in forecasting these numbers for 1978.

Once developed, the technique should be reviewed and refined. The audit process will change over time as the tasks become more familiar to the auditors, as bookkeeping records improve, and as recommendations in this report are adopted.

4.5 Estimate personnel resources over a four-year time frame, based on projected workload estimates.

The estimating technique should be used to project yearly workloads over the next four years. The number of audits is a direct function of the number of offices up for election, the number of candidates, the number of lobbyists, and the number of ballot issues. Since the only "unknown" is the number of candidates seeking each office, the number of audits can be determined fairly accurately for estimating purposes. All that remains is to apply the estimating technique to the number of audits, project workloads on a four-year basis, and periodically refine the estimate.

A four-year time frame is appropriate since the workload cycle is not consistent from year to year and is affected by elections for four-year state offices.

4.6 Budget in accordance with the yearly workloads and allow the FTB to borrow and lend staff between years to reduce the need to smooth audit workload.

Once the yearly workloads have been estimated, they should be smoothed so that a staffing level can be established. One alternative would be to lend personnel to and borrow them from other divisions of the FTB. As noted above, such lending and borrowing between years is presently prohibited. The FTB should be allowed to build its Political Reform Audit Division staff in peak years by transferring auditors to the Division from other FTB programs. Under no circumstances should the FTB be required to adjust its Division staffing only via hiring and firing.

The current borrowing and lending restrictions incorporated into the FTB's budget language should be modified to allow the FTB to expand or contract its staff to some extent, in accordance with yearly workload, by transferring auditors into and out of the program. This change would enable the FTB to complete audits more promptly because it would reduce the need to "downstream" audits until staff is available.

With the increase in the statute of limitations recommended above, the workload could also be smoothed somewhat between years. This approach was advocated in the Department of Finance study and appears to be a practical one. The need to smooth the workload is shown in Exhibits B and D, which were taken from the Department of Finance study.

4.7 Adjust FTB staffing based on changes in audit workload.

In previous sections we have recommended that auditing requirements be adjusted so that an appropriate random sample, rather than 100 percent, of mandatory audits be performed each year. It is difficult to recommend that a sample of a specific size be audited. Clearly the sample must be large enough to encourage those who will not always be audited to comply with the Act. As discussed above, the decision to use random sampling has political ramifications, and should be considered fully before staffing is adjusted to reflect its use. For example, is it politically acceptable not to audit a large campaign because it is not selected in a random sample?

Exhibits E and F show the effect on the requirements for FTB auditors based on auditing 50% or 75% of the entities now being audited. In both cases the yearly audit workload is shown along with a fixed staff based on a workload smoothed over four years. This exhibit is based on the Department of Finance audit workload and time estimates (Exhibit G) and uses the standard of 1530 productive audit hours per year per auditor.

The Department of Finance workload estimates would result in a staffing level of approximately 45 FTB auditors if 100 percent of the mandatory audits are performed, 34 auditors if 75 percent are performed, and 25 auditors if 50 percent are performed. Our computation of a requirement of 45 auditors to do 100 percent of the mandatory audits is based on data shown in the Department of Finance report. This

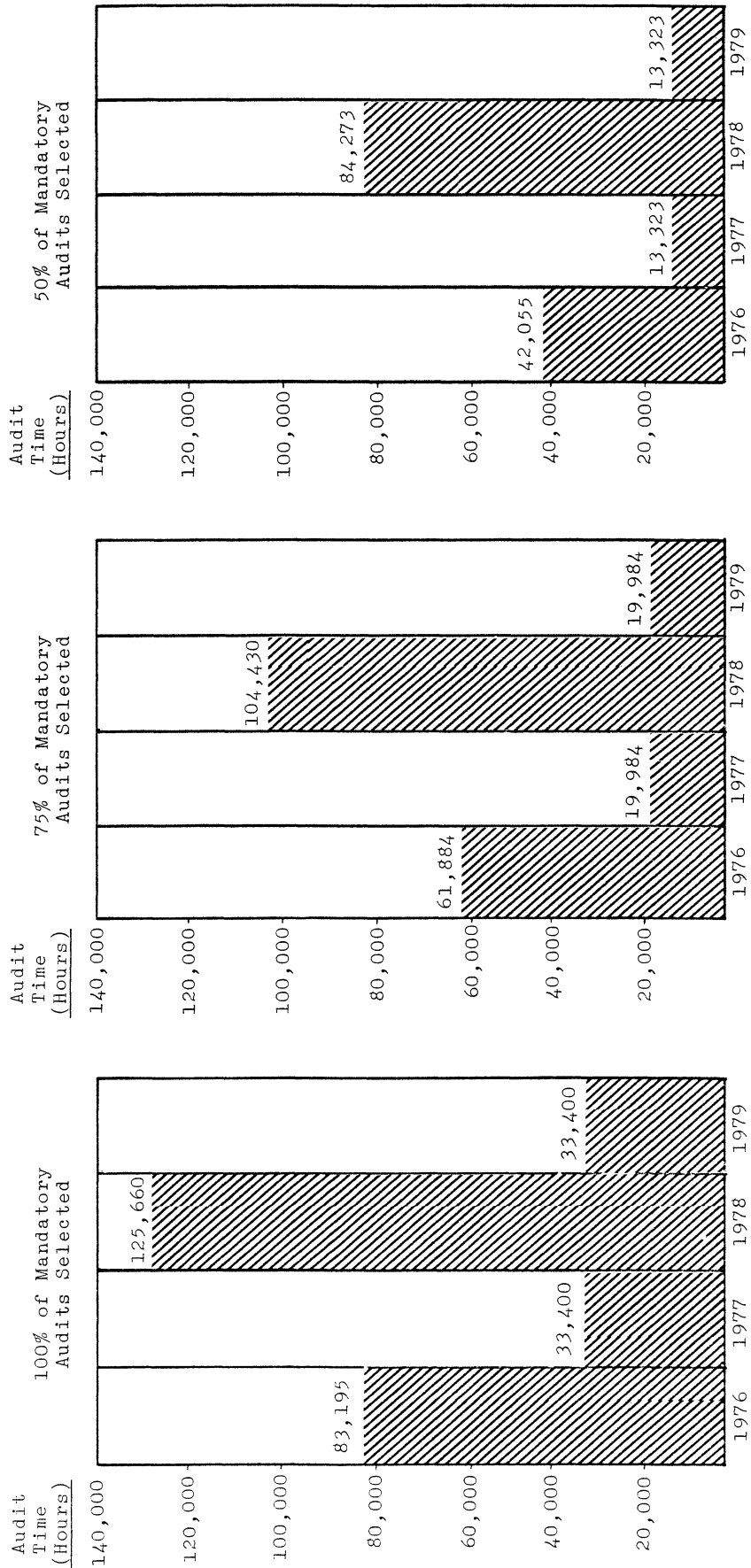
POLITICAL REFORM AUDIT PROGRAM
ESTIMATED TOTAL TIME FOR COMPLETION OF
MANDATORY AUDITS USING RANDOM SAMPLING

