

# California Legislature

## SENATE COMMITTEE ON ELECTIONS AND CONSTITUTIONAL AMENDMENTS

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### Oversight Hearing: Status of Lobbyist Audits – Franchise Tax Board

#### HEARING BACKGROUND

##### History of the Political Reform Act of 1974

In June 1974, California voters passed Proposition 9, an initiative commonly known as the Political Reform Act of 1974 (PRA). Proposition 9 codified significant restrictions and prohibitions on candidates, officeholders, and lobbyists. In the aftermath of the Watergate scandal, California was the first state to pass a comprehensive political reform package. The initiative was championed by a coalition consisting of then-Secretary of State Jerry Brown, the People's Lobby, and Common Cause. By including provisions regulating campaign finance, lobbying activity, and conflicts of interest, California's Proposition 9 represented the most significant response to the concerns about corruption and conflicts of interests following Watergate.

The PRA requires detailed disclosure of the role of money in California politics. This includes the disclosure of contributions and expenditures in connection with campaigns supporting or opposing state and local candidates and ballot measures, as well as the disclosure of expenditures made in connection with lobbying the Legislature and attempting to influence administrative decisions of state government.

As enacted in 1974, the PRA consisted of six main provisions. Among these provisions, the PRA imposed restrictions on lobbyists and required lobbyists to register with the state and to file reports disclosing their activity expenses. Additionally, the PRA imposed a \$10 gift limit on lobbyists and prohibited lobbyists from making contributions.

The original provisions also created the Fair Political Practices Commission (FPPC), an independent centralized authority to secure compliance with the PRA. Prior to the PRA, no systematic method existed to determine whether a candidate, committee, or lobbyist reported all contributions and expenditures.

## **PRA Shared Administrative Responsibilities**

The PRA shared administrative responsibilities between the FPPC, the Secretary of State (SOS), and the FTB.

The FPPC reports on the money spent in California political campaigns. The reports list the offices, candidates, and amount of increased historical spending and raised monies of the political campaigns. The FPPC selects a pool of entities and candidates that are subject to audit and notifies FTB of the candidate pool. Pursuant to the PRA, the FTB is required to make audits and field investigations for the reports and statements filed with the SOS and for local candidates and their controlled committees. The PRA also requires that each lobbying firm and each lobbyist employer who employs one or more lobbyists is subject to an audit on a random basis with a 25-percent chance of being audited. In other words, 25 percent of lobbying firms and lobbyist employers are required by law to be audited. When a lobbying firm or lobbyist employer is audited, the individual lobbyists who are employed by the lobbying firm or the lobbyist employer are also audited. For lobbying firm and lobbyist employer audits, the selection is made in public in February of odd-numbered years.

The SOS Political Reform Division administers provisions of the PRA which require the disclosure of financial activities related to political campaigns and lobbying. Specifically, activities related to lobbying include:

- Provides records of FTB's submittal of audit reports on its website.
- Registers lobbying firms and lobbyist employers that make expenditures to lobby California State government.
- Receives lobbying disclosure statements filed by lobbyists, lobbyist employers, and lobbying firms. Additionally, these statements are filed electronically or online and posted online.
- Provides technical assistance regarding lobbying disclosure provisions of the PRA to lobbyists, lobbying firms, lobbyist employers, and the public.
- Reviews lobbying documents to ensure compliance with reporting requirements.
- Provides public access to all lobbying disclosure filings
- Publishes a lobbying directory to help identify the people, organizations, and firms that have registered with the SOS to lobby the Legislature and California State government.
- Determines if lobbying documents have been filed on time and imposes and collects fines for late filings.

The FTB has administered the Political Reform Audit Program since the passage of the PRA. FTB's audit program is required under the PRA. There are 17 different types of workload and each has separate conditions for determining which entities are required to be audited. The workload relevant to this hearing includes audits on lobbying firms and lobbyist employers which employ one or more lobbyists.

The PRA requires that audits be performed by professionals with specialized technical training and proficiency and the FTB has noted the need for various enhancements to ensure sufficient resources are available to administer the Political Reform Audit Program. Once the FPPC has identified a pool of candidates for audit, the Political Reform Audit Program is responsible for identifying whether the audit is mandated for each entity based on criteria detailed in existing law.

