



FEDERAL ELECTION COMMISSION  
WASHINGTON, D.C. 20463

SECRETARIA

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MAY 30, 2007

**MEMORANDUM**

TO: The Commission

FROM: Thomasenia P. Duncan *JPD*  
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SUBJECT: Supplemental Submission from Kerry-Edwards 2004, Inc. and Kerry-Edwards  
2004 Inc. General Election Legal and Accounting Compliance Fund (LRA # 658)

**AGENDA ITEM**  
For Meeting of: 05-31-07

**SUBMITTED LATE**

The Audit Report on Kerry-Edwards 2004, Inc. (the "General Committee") and Kerry-Edwards 2004 Inc. General Election Legal and Accounting Compliance Fund is on the Commission's open session agenda for Thursday, May 31, 2007. The General Committee responded to the Preliminary Audit Report ("PAR") on December 22, 2006. On May 24, 2007, the General Committee made a supplemental submission, addressing two issues in the draft Audit Report. The Office of General Counsel recommends that the Commission not consider this supplemental submission.

A candidate and his authorized committee may submit in writing within 60 calendar days after receipt of the preliminary audit report, legal and factual materials disputing or commenting on the proposed findings. 11 C.F.R. § 9007.1(c)(2). Generally, the Commission will not consider any arguments that are raised after 60 days. *See Americans for Robertson v. Federal Election Commission*, 45 F.3d 486 (D.D.C. 1995). If 60 days has expired and the arguments relate to a repayment determination, then a committee may raise the issue by seeking an administrative review of the repayment determination. 11 C.F.R. § 9007.2(c)(2).

The General Committee asserts that the Commission should consider its supplemental submission because the draft Audit Report introduces new legal standards that were not included in the PAR and other issues not included in the PAR. In fact, however, the Committee is continuing to contest the attribution to the expenditure limitation of airplane reconfiguration expenses and a \$100,000 payment to Riverfront Media, which had been included in the PAR finding and calculations. The General Committee first objects to references in the draft Audit Report to Generally Accepted Accounting Principles ("GAAP"). The PAR had cited one source as an example of the broader application of GAAP in the valuation of capital assets. In the draft Audit Report, the auditors added citations to additional sources, again as examples of GAAP being applied or explained. The underlying principle was present in the PAR and additional citations and examples do not make it somehow new. Second, the General Committee addresses the attribution of a \$100,000 payment to Riverfront Media as an operating expense rather than as a winding down cost. Although the Committee correctly notes that this expense was not specifically discussed in the PAR, the amount had been included in the calculation of expenditures subject to the limitations in the PAR. The Committee was fully aware of this issue because it addressed it in its December 22, 2006 response to the PAR: "The Audit staff attributes to the Committee, rather than the GELAC, a \$100,000 payment to Riverfront Media, which was for the purpose of compliance and consulting in connection with the audit." PAR Response at 1.

Both issues the General Committee raises relate to the Audit staff's finding that the General Committee incurred expenditures in excess of its expenditure limitation and recommendation that the Commission determine that the Committee must make a repayment to the United States Treasury of \$1,344,082, the amount in excess of the limitation. *See* 2 U.S.C. § 441a(b)(1) and (c); 26 U.S.C. § 9007(b)(2). The General Committee has already had the opportunity to respond to this finding and submit its analysis of the attribution of these particular expenses in the PAR, and it has done so. The 60-day period for responding to the PAR has expired. 11 C.F.R. § 9007.1(c)(2). This untimely additional submission seeks to make additional arguments about expenses the General Committee has already contested. There is no new repayment determination or finding in the Audit Report, and these expenses were included in the expenditure limitation calculation in the PAR. Therefore, there is no need to give the Committee another opportunity to present new or different arguments.

This Office's recommendation does not mean the Commission will never consider the General Committee's arguments delineated in the supplemental submission. Our position simply means that the Commission should move toward closure of the Audit Report stage of the repayment process. The Committee may raise these arguments if it chooses to seek administrative review of the repayment determination. 11 C.F.R. § 9007.2(c)(2).

## **RECOMMENDATION**

The Office of General Counsel recommends that the Commission not consider this supplemental submission from Kerry-Edwards 2004, Inc. and Kerry-Edwards 2004 Inc. General Election Legal and Accounting Compliance Fund dated May 24, 2007.

Memorandum to the Commission  
Kerry-Edwards 2004, Inc. and Kerry-Edwards 2004 Inc.  
General Election Legal and Accounting Compliance Fund  
(LRA # 658)  
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**Attachment**

Supplemental submission from Kerry-Edwards 2004, Inc. and Kerry-Edwards 2004 Inc.  
General Election Legal and Accounting Compliance Fund dated May 24, 2007.

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May 24, 2007

Dear Ms. Dove:

We write on behalf of Kerry-Edwards 2004, Inc. (the "Committee"). On Friday, May 18, 2007, the Committee received the draft Final Audit Report (the "draft FAR"), now labeled Agenda Document 07-37, which the Commission is to consider at its May 31 meeting.