EXHIBIT F

Entity Type	Audit Hours if 75% of Entities Were Randomly Selected				Audit Hours if 50% of Entities Were Randomly Selected				
	1976	1977	1978	1979	1976	1977	1978	1979	
CANDIDATES									
Statewide Office*	0	0	700	0	0	700	0	0	
Senate	750	0	750	0	500	500	0	0	
Assembly	2,700	0	2,700	0	1,800	1,800	0	0	
Judicial	375	0	375	0	250	250	0	0	
CONTROLLED COMMITTEES									
Statewide Office*	0	0	33,660	0	0	33,660	0	0	
Senate	4,860	0	4,860	0	3,240	3,240	0	0	
Assembly	15,720	0	15,720	0	10,480	10,480	0	0	
Judicial	1,365	0	1,414	0	910	943	0	0	
INDEPENDENT COMMITTEES									
\$90001(e), spend > \$10,000	10,388	4,890	10,950	4,890	6,925	7,300	3,260	3,260	
\$90001(d), spend < \$10,000	9,413	2,044	9,863	2,044	6,275	6,575	1,363	1,363	
Ballot Measure Committees*	2,400	0	9,600	0	2,400	9,600	0	0	
SPECIAL ELECTIONS									
Candidates	113	225	113	225	75	75	150	150	
Controlled Committees	750	1,350	750	1,350	500	500	900	900	
LOBBYISTS	11,550	10,725	10,725	10,725	7,700	7,150	7,150	7,150	
MISC. AUDIT TIME	1,500	750	2,250	750	1,000	1,500	500	500	
TOTAL HOURS	61,884	19,984	104,430	19,984	42,055	84,273	13,323	13,323	
PERSON-YEARS (@ 1,530 Hrs/Year)	40	13	68	13	27	55	9	9	
AVERAGE AUDITOR STAFFING LEVEL	34			25			25		

* 100% selection for these entities.

COMPARISON OF TOTAL TIMES FOR COMPLETION OF MANDATORY AUDITS



report estimated the audit workload for the four-year audit cycle beginning in 1976 and running through 1979. The report recommended a staffing level of 55 auditors to handle this workload plus carry-over work from 1975. (No carry-over work is projected which will affect the workload of the next four-year cycle, 1980 through 1983.)

The discrepancy among Department of Finance audit estimates, FTB audit estimates, and actual audit times highlights the need for improved estimates so that proper staffing levels can be established.

5. CONDUCTING THE AUDIT

Findings:

5.1 Auditors are now using sampling to confirm contributions and expenditures.

The FTB's policy is to confirm less than 100% of reported contributions and expenditures.

Contributions and expenditures are treated differently for sampling purposes. Auditors select a sample size in accordance with statistical sampling principles. They aim for statistical reliability in their sampling approach and choose a sample size that will provide the desired reliability. The use of a statistical sampling technique is an appropriate and economical approach for confirming contributions.

Expenditures are generally not confirmed if they are supported by an invoice or bill. Large expenditures appearing in records, but not supported by a proper receipt, may be confirmed. Bank balances have generally not been confirmed.

5.2 Auditors use an FTB-prepared checklist as a guide to conducting the audit.

In order to conduct each audit using uniform minimum standards, the FTB has developed checklists to be used in the field while conducting the audit and to be used as a basis for reviewing the completeness of the field work. These checklists were developed before the Act took effect. Additionally, some auditors have developed their own working paper guides. These guides are usually developed from the FTB audit manual and help to ensure that all pertinent questions are asked and all factors are considered while in the field.

5.3 Materiality guidelines are not well documented.

The issue of materiality was resolved by the Commission and the FTB last year. Adopting the practice of reporting only material findings reduced the audit times considerably and eased the audit report writing process.

Materiality decisions are initially made by the individual auditors. However, there is little documentation of guidelines or past decisions for the auditor to use in his determination. Some materiality guidelines are incorporated into the FTB's political reform policy manual.

Audit supervisors generally review both material and nonmaterial findings. Further reviews of the audit report by a central review group and by FTB management focus only on material issues with changes occurring at all stages of the review process. Although discussions on materiality issues are held between auditors at office meetings, there is no formal process which currently allows office or division-wide feedback on new materiality decision guidelines.

5.4 The average elapsed time for an audit exceeds 8 months.

We found by sampling 50 closed cases that the average elapsed time from assignment of an audit to a field office to the time it was adopted by the Franchise Tax Board was over 8 months. The average elapsed time for field work was more than 5 months. 28% of the cases had an elapsed time of over 11 months. (The actual average time spent on these audits was 23 hours.)

The average elapsed time the audit was in the review process was 3 months. There are 5 levels to the audit review process: the audit supervisor, the district manager of audit field offices, central review within the program coordination section, the Political Reform Audit Division Chief and the FTB Executive Officer. While in the review process, an audit report can be returned to a previous review level for correction and modification. Changes can be made on audit reports at each of these review points.

At the time of our review, the steps in the review process were being reevaluated and restructured.

5.5 There is little preplanning of audit field activity.

In the field offices there is limited preplanning of audit activities. Mandatory audits are determined by the Program Coordination Section of the FTB's Political Reform Audit Division. Copies of field documents are

gathered to form audit packages, and the packages are sent to assigned field offices. When the packages are received in the field office, the standardized FTB checklist is used as the work program for conducting the audit. Field office supervisors do not develop individual work plans tailored to the audit at hand and to the individual doing the audit. The auditor begins his field work without having specific estimated audit times and milestone dates to work against. No time estimates for the audit or completion dates are given to the auditor at the time of the assignment. Evaluations on whether an audit was performed in the proper amount of time are subjectively made by the audit supervisors at the conclusion of the audit.

5.6 Minimal supervision is performed in the field.

Audits have typically been assigned to one auditor, regardless of the size, complexity or political sensitivity of the audit. The supervisors monitor jobs from the field office. There is minimal field supervision or contact.

In a field office there are three types of audit personnel, field auditors, supervisors, and office management. We found by surveying these personnel that field auditors spend virtually full time on audits, supervisors spend approximately 60% of their time on audit related activities, with only a minimum amount of this time actually being spent in the field, and office management spends no time auditing. Supervisors are seldom in the field. The majority of their time is devoted to review work performed at the conclusion of the audit.