### **What's Happening with Audits?**

The PRA has had numerous legislative and regulatory changes in its 45-year history. Each change has brought additional layers of complexity. The sophistication of filings continue to increase the complexity of the political audits and require increased skill sets by Political Reform Audit Program staff. Since 1974, the number of registered lobbying firms, lobbyist employers, and individual lobbyists has grown significantly.

According to the FTB, their Political Reform Audit Program is responsible for auditing a variety of mandated workloads, including lobbying firms and lobbyist employers. The Political Reform Audit Program has resource deficiencies that impact FTB's ability to complete these audits, as well as all other mandated workloads. FTB continues to work with their external stakeholders to solicit additional resources.

The SOS provides online records of FTB yearly submittal of audit reports from January 31, 2014 through January 31, 2023, to the FPPC, the SOS, and the Attorney General. A committee staff review of the audits submitted for this ten-year period indicates that the audits are predominantly related to campaigns and include a relatively small number of lobbyist employers and lobbying firms.

On February 8, 2023, the FPPC conducted two drawings. One drawing selected lobbyist employers for audit. Another drawing selected lobbying firms for audit. Both audits required include audits of their individual lobbyists. As a result, 192 lobbyist employers were selected for audit in 2023 for all reports filed in 2021 and 2022. Additionally, 114 lobbying firms and individual lobbyists employed by the lobbying firm were selected for audit in 2023 for all reports filed for 2021 and 2022.

Below is a table containing the total of randomly selected lobbying firms and lobbyist employers, the number of FTB audits conducted, and the percent of audits when compared to the total number of lobbying firms and lobbyist employers.

## Lobbying Firms and Lobbyist Employers

Year*	Drawn by FPPC (25% of Lobbying Firms / 25% of Lobbyist Employers)	Total (Lobbying Firms + Lobbyist Employers)	FTB/SOS Audits**	Percent of Total (25% Required)***
2013-14	121 / 183	1,215	36 / 29	2.96% / 2.24%
2015-16	116 / 198	1,255	27 / 30	2.15% / 2.39%
2017-18	119 / 192	1,243	0 / 0	0 / 0
2019-20	118 / 189	1,226	4 / 0	0.33% / 0
2021-22	114 / 192	1,223	Pending	Pending

\*The FPPC does their random drawing (i.e. "Drawn by FPPC") in the year following each session. For example, the random drawing for lobbying firms and lobbyist employers in 2013-14 took place in 2015.

\*\*Even though the FTB performed their audits beginning in the year following each two-year session, the number of completed audits (i.e. "FTB Audits") is contained within the two-year session being audited.

\*\*\*Both FTB and SOS audit numbers and calculated percentages are included and reflect minor discrepancies.

The FTB Political Reform Audit Program audits the entities in order of the draw within their resource constraints. According to FTB, in 2015, 19 lobbying firms and 17 lobbyist employers were audited. In 2017, 13 lobbying firms and 14 lobbyist employers were audited. In 2019, FTB did not complete any audits of lobbying firms and lobbyist employers due to a lack of resources. Finally, in 2021, two lobbying firms and two lobbyist employers were audited.

According to the SOS, for audits conducted in 2013-14 and reported in 2015, 15 lobbying firms and 14 lobbyist employers were completed. For audits conducted in 2015-16 and reported in 2016, one lobbying firm and two lobbyist employers were completed. For audits conducted in 2015-16 and reported in 2017, 13 lobbying firms and 14 lobbyist employers were completed. The SOS noted that no audits were reported after 2017. The SOS posts these summaries on their political reform division's website.

### The Problem

Based upon current FTB funding levels (and allocation of those funds), most of the recently selected lobbying firms, lobbyist employers, and their individual lobbyists are not being audited. If the purpose of the conducting random audits is to ensure compliance with the PRA, then the lack of auditing poses significant challenges to the PRA's effectiveness.

Committee staff requested information regarding the enforcement actions that have been taken place as a result of audits submitted to the FPPC and no information has been received as of this printing.

Committee staff also requested information on FTB's budget as it relates to audits required by the PRA and the amount that currently is being spent to conduct the Political Reform Audit Program. As of this printing, no information has been received. Additionally, the breakdown of expenditures between campaign audits and lobbying audits is unknown. As previously mentioned, audits submitted over a ten-year period show a predominance of campaign audits versus a small number of lobbying audits.