The draft FAR raises a number of significant concerns; this letter is intended to narrowly address two issues that raise not only substantive concerns, but also procedural concerns about the manner in which information is presented to the Commission.<sup>1</sup> The draft FAR introduces references to new "Legal Standards" that were not included in the Preliminary Audit Report (the "PAR") or raised earlier in the audit process (*See I, supra*), and it raises other issues not included in the PAR (*See II, supra*). Because these issues were not raised in the PAR, we submit this letter for the Commission's consideration. *See* Memorandum to the Commission from the Office of General Counsel regarding Report of the Audit Division on Gephardt for President, Inc. at 2, Agenda Document No. 07-39 (May 22, 2007) (permitting the committee to provide a supplemental response to issues not raised in the PAR).

The Commission has, in the past, declined to apply new legal standards in the midst of conducting a presidential audit, out of concern for procedural infirmities that arise from doing so. *See* Statement of Reasons of Commissioners Elliott, Mason, Sandstrom and Wold on the Dole/Clinton Audits, June 24, 1999 ("[T]he regulated community most likely does not have notice as to how this standard will govern its conduct, and it certainly did not have an opportunity to comment on whether it should"). The Commission should not abandon this approach in favor of the one urged by the Audit Division, to argue for any interpretation, however strained, that results in a "finding" and a requirement for repayment.

#### **I. Sale of Assets from Primary Committee to the Committee (Finding 2)**

In its response to the PAR, the Committee objected to the Audit Division's reliance on the Federal Accounting Standards Advisory Board's Statement of Federal Financial Accounting Standards

<sup>1</sup> Issues not addressed in this letter were addressed in the Committee's response to the PAR, and the Committee continues to urge the Commission to reject the auditors' findings on the basis set forth therein.

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No. 6 (Accounting for Property, Plant, and Equipment), on the grounds that it is inapplicable to the Committee. *See* Committee's Response to PAR at 11-19. In the draft FAR, one of the new Legal Standards now offered under Finding 2, in connection with the dispute over the valuation of plane assets, is Generally Accepted Accounting Principles (GAAP), as stated on p. 376 of Barry J. Epstein, Ralph Nach, Steven M. Bragg, Wiley GAAP 2007 Interpretation and Application of Generally Accepted Accounting Principles. Draft FAR at 13. Similarly, the draft FAR's discussion of the valuation of plane assets cites to the following texts: J. David Spiceland, James F. Sepe, Lawrence A. Tomassini, Intermediate Accounting, 4th ed., vol. 1, New York: The McGraw-Hill Companies, Inc., 2007, 455; Barry J. Epstein, Ralph Nach, Steven M. Bragg, Wiley GAAP 2006 Interpretation and Application of Generally Accepted Accounting Principles. Hoboken, NJ: John Wiley & Sons, Inc., 2005, 340. Draft FAR at 18.

No reference to GAAP or any of these "Legal Standards" appeared in the PAR's "Legal Standards" section or anywhere else in the PAR. They were published after the 2004 election. Yet even assuming for the moment that the 2004 editions of these texts were identical to the later editions (like the Audit Division, we have yet to locate the 2004 editions), there is no indication the Commission has adopted these accounting standards, and made them controlling authority, when valuing property that is sold from a primary committee to a general committee under 11 C.F.R. § 9004.9(d)(1)(i)-(ii).

Equally unpersuasive is the Office of General Counsel's analysis of GAAP. It suggests that this section of the draft FAR be revised to clarify that "citations to specific accounting standards are intended to provide non-exclusive examples of generally accepted audit principle (GAAP) that can also be found in many other sources." Memorandum to Joseph F. Stolz from the Office of General Counsel at 5, Agenda Document No. 07-39 (May 22, 2007). Again, there is the absence of a link between GAAP and the Commission's regulations, or even an explanation of how the Commission's policy goals are furthered by importing GAAP in this context. It is telling that there was no concern raised by the Office of General Counsel about citing to textbooks published after the regulated activity took place. Glaringly absent is any acknowledgment that citing to GAAP and textbooks in this fashion calls into question a fundamental duty of the Commission, as a federal agency: to establish legal standards prospectively, not retroactively.

Certainly, if the Commission wanted to require its regulated community to adhere to GAAP – similar to the way the Securities and Exchange Commission requires publicly traded companies to adhere to GAAP in their final statements – it could seek the necessary regulatory changes to implement such a system. The Commission has not; FEC reports, for example, do not comply with GAAP.