Recommendations:

5.7 Reduce the elapsed time required to complete audits.

The eight-month average elapsed time that we observed in our sample of fifty audits is excessive, given that an average of only 23 hours of audit time was required for each audit. The five-month average elapsed time that an audit is in process could be reduced by assigning a small number of audits to each auditor at frequent intervals and requiring completion of these audits before assigning additional ones.

The three-month average time for review by the FTB also seems excessive. Complex financial audits performed by public accountants are reviewed by three or four levels of people within a matter of weeks, including one level of field review. The number of levels of review performed by FTB management should be analyzed and reduced. Also, schedules for reviews should be developed and monitored.

Included in the review time is the time it takes to adopt the audit reports by the FTB. There are often considerable delays in the adoption process. At the time of our evaluation there was a backlog of over 150 audit reports waiting for FTB approval. Half of these audits had been completed and had been waiting for adoption for over a month. This backlog causes an unnecessary strain on the Commission and Attorney General's Office which must review the approved audit reports. The FTB members should meet as often as necessary to eliminate this situation.

5.8 Increase field involvement by supervisory personnel on large audits.

Audit supervisors should be spending a greater portion of their time in the field on large audits. They would then be more familiar with audit problems as they are encountered. We believe that increased field involvement by supervisors will help them to better judge the quality of auditing being conducted, evaluate the time spent on each of the work tasks, and become familiar with the performance of the auditor while the audit is going on. This kind of involvement would have a more beneficial effect on the audit than would after-the-fact reviews. On larger and more complicated audits, a longer amount of time should be spent in the field by the supervisor.

5.9 Develop detailed field audit plans for large audits.

We recommend that as each audit package is recorded in the field office, supervisors should develop specific work programs, and determine the proper staffing. For large audits, individual work programs should represent a refinement of the average hourly estimates now used. These work programs should then be used as a basis of establishing target dates for each task and milestone dates for major reviews by supervisory personnel.

The individual work plan would be used as a basis for organizing the final audit working papers, and as a basis of reporting actual time spent on the major audit tasks.

The initial supervisory review of the audit package should also serve to confirm the staffing for the audits. While most audits are small and can be handled by one auditor, the practice of assigning only one auditor to each audit should not be followed across the board. Those audits that can be estimated to run greater than 500 hours should be staffed with more than one person.

We understand that the FTB is planning to use audit teams to audit committees with statewide activities and operations.

5.10 Develop documentation for materiality decisions.

As new or recurring decisions are made regarding materiality issues, guidelines should be developed, documented and distributed to all auditors in the field offices. In those instances when specific guidelines cannot be drawn up, examples of materiality decisions made on recent cases should be used.

Materiality decisions should be routinely communicated to all audit staff, not just the auditor and supervisor involved in the audit. Materiality decision guidelines should be used by auditors making the initial decisions regarding materiality and by auditors attending training sessions.

The Commission should be involved in and provide feedback to the FTB regarding the appropriate level of materiality.

6. EDUCATION OF THE FILERS CONCERNING THE REQUIREMENTS OF THE ACT

Findings:

- 6.1 The Commission prepares and distributes educational material for use by candidates, committees and lobbyists, and this material has been helpful to these individuals and groups.

The Technical Assistance & Analysis (TAA) Division has developed several information packets to educate lobbyists, candidates, committees and elected officials in the reporting requirements of the Act. The TAA Division obtains, from the Secretary of State, lists of candidates, lobbyists and committees who have filed campaign disclosure statements under the Act. With the use of these lists, the Division sends information packets to candidates for state office with the expectation that they will be turned over to the treasurer, or other appropriate individuals, of the committees supporting the candidate. These information packets are also supplied to county clerk offices for presentation to candidates and committee representatives at the time of their filing.

The TAA Division also conducts seminars to assist local filing officers, committee treasurers and other members, lobbyists and candidates in understanding the reporting requirements of the Act and in developing record-keeping practices that will expedite the subsequent audit process.

The TAA Division has prepared informational packets for candidates, committees and lobbyists which contain educational information summarizing the filer's responsibilities under the Act. These packets are sent to candidates and their committees, distributed at educational seminars held by the Division, and made available to city or county clerk filing offices for distribution at local levels. These packets contain instruction manuals and forms for campaign disclosure and conflict-of-interest reporting.

The TAA Division has also prepared as part of these packets short 2 to 4 page fact sheets which describe filing deadlines, prohibited activities under the Act and regulations adopted by the Commission.

One fact sheet that has been found to be very helpful and widely requested is a sheet describing how to set up bookkeeping records. This fact sheet was developed with the assistance of the FTB. It was found to be so useful that it has been included as an attachment to mass mailings by the Commission.

The Technical Assistance & Analysis Division spends a great amount of time answering individual questions received over the telephone. Over 1,800 inquiries were received and recorded in one peak month.

6.2 The bookkeeping records of some filers have been found to be inadequate.

In the course of the audit process, the FTB has found that the single most important element that determines how much time a particular audit takes is the condition of the bookkeeping records. The auditors have encountered both good accounting records and very poor records. Good accounting records have been found to speed up the audit process and enhance its reliability.

Lobbyists have shown a dramatic improvement in their bookkeeping practices. This improvement is due primarily to the learning that has occurred as a result of their initial audit. New candidate and committee records, however, have not shown similar improvements. It is doubtful that the learning process can be relied upon to improve these records, since each election brings new candidates and one-time committees who have never reported under the Act. Furthermore, it is not uncommon for committees to have turnover among treasurers and bookkeeping personnel in the course of an election.

Recommendations:

6.3 Distribute accounting fact sheets to each committee treasurer when he files his Statement of Organization with the Secretary of State.

Committee audits require the most time. Audit time is directly related to the condition of the bookkeeping records, and committee records have generally been found to be in worse condition than other entities' records.

The Commission should emphasize its bookkeeping educational efforts for committees. The most effective educational tool developed to date has been the

four-page fact sheet on bookkeeping and record requirements. These sheets should be made available to committee treasurers through the Secretary of State when the committees file their Statement of Organization. In addition, the Commission should mail the fact sheet to all committee treasurers and to candidates to ensure that it reaches the appropriate individuals. The fact sheet should not replace, but rather supplement, the information packet now produced by the Commission.

6.4 Provide record-keeping reviews when requested.

The Commission should identify personnel who will be responsible for reviewing the bookkeeping practices of committees, candidates or lobbyists. Reviews should be made only when requested by the committees, candidates or lobbyists.

Reviews would be most beneficial at the point when the requestors' record-keeping policies have been set up and have just begun to be put in practice. Reviews should be oriented toward observing the record-keeping process and identifying:

- 1) Areas where the records will not comply with the requirements of the Act.
- 2) Areas where the record keeping can be streamlined and performed on a more economical basis.
- 3) Elements of the records that are more elaborate than required to comply with the Act.

The availability of this service should be publicized in the bookkeeping fact sheet distributed to committee treasurers and candidates. Another effective means of informing filers of this service would be to send information on the availability of this service to individuals or committees whose FTB audit reports indicated poor record-keeping practices. Commission staff could develop a list of individuals to whom this information should be sent or the FTB could provide the Commission with similar lists developed during the course of their audits.

While the Division does answer specific questions related to an individual's bookkeeping records, an expansion of this effort would require additional staffing resources and an increase in the Commission's budget.

7. COMMISSION AUDIT RESPONSIBILITIES

Findings:

7.1 The Commission has the responsibility to audit candidates for Controller and member of the Board of Equalization.

The Commission is required by the Act to audit the filings and make field investigations of the records of candidates for Controller and member of the Board of Equalization and committees supporting these candidates. These candidates are running to become members of the Franchise Tax Board, the agency responsible for performing all other audits. Therefore, different auditing responsibilities are required to ensure audit independence.

Elections for Controller and Board of Equalization offices have not been held since the Commission was formed. Consequently, the Commission has not conducted audits required by the Act. However, the offices of Controller and member of the Board of Equalization will be on the 1978 ballot, and interim statements for incumbents have been filed with and reviewed by the Secretary of State. As a result, the Commission staff will have to perform some audit activities in late 1978 and early 1979.

7.2 The Commission has not formalized any auditing plans or procedures for the 1978 elections.

The Commission has not yet developed plans for auditing the above candidates after the 1978 primary and general elections. Likewise, plans have not yet been developed for auditing interim statements of incumbents in these offices.

The Commission has not felt the need to finalize these audit plans, however, it has identified the need for a permanent "accounting specialist" position. This staff member would bring auditing and accounting expertise to the Commission and would be involved in helping all divisions in accounting related matters. Currently, this position is filled by a member of the FTB on contract to the Commission. The specialist's major responsibilities are reviewing audit reports, developing record-keeping guidelines, assisting in enforcement investigations and acting as a liaison between the FTB and the Commission. However, because of the contractual relationship with the FTB and the question of independence, the accounting specialist does not take part in the auditing efforts which the Commission is responsible for.

Recommendation:

7.3 Develop plans for auditing candidates for Controller and member of Board of Equalization.

The Commission should develop plans and assign responsibilities for conducting audits of State Controller and Board of Equalization candidates and their supporting committees.

These plans should address the workloads that the audits will impose on the Commission staff, and should identify the detailed work tasks to be performed by the auditors. Materiality and sampling guidelines should be provided to the auditor, and the format for the final audit report should be identified. These auditing procedures and guidelines should be consistent with those of the FTB.

The accounting specialist position should be filled with a permanent noncontracted staffmember who would then be responsible for developing the audit program suggested above and conducting the required audits after the next year's election. We understand that this position has been authorized and incorporated into the budget.

8. LOBBYIST FILING REQUIREMENTS

Findings:

8.1 Lobbyists are required to file monthly reports when the legislature is in session.

The Act specifies that lobbyists and their employees are required to file periodic statements discussing all monetary activity incurred while performing lobbyist activities. These statements are required to be filed with the Secretary of State on a monthly basis. This results in about 700 lobbyist filings and 900 lobbyist employer filings per month. The Secretary of State's office is required to monitor late filings and assess fines for noncompliance on a monthly basis.

8.2 The FTB audits lobbyists annually.

While the original documents are retained by the Secretary of State for public viewing, copies of all statements filed are forwarded to the FTB. The information is entered into the computer system, and the documents are stored with other FTB documents in a centralized filing area. As audit assignments are determined, audit packages are developed by retrieving and copying the filed documents. Lobbyists' audits are usually performed at least once a year for all lobbyists.

Recommendation:

8.3 Change filing procedures for lobbyists from a monthly to a quarterly basis.

Lobbyist and lobbyist employers should be required to continue to report lobbyist activities on a monthly basis. However, filings should be changed to a quarterly basis. Timely disclosure is still achieved, with less work being required by the lobbyists, the Secretary of State, and the FTB.

9. CAMPAIGN ANALYSIS REPORTING

Findings:

9.1 The Commission has published a series of campaign analysis reports.

The Technical Assistance & Analysis Division has published several campaign analysis reports dealing with candidate and committee activities in the primary and general elections of 1976. In March, 1977, the Division published a comprehensive Campaign Contribution and Spending Report for the general election. The report lists campaign contributions and expenditures of state legislative office candidates and committees supporting ballot measures in the general election held in November, 1976. Information pertaining to election contributions and spending activities was obtained from campaign disclosure statements filed with the Secretary of State. The information was collected manually by temporary personnel. The format and content of the report was developed by the Division and is under its control.

The report was well received by the news media, evidenced by the number of articles written referencing the analysis results.

9.2 The FTB also generates computerized campaign analysis reports.

The FTB also produces computerized campaign analysis reports which are used to determine which audits will be mandatory. The FTB reports list expenditures made by committees supporting each candidate in an election. Information from all election-related forms filed under the Act is entered into the FTB computer system and used to generate various reports.

The major differences between the FTB and Commission reports are that the:

- 1) The Commission report lists receipts, expenditures and cash-on-hand for state legislative candidates and committees supporting and opposing ballot measures. The FTB reports list only expenditures made by committees for candidates.

-
- 2) The Commission report lists candidate contributions made by individuals, major donors, and committees. The FTB report lists expenditures made by campaign committees only but not contributions.
 - 3) The Commission reports receipts and payments of state party central committee organizations. The FTB does not report this information.

Information from campaign disclosure statements filed with the Secretary of State forty days and twelve days before an election date has been reported in some of the newspapers in the state.

Recommendations:

9.3 Utilize FTB data processing to produce campaign analysis reports.

The FTB computer system should be modified to produce the Commission's reports. It now produces reports which contain some of the information appearing on the Commission reports, and the format of the Commission reports can be modified at the discretion of the Commission's staff.

FTB production of Commission reports would require the volume of data captured by the FTB keypunchers to increase, but only a limited number of new types of input fields would be involved. Expanding the input capability of the FTB's data capture programs would allow the additional required information to be entered and processed along with the current input data. Once captured, the information can be easily sorted and reported as desired by the Commission.

We understand that the Commission is carrying out a feasibility study of using the FTB computer system to generate its campaign contribution and expenditure reports.