As noted, the Commission has previously and clearly stated its expectations that audit issues would not be resolved against committees, if liability depended on new legal standards and, therefore, on the generation of procedural infirmities. *See* Statement of Reasons of Commissioners Elliott, Mason, Sandstrom and Wold on the Dole/Clinton Audits, June 24, 1999

("[T]he regulated community most likely does not have *notice* as to how this standard will govern its conduct, and it certainly did not have an opportunity to *comment* on whether it should"); *see also* Final Audit Report of Bush-Cheney 2000 at 6-7 (discussion of allocation of phone bank costs) and Final Audit Report of Bush-Cheney '04 at 4-7 (discussion of payment for private aircraft). The Commission should continue to respect due process in this presidential audit as well, and should affirm that the Committee's interpretation of 11 C.F.R. § 9004.9(d)(1)(i)-(ii), given the Commission authority available at the time, was reasonable. Should the Commission choose to require adherence to GAAP in this context in the future, such a decision should be made through the proper regulatory procedures.

## II. \$100,000 Payment to Riverfront for Wind-Down Costs (Finding 2)

The Committee paid its media buyer, Riverfront, \$100,000 for recordkeeping and reconciliation work that it performed after the expenditure report period. The Audit Division contends that the work performed by Riverfront during this period should be treated as an operating expense of the Committee, and should be paid for with public funds, not GELAC funds. The PAR contained no explanation of this important issue; it merely improperly included this dollar amount in the calculation of the Committee's expenditures subject to limitation.

The draft FAR's explanation of why these costs do not qualify as winding down costs, if accepted, would eviscerate the definition of winding down costs:<sup>2</sup>

[C]osts incurred for reconciliation of media buys, calculations of commissions earned, collection of affidavits relating to media buys and application of refunds, all relate to activities that occurred during the campaign; normal operating expenditures that are subject to the limitation.

Draft FAR at 25. Of course these activities "relate to activities that occurred during the campaign." If they did not, they would not qualify as winding down costs. But the work was performed – as the Audit Division is aware from first-hand knowledge, and from Riverfront's records of its staff time and resources devoted to this audit that were previously provided to the Audit Division – for these wind-down activities after the expenditure report period. The Committee cannot conceive of what possible policy goal is furthered by preventing the

<sup>2</sup> Commission regulations permit GELAC funds to be used "[t]o defray winding down expenses for legal and accounting compliance activities incurred after the end of the expenditure report period by either the candidate's primary election committee, general election committee, or both committees." 11 C.F.R. § 9003.3(a)(2)(I). "Winding down costs" for a publicly funded general committee are defined as "costs associated with the termination of the candidate's general election campaign such as complying with the post-election requirements of the Federal Election Campaign Act and the Presidential Election Campaign Fund Act, and other necessary administrative costs associated with ending the campaign, including office space rental, staff salaries, and office supplies." 11 C.F.R. § 9004.11(a).

Committee from compensating a vendor for the time it devotes to recordkeeping and other compliance issues during the winding down of the Committee.

There also appears to be confusion from the Audit Division about the payment of \$100,000 in October 2006 to Riverfront for audit services. *See* Draft FAR at 25. It is the same \$100,000 at issue. Payment to Riverfront was delayed until then because the document and spreadsheet requests to Riverfront that arose from the Audit Division extended far longer than expected.

It is unclear whether the Office of General Counsel supports the Audit Division's position. On the one hand, the Audit Division's cover memo to the draft FAR states: With respect to the matters addressed in the Report, the Audit Division and the Counsel's office are in agreement. Counsel's recommended changes have been made." *See* Memorandum, dated May 21, 2007, from the Audit Division to the Commission. On the other hand, the Office of General Counsel's memorandum on the draft FAR states: "The expenses for activity between the election and November 2005 may be winding down costs. If the Audit Division believes they are not, the auditors should more fully explain why these expenses are not winding down costs." Memorandum to Joseph F. Stolz from the Office of General Counsel at 6, Agenda Document No. 07-37 (May 22, 2007).

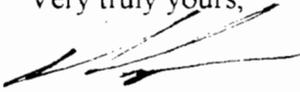
The Commission has previously shown deference to a presidential committee's decisions regarding winding down costs, even when leftover public funds were used to pay such expenses. *See* Final Audit Report on Gore/Lieberman, Inc. and Gore/Lieberman GELAC. Here, where the Committee used GELAC funds, not public funds, for winding down costs that demonstrably occurred during the wind-down period, there is no basis for concluding that 11 §§ C.F.R. 9003.3(a)(2)(I) and 9004.11(a) do not permit GELAC to pay for these winding down costs.

Finally, we respectfully request that the Committee's response to the PAR, which has already been submitted to the Commission and a copy of which is attached (without exhibits), be placed on the public record prior to the May 31 open session.

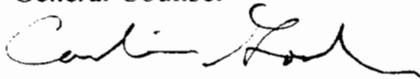
Thank you for your consideration.

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Very truly yours,



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General Counsel



Caroline P. Goodson  
Deputy General Counsel

Kerry-Edwards 2004, Inc. and  
Kerry-Edwards 2004, Inc.  
General Election Legal and Accounting Compliance Fund

cc: Chairman Lenhard  
Vice Chairman Mason  
Commissioner von Spakovsky  
Commissioner Walther  
Commissioner Weintraub  
Mr. Joseph F. Stolz  
Thomasenia Duncan, Esq.