10. CLERICAL STAFFING OF THE COMMISSION

Findings:

10.1 The Commission has recently reviewed its clerical workload.

The Commission staff of 41 includes 14 clerical personnel. The Commission has recently completed a clerical workload and staffing study. This study was aimed at equalizing the existing workload among the clerical personnel. The implementation of recommendations made in this study has resulted in a more even distribution of the workload.

As a part of our review, we surveyed most of the Commission's personnel including all of the clerical personnel. This survey addressed the activities performed by the clerical staff as well as the time devoted to these activities. We found that there was very little nonproductive time and that clerical functions could be directly related to thorough performance of staff-generated work.

Recommendation:

10.2 Keep clerical staffing at its current level.

The Commission should keep its clerical staffing at at its present level, but should continue to monitor and review the clerical workloads. Clerical staffing may have to be increased in the future if, for example, the future volume of audit reports causes a corresponding increase in enforcement and investigative efforts.

Workload analysis studies like the one recently performed by the Commission should be performed periodically. These studies should address both the distribution of the workload, the need to continue to perform all functions, and the proper level of effort that should be directed to each function.

11. SECRETARY OF STATE ACTIVITIES

Findings:

11.1 The Secretary of State's filing system lacks adequate controls.

The Secretary of State is the filing officer for individuals, committees, and other entities including:

- Lobbyists and employers of lobbyists.
- Candidates for state elective offices.
- Committees supporting such candidates.
- State and county central committees of political parties.
- Committees supporting or opposing statewide measures.
- Organization statements for all committees that receive contributions of \$500 or more.

The filings received by the Secretary of State are reviewed for conformance on their face, copied and sent to the FTB. They are also made available for public viewing. All filings are reviewed by clerks and exceptions are referred to an auditor. A word-processing system is used to prepare "individualized" letters informing the filer of any omissions. A staff of three auditors reviews the omissions found and signs the letters prepared. In 1976, over 23,000 lobbyist filings were received and over 10,000 campaign disclosure filings were received. The public viewing rooms averaged about 6 people per day in 1976 and made over 17,000 photocopies at the request of the public.

The controls over the movement of these filings from the time mail is opened until the time the documents are placed in the files are inadequate for ensuring that each step of this movement is performed accurately and reliably and that forms are not lost. When the mail is opened, the forms are separated and processed without being logged. Forms are processed differently depending on the type of filing. Lobbyist filings are processed via a computerized system which records the date of receipt, the filer and type of document filed. All other filings are processed by a manual system which records the same type of information. There is no control log created at the mail opening point to identify the number and type of filings received.

Similarly, as forms move from one processing point to another there is no record kept of the number of forms into each point and the number of forms out. This type of control would ensure that documents are not misplaced and that documents are not placed directly in the files without being properly reviewed for conformance on their face. There is no adequate control to ensure that documents removed from the processing flow to be copied are returned to the proper point in the processing flow. No record is kept of copies actually sent to the FTB.

11.2 The Secretary of State's Office answers questions from prospective filers that require an interpretation of the Act.

The Secretary of State's Office receives many questions from prospective filers regarding filing deadlines and their obligations under the Act. Many questions require an interpretation of the Act. While the Office would prefer not to answer interpretive questions, it attempts to answer as many questions as possible. For this effort, it maintains and reviews copies of the Act, regulations, and opinion advices developed by the Commission. It prefers not to switch a caller to the Commission's Technical Assistance & Analysis Division, but will do so as a last resort. A comprehensive log is not maintained on the nature of all telephone conversations. While telephone memos are prepared for some conversations and placed in the caller's file, there is no log that serves as a ready reference of the topic of all phone calls. Such a log would be useful in substantiating advice given over the phone.

11.3 382 fines have been imposed on nonfilers and late filers, but 316 of these fines have been waived.

From January through June of 1977, the Secretary of State's Office imposed 382 fines. 316 waivers were subsequently granted, 42 fines were paid, and 24 are currently outstanding. \$1,640 has been collected in fines paid and the outstanding fines represent \$4,100.

The waiver request form is currently enclosed with the letter that imposes the fine. Only one follow-up letter is sent to delinquent payors. No other collection activity is performed.

Lobbyist filings are tracked by the computerized logging system. Statewide campaign and committee filings are tracked by manually comparing computerized listings of Statements of Candidacy and Statements of Organization against the earlier filings received.

Recommendations:

11.4 Completely redesign the filing system to improve control over documents filed.

The current system for processing political reform documents should be redesigned to incorporate adequate controls. The controls should ensure that all documents filed are processed properly and completely and that no documents are misplaced.

The objective of these controls should be to identify any processing problems at the earliest possible point in the processing flow.

A log of all forms received should be established at the mail opening point. Forms could be stamped with sequential numbers to readily track them through subsequent processing points. Forms could be sent in small batches from one processing point to another. All forms into and out of each processing point should be counted and these counts should be reconciled. Documents sent to the FTB should be recorded or notated on the control log.

11.5 Refer telephone questions concerning the Act to the Commission.

Callers who ask interpretive and responsibility-related questions should be switched to the Commission while the filer is still on the phone. The Secretary of State's Office should normally handle only questions relating to dates of filing, public viewing of documents, and Secretary of State initiated correspondence. Discretion should be used in determining which questions to answer. Callers need not be referred to the Commission, but simply transferred to the Technical Assistance & Analysis Division. Notations should be made on the nature of all information provided over the phone.

11.6 Take a more aggressive approach to collecting fines.

Instead of enclosing the waiver request form with the letter that imposed the fine, we recommend that the late filer be provided with a copy of the section of the Act that tells him he can request a waiver. The reasons for giving waivers should be reevaluated in view of the large percentage of waivers given. At a minimum, the criteria and procedures for determining when waivers should be granted should be formally established and documented. Further follow-up action beyond the one letter sent to delinquent payors should be established.

12. ATTORNEY GENERAL ENFORCEMENT ACTIVITY

Findings:

12.1 No formal policies exist for determining when criminal investigation and enforcement action should be initiated.

The Division of Criminal Law of the Attorney General has established procedures for reviewing audit reports prepared by the FTB. They are reviewed to determine where further investigation should be conducted to determine whether a criminal violation has occurred. Formal policies have been developed for conducting criminal investigations, but have not been developed for determining when an audit report should initiate an investigation.

Audit reports are currently reviewed by two Criminal Law Division attorneys separately to double-check the evaluation of the audit reports. The Criminal Law Division quickly recognizes and has communicated to the FTB its preference for special terms and phrases used in audit reports which may highlight possible criminal infractions. No written policies or procedures exist which clarify what considerations should be used to initiate follow-up investigative action.

Audit reports which indicate the possibility of a criminal violation may initiate either an inquiry or investigation case.

The Attorney General typically consults the FTB for clarification of facts and impressions developed during the audit, and tries to establish whether criminal intent existed or the violations were a result of record-keeping and reporting negligence.

12.2 The Attorney General has not conducted any prosecution for criminal violations of the Act.

The Division of Criminal Law has conducted several inquiries and investigations, stemming from audit reports and complaints. Its reported activity included eighteen inquiries and six investigations over an eight-month period ending February, 1977.

The Bureau of Investigations within the Attorney General's Office was involved with in-depth investigations on at least eight cases concerning alleged criminal violations. Investigations do not always

center on a single audit report or complaint, but often, when applicable, encompass all the candidates of a given race for which an investigation is being conducted.

Complaints concerning possible violations of the Act are also received directly by the Division of Criminal Law and also become the basis for inquiries and investigations. Complaints are investigated and will often correlate to subsequent audit reports. Approximately 12 complaints are received weekly including complaints referred to the Attorney General by the Commission.

For the eight-month period ending in February, 1977, the Attorney General's Office has expended the equivalent of slightly more than their budgeted four person-years, fulfilling their responsibilities as defined by the Political Reform Act. Half of this effort has been put into reviewing audit reports and following up on complaints, inquiries and investigations. To date, the Attorney General's Office has not taken any criminal enforcement action.

The Division of Criminal Law has, however, referred some cases to other entities for enforcement action. While the Commission will refer investigations to the Attorney General when it feels that possible criminal action is warranted, the Attorney General has also recommended that certain cases be prosecuted as a civil violation, emphasizing an administrative hearing as the process to conduct enforcement action. The Division of Criminal Law also refers cases to local District Attorneys for enforcement action. District Attorneys have brought prosecution based on the referrals.

Recommendations:

12.3 Develop written policies for reviewing audit reports and following up on possible violations.

The Attorney General's Office should develop written policies which better identify which violations it considers to be of a criminal nature, and the action that will be instigated when such a violation is detected. A formal policy will help ensure that consistent action is taken from case to case, and that political pressure is not brought to bear on the enforcement process.

Such a written policy will also communicate to the other agencies involved in carrying out the Act, those infractions the Attorney General's Office considers part of their enforcement jurisdiction. This can help resolve differences of opinion as to who is responsible for certain enforcement action.

12.4 Increase enforcement investigation and prosecution activity.

The more than 25 inquiries and investigations recorded during the eight-month period that have been conducted by the Attorney General's Office have not been significant in comparison to the total number of audit reports and discrepancies reported. However, this volume has taxed the staff assigned to investigate and prosecute violations of the Act. While only budgeted for two attorneys with regard to political reform activity, the Office has expended hours for almost three attorneys in carrying out its responsibilities.

The Attorney General's Office should conduct a thorough review of the manpower and procedures necessary to investigate the volume of discrepancies reported. The procedure established should ensure that investigations are performed in accordance with formal investigation policy. The workload should be estimated based on thorough performance of these procedures for the volume of audit reports anticipated. Personnel should be assigned to the investigation efforts in accordance with these workload estimates.

State of California



Fair Political Practices Commission

P.O. BOX 807 • SACRAMENTO, 95804 ••• 1100 K STREET BUILDING, SACRAMENTO, 95814

August 11, 1977

Mr. John H. Williams
Auditor General
925 L Street, Suite 750
Sacramento, CA 95814

Dear Mr. Williams:

Thank you for your courtesy in submitting to us a draft copy of the report prepared by Arthur Andersen & Co. entitled "Efficiency, Economy, and Effectiveness Audit of State Agency Responsibilities as Specified by the Political Reform Act." I am pleased to say that we consider the report thorough, sound and helpful.

The task of the Fair Political Practices Commission is to implement the Political Reform Act, the most comprehensive political reform statute ever adopted in the United States. Looked at from an administrative standpoint alone, the Commission's workload during its start-up period has been enormous. The Commission's task has been made more difficult by the extreme sensitivity of its work. We must perform our functions so that: the public will be assured that the reform laws are in fact being implemented; participation in government and politics will not be discouraged; and the fairness and impartiality of the Commission will be beyond question. To carry out its functions the Commission was given a budget that is a fraction of other major state regulatory commissions.^{1/} Finally, the Commission has had to operate continuously in an atmosphere permeated by controversy.

Viewed in this context, we believe the Arthur Andersen report is a strong vote of confidence in the performance of the Commission. Of course, we welcome the

^{1/} For example, the 1976-77 appropriations for four such commissions were as follows:

Energy Commission	\$24.46 million
Agricultural Labor Relations Board	6.96 million
Coastal Commission	2.52 million
FPPC	1.28 million

Mr. John H. Williams
August 11, 1977
Page Two

specific praise given to many aspects of the Commission's work in the report,^{2/} but we recognize that the primary mission of the auditors was to seek out problem areas and make recommendations. We are gratified that each of the few recommendations which touch the Commission may fairly be described as technical or peripheral. Some of the recommended procedures were already being planned when the audit began,^{3/} while others are constructive suggestions that we will explore and likely implement in the near future.^{4/} But the specific recommendations should not obscure what is unmistakably the central finding underlying the report, that in all major areas the Commission is doing its job to the limit of its resources and doing it well.

The one subject area where some clarification may be useful is enforcement, dealt with in Part 1 of the findings. We believe the goal of enforcement is not merely to catch and punish violators, but more broadly to bring about compliance. Thus, "enforcement" begins with what we call technical assistance -- providing information and helping people comply with the Act. The next stages are the review of statements by filing officers and the audits performed by the Franchise Tax Board. These stages serve a further educative function as well as weeding out the vast majority of violations that are inadvertent and immaterial. Finally, the cases that come to the Commission's enforcement division may be divided into two categories. First, the more serious of the "routine" violations, which may be unearthed by the FTB audit or may be the subject of a complaint. Second, the more serious and major cases which may involve deliberate efforts to conceal, or the failure to report information which, under the particular circumstances, was particularly material.

As the Arthur Andersen report states in Sections 1.7 and 6.4, the Commission's budget is not large enough to support every activity that would be desirable. With respect to the enforcement division in particular, in 1975 the Legislature deleted from the Governor's budget supplemental funds

^{2/} See, for example, Sections 2.1, 6.1, 9.1 and 10.1.

^{3/} See, for example, Sections 2.4, 7.3 and 9.3.

^{4/} See, for example, Sections 1.9, 2.3 and 6.3.

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Page Three

to hire two additional investigators. Had those funds not been deleted, there would be no backlog of cases today. Correctly, in our opinion, Section 1.7 of the Anderson report states that the backlog can be reduced only if the Legislature provides the Commission with additional staffing resources.

In the absence of adequate resources, our enforcement division has had to establish priorities and strictly focus its activities. Our highest priority has been and will continue to be the most serious violations. This does not mean that the more routine cases are unimportant or have been ignored. To the contrary, such cases must be followed up to discourage future violations and as a matter of fairness to the vast majority who have complied with the law. As a matter of priorities, however, it has seemed clear to us that we must place the most serious violations above all others. The Commission, for instance, has devoted very substantial resources to investigations involving Proposition 13 (Greyhound Racing Initiative), which resulted in a \$1 million lawsuit; the Robert Mendelsohn campaign matter, which is still pending but has been publicized because of court proceedings; and other matters that have not yet been made public. We believe neither the purposes of the Political Reform Act nor simple justice would be served if inadvertent and routine violators were punished while the Commission failed to investigate serious improprieties.^{5/}

The enforcement division's emphasis on the most serious cases has not caused us to ignore the more routine matters. The Arthur Andersen report indicates that 186 complaints that have been received by the enforcement division (Section 1.3) and 32 audit reports have been preliminarily categorized as involving substantial noncompliance (Section 1.5). The enforcement division has therefore received a total of 218 "cases." Of these, 145 have been investigated and appropriate action has been taken. Seventy-three matters are pending, including 31 of the audit report violations. While the present backlog is probably tolerable, we would

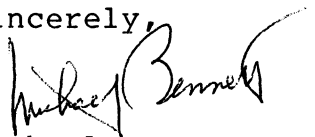
^{5/} Of course, it is not the purpose of this letter to comment on the merits of the cases mentioned. It is sufficient that those matters involve at least a possibility of serious improprieties.

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August 11, 1977
Page Four

prefer that we had been provided with the funds for additional investigators so that no backlog would exist. A far more serious problem will arise if, as the report predicts in Section 1.7, the caseload increases dramatically in the next two years. In that event, our backlog would likely get out of hand. We believe the report's conclusions are sound, and we anticipate that we will follow its recommendation and seek supplemental funds from the Legislature for additional staff for our enforcement division.

In conclusion, we are very proud of the Commission's record over the last two-and-a-half years. We welcome this report because it confirms our feeling of pride and because its recommendations will help us to do an even better job in the future.

Sincerely,

A handwritten signature in cursive script, appearing to read "Michael Bennett". The signature is written in dark ink and is positioned above the typed name.

Michael Bennett
Executive Director

MB:plh

NOTE: Because of the time limitations imposed by the Joint Legislative Audit Committee, it has not been possible for us to seek approval of this letter from the Fair Political Practices Commission. Accordingly, the views expressed are those of the staff.

STATE OF CALIFORNIA



OFFICE OF THE ATTORNEY GENERAL

Department of Justice

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August 10, 1977

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DIVISION OF SPECIAL OPERATIONS
ELIZABETH PALMER
CHIEF ASSISTANT ATTORNEY GENERAL
DIVISION OF CIVIL LAW
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CHIEF ASSISTANT ATTORNEY GENERAL
DIVISION OF CRIMINAL LAW

Honorable John H. Williams
Auditor General
925 L Street, Suite 950
Sacramento, California 95814

Dear Mr. Williams:

The Attorney General's Office has reviewed the audit of the Political Reform Act of 1974 produced for the Auditor General by Arthur Anderson, Inc. The report is composed of two findings and two recommendations.

With respect to the first finding which states that "[n]o formal policies exist for determining when criminal investigation and enforcement action should be initiated" and the first recommendation wherein it is suggested that the Attorney General "[d]evelop written policies for reviewing audit reports and following up on possible violations," we submit that formal policies, although unwritten, do exist which are consistent with the guidelines applicable to all criminal investigations performed by a prosecutor. The issues of intent, motive, past record, sophistication of the participants and others which vary with each case are analyzed during the process of a complete investigation. The American Bar Association Standards on the Prosecution Function has set forth criteria regarding the decision to prosecute which are applicable to the Political Reform Act and are followed by the Attorney General. First, our office determines whether the evidence available will convince the trier of fact of each element of the offense charged beyond a reasonable doubt. Second, even in cases where the evidence would support a conviction, our office may decline to prosecute because of such factors as (a) the minimal harm caused by the offense, (b) the cooperation of the accused in the apprehension or conviction of others, and (c) the availability and likelihood of prosecution by another, such as a district attorney or the Fair Political Practices Commission. In summary, the first recommendation that written policies be developed is impractical and unnecessary.

With respect to the second finding that "[t]he Attorney General has not conducted any prosecution for criminal violations of the Act," it should be emphasized that the report does not question the validity of the decisions not to prosecute criminally in any particular case. Likewise, district attorneys have prosecuted criminally and the Fair Political Practices Commission has initiated administrative and civil actions on cases originally investigated and referred by the Attorney General. It should be noted that the Attorney General has informally agreed with district attorneys that we will conduct statewide campaign prosecutions and they will investigate and prosecute city and county election violations.


August 10, 1977

With respect to the second recommendation that the Attorney General "[i]ncrease enforcement investigation and prosecution activity," The Attorney General firmly believes that the audit review and investigations have been accurate and competent in their results. The Political Reform Act is being enforced consistently with the intentions of the voters of the State of California who passed the initiative in June 1974, and with policy applicable to all criminal investigations conducted by the Attorney General.

It is correct that the number of reporting discrepancies and investigations has resulted in greater expenditure of attorney time than anticipated. However, these activities are only part of the Department's Political Reform Act workload. At such time that the total workload significantly exceeds the staff budgeted for this purpose, the Department will address any need for additional staff through the normal budget process.

In conclusion, the Attorney General's Office has enforced the Political Reform Act in the public interest whether that be by current investigations which may result in criminal prosecutions, referrals to local jurisdictions or other state agencies for appropriate disposition, concluding that no enforcement action is justified, or written communication educating those being audited by the Franchise Tax Board in order to prevent serious violations in the future.

Sincerely,



CHARLES A. BARRETT
Chief Deputy Attorney General

emm

Memorandum

To : John H. Williams, Auditor General
Joint Legislative Audit Committee
925 L Street, Suite 750
Sacramento, CA 95814

Date : August 11, 1977

File No.:

From : Martin Huff

Subject: Report No. 704.1
Efficiency, Economy, and Effectiveness Audit of
State Agency Responsibilities as Specified by
the Political Reform Act

Our comments are restricted to Sections 3-5 (pp 15-31).

Recommendation 3.7, page 17 - Introduce randomness in the audit selection process.

We do not disagree with this recommendation, but it is fraught with political hazards. Our principal concern would be that whatever method was selected be eminently fair to all concerned participants, and that the procedures be specifically spelled out in the law so that both the reality and perception of fairness would be clear and undisputed.

Recommendation 3.8, page 19 - Increase the statute of limitations.

Concur.

Recommendation 3.9, page 19 - Audit candidates and their committees at the same time.

Concur.

Finding 4.1, page 21a (Exhibit C)

This exhibit intends to show a comparison of actual audit workload estimates. Actually it compares estimates of mandatory workload arising during the year with the number of audit cases actually closed during the year.

On the line for "Actual FTB Experience", the figures for "Number of Audits Per Year " (1,178) and "Average Number of Audits Per Auditor" (22.2) are understated and misleading. Both figures are based upon audits actually completed during the 1976-77 fiscal year and do not recognize work-in-process. At the close of the fiscal year, 275 1976 campaign audits, averaging 80 hours, were completed or nearing

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completion. At the beginning of the fiscal year, the work-in-process was primarily 448 lobbyist audits, averaging 22 hours. Thus, the work-in-process at the close of the year was substantially greater than at the beginning.

Recommendation 4.4, page 22 - Finalize development of a workload estimating technique.

Concur in principle as to desired end result. We have been laboring in this vineyard since the beginning. We are barely in to the first campaign cycle, so experience to date in this area is limited. Recommendation is a statement of the obvious, but is premature. We would welcome specific suggestions in this area and we note their absence in this report.

Recommendation 4.5, page 23 - Estimate personnel resources over a four-year time frame, based on projected workload estimates.

Concur.

Recommendation 4.6, page 23 - Budget in accordance with the yearly workloads, and allow the FTB to borrow and lend staff between years to reduce the need to smooth the audit workload.

Although some borrow and loan of staff is desirable, the primary emphasis should be on smoothing the workload. Extreme fluctuations such as those shown on Exhibit E, page 24a, from a low of 13 to a high of 68 or from 9 to 55 will result in a substantial increase in training and a corresponding decrease in efficiency and effectiveness. For best results, both extension of the statute of limitations and increased ability to borrow and loan are needed.

Recommendation 4.7, page 24 - Adjust FTB staffing based on changes in audit workload.

The caption is a statement of the obvious, but the supporting detail is only a discussion with no substance.

Recommendation 5.7, page 28 - Reduce the elapsed time required to complete audits.

The eight-month average elapsed time is misleading since it relates to physical location of the audit file in a field office, rather than actual time assigned to an auditor. In practice, a small number of audits are

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assigned to each auditor at frequent intervals. Each field office should continue to receive their workload at an early date to facilitate planning within that office.

Recommendation 5.8, page 29 - Increase field involvement by supervisory personnel on large audits.

The audit supervisor is responsible for a group of 5 to 6 auditors and is not utilized as a lead auditor. Although a limited amount of time in the field is currently encourage and practiced, any significant increase will require a substantial reduction in the ratio of auditors to supervisors. The consultants performing this study indicated a ratio of 3 to 1 might be appropriate. We do not concur.

Recommendation 5.9, pages 29-30 - Develop detailed field audit plans for large audits.

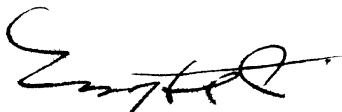
The range of average audit hours is from 10 to 120 (Exhibit G, page 24c); we anticipate few large audits of 500 or more hours. Seven audits of this size have been conducted to date and five were assigned by the supervisor to more than one auditor.

Recommendation 5.10, page 30 - Develop documentation for materiality decisions.

Materiality decisions with general application are routinely communicated to the entire audit staff via the file of Policy Statements referred to in Section 5.3. It should be recognized that the audit program is still in its first four-year cycle and the first campaign audits are just now under way. The number of Policy Statements can be expected to grow as new issues are developed during current and future audits.

Summary

The report is interesting, but contributes nothing new to our body of knowledge. The few specific, substantive recommendations in our area of the report mirror our own prior views. We recommend that a more detailed and comprehensive review be initiated after the first full four-year audit cycle has been completed in 1980.



Executive Officer

cc: Arthur Andersen & Co.



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POLITICAL REFORM DIVISION
(916) 322-4880

August 11, 1977

Mr. John H. Williams
Auditor General
925 L Street, Suite 750
Sacramento, CA 95814

Dear Mr. Williams:

The following comments are submitted in response to findings and recommendations pertaining to this office contained in Report Number 704.1 entitled, "Efficiency, Economy, and Effectiveness Audit of State Agency Responsibilities as Specified by the Political Reform Act."

Filing System (Items 11.1 and 11.4)

Control of documents filed exists. Upon receipt, documents received are logged before any photocopying, evaluation, or further processing occurs. Mail is opened, stamped received, segregated and immediately logged. Information logged upon receipt is used as the control feature for internal file maintenance. Further control in the movement of documents through processing points is not employed. All documents are retained in a work area of three adjacent rooms. Totals of documents processed or evaluated are maintained for workload and workflow monitoring purposes.

Periodic file maintenance includes reconciling the respective logs to documents on file. The Franchise Tax Board periodically has been provided computer listings of documents filed and, if requested, could be provided an additional means of document control by reconciling their files to copies of manually maintained logs.

At this time, revisions of the existing system are being considered in anticipation of a microfilm and computer-generated index capability.

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Inquiries Regarding the Act (Items 11.2 and 11.5)

Callers asking interpretive questions are transferred to the Technical Assistance and Analysis Division of the Fair Political Practices Commission unless the question is clearly answered by statute or a manual issued by the Commission. Questions and responses of materiality or substance are recorded on a "Telephone Information Record" and, in some instances, a letter of confirmation. These records are retained in the file of the respective entities or the miscellaneous phone record file if the person requesting information has not filed with this office. For statistical purposes, calls concerning general information are logged.

Late Filing Liabilities (Items 11.3 and 11.6)

Discretion in waiving liabilities incurred has been exercised based on an individual review of an explanation submitted by the filer under penalty of perjury. That procedure and criteria are formally established and documented for office use. The procedure of using the waiver request form together with the notice of liability due for late filings has been determined to be the most cost-effective technique. The elements of limited discretion in waiving liabilities are clear in the notice and request. Discretion is exercised in only those cases of eligibility based on response to nonfiling notices.

Sincerely,

WILLIAM N. DURLEY
Assistant to the Secretary of State
Elections and Political Reform



DAVID B. PITMAN, Manager
Political Reform Division

Office of the Auditor General

cc: Members of the Legislature
Office of the Governor
Office of the Lieutenant Governor
Secretary of State
State Controller
State Treasurer
Legislative Analyst
Director of Finance
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
California State Department Heads
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