



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

June 15, 2011

MEMORANDUM

To: The Commission

Through: Alec Palmor
Acting Staff Director

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Audit Division

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Lead Auditor

Subject: Preliminary Audit Report - McCain-Palin 2008 Inc. and McCain-Palin
Compliance Fund, Inc.

Attached for your approval is the subject Preliminary Audit Report (PAR). Also attached is the Office of General Counsel (OGC) legal analysis of the PAR (Attachment 1).

In its legal analysis, OGC recommended the Audit Division raise two matters for the Commission's consideration that are not included in the PAR. These two matters are attached to this cover memorandum (Attachment 2- Media Vendor Interest and Hybrid Communications). It is noted that the Commission addressed similar matters in the respective audit reports of the general election candidate committees in the 2004 election cycle. Neither of these matters received the four affirmative votes necessary for a finding and they were presented as "Additional Issues" in the audit reports for the 2004 election cycle.

With respect to the PAR, OGC concurs with the Audit staff's method for billing the Press in Finding 1: Campaign Travel Billing for Press. OGC agrees that the General Committee should refund the amounts of excess reimbursements to the press rather than transferring funds to the candidate's primary election committee. OGC also concurs with the Audit staff's calculation of the amount the media should reimburse to the General Committee for the actual costs of the air charter contract paid for and used by both the primary and general campaigns.

OGC recommended that the Audit staff also raise the issue of aircraft configuration costs to the Commission in this cover memorandum. Specifically, OGC questioned the legal basis for the Audit staff's use of a "reasonable benefit" approach for calculating the plane reconfiguration costs billable to the Press.

The Audit staff analyzed \$650,000 in reconfiguration costs associated with the plane chartered for the Presidential candidate. Originally, the Audit staff determined that the General Committee could include in the actual cost of travel: (1) 100 percent of reconfiguration costs attributable primarily to the convenience and needs of the press; (2) 78 percent, based on the proportion of press passengers to the number of total passengers, of reconfiguration costs attributable to the convenience and needs of all passengers; and (3) zero percent of costs that were allocable only to the convenience and needs of the campaign.

In light of the guidance from OGC with respect to the 78 percent allocation noted above, the Audit staff has revised its calculation for the actual cost of travel that is billable to the Press. The new calculation does not apply the 78 percent allocation to any reconfiguration costs and limits the items not considered billable to the Press to the costs for painting and applying logos totaling \$161,386 and the cost for one divider curtain totaling \$1,167. The new calculation presented in the Preliminary Audit Report of billable reconfiguration costs is \$487,447 (\$650,000-\$161,386-\$1,167). This calculation aligns with the General Committee's opinion expressed in response to the exit conference that costs for painting and applying logos and the cost of one divider are not billable reconfiguration costs. It is also noted that this new calculation resulted in only a \$5,808 adjustment to the amount recommended to be refunded to the Press (\$344,892).

Recommendation

The Audit staff recommends that the report be approved.

This matter is being circulated for a tally vote. If an objection is received, it is requested that this matter be placed on the next Executive Session agenda. If you have any questions, please contact Riokida Mercamb or Thomas Hinternister at (202) 694-1200.

Attachments:

Preliminary Audit Report on McCain-Palin 2008 Inc. and McCain-Palin Compliance Fund, Inc.
Attachment 1- Office of General Counsel Legal Analysis (LRA 759), dated December 1, 2010
Attachment 2- Media Vendor Earned Interest and Hybrid Communications
Attachment 3- Summary of Previous Audits

cc: Office of General Counsel



Preliminary Audit Report on McCain-Palin 2008 Inc. and McCain-Palin Compliance Fund, Inc.

March 24, 2008 - December 31, 2008

Why the Audit Was Done

Federal law requires the Commission to audit every political committee established by a Presidential candidate who receives general funds for the general campaign.¹ The audit determines whether the candidate was entitled to all of the general funds received, whether the campaign used the general funds in accordance with the law, and whether the campaign otherwise complied with the limitations, prohibitions, and disclosure requirements of the election law.

Future Action

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

About the General Committee

McCain-Palin 2008 Inc. (General Committee) is the principal campaign committee for Senator John S. McCain, the Republican Party's nominee for the office of President of the United States. The General Committee is headquartered in Arlington, Virginia. For more information, see chart on Campaign Organization, p. 2.

Financial Activity of the General Committee

• Receipts	
○ Federal Funds Received	\$ 84,103,800
○ Offsets to Operating Expenditures	9,318,570
○ Loans Received	17,076,880
○ Other Receipts	1,154,733
○ Total Receipts	\$ 111,653,983
• Disbursements	
○ Operating Expenditures	\$ 92,083,836
○ Loans Repayment	17,076,880
○ Other Disbursements	1,491,107
○ Total Disbursements	\$ 110,651,823

Findings and Recommendations for the General Committee (p. 5)

- Campaign Travel Billing for Press (Finding 1)
- Expenditure Limitation (Finding 2)

¹ 26 U.S.C. §9007(a).

About the Compliance Fund

The McCain-Palin Compliance Fund, Inc. (Compliance Fund) was established pursuant to 11 CFR §9003.3(a)(1)(i). The Compliance Fund accepts contributions to be used solely for legal and accounting services to ensure compliance with the Federal Election Campaign Act (Act). These contributions include the Compliance Fund's share of contributions from affiliated joint fundraising committees. The Compliance Fund is also headquartered in Arlington, Virginia. An overview of financial activity for the Compliance Fund is presented below.

Financial Activity of the Compliance Fund

• Receipts	
○ Contributions	\$ 9,679,490
○ From Other Authorized Committees	25,046,453
○ Offsets to Operating Expenditures	1,131,139
○ Other Receipts	12,471,782
○ Total Receipts	\$48,328,864
• Disbursements	
○ Operating Expenditures	\$11,675,642
○ All Other Disbursements	13,112,237
○ Total Disbursements	\$24,787,879

Finding and Recommendation for the Compliance Fund (p. 5)

- Failure to File 48-Hour Notices

About Joint Fundraising Committees

This audit included seven joint fundraising committees. Each of the joint fundraising committees is headquartered in Alexandria, Virginia and was an authorized committee of the candidates John McCain and Sarah Palin. The combined financial activity for these joint fundraising committees is presented below and the financial activity for each of these committees is presented on page 4.

Financial Activity of the Joint Fundraising Committees

• Receipts	
○ Contributions	\$ 207,620,125
○ From Other Authorized Committees	812,325
○ Offsets to Operating Expenditures	159,926
○ Total Receipts	\$208,592,376
• Disbursements	
○ Operating Expenditures	\$30,374,903
○ All Other Disbursements	167,116,292
○ Total Disbursements	\$197,491,195

Finding and Recommendation for the Joint Fundraising Committees (p. 5)

Based upon the limited examination of the reports and statements filed, and the records presented by seven joint fundraising committees, the Audit staff did not discover any material non-compliance.

**Preliminary Audit Report on
McCain-Palin 2008 Inc. and
McCain-Palin Compliance Fund,
Inc.**

March 24, 2008 – December 31, 2008



Table of Contents

	Page
Part I. Background	
Authority for Audit	1
Scope of Audit	1
Inventory of Campaign Records	1
Part II. Overview of Campaign	
Campaign Organization	2
Overview of Financial Activity	3
Part III. Summaries	
Findings and Recommendations – General Committee	5
Finding and Recommendation – Compliance Fund	5
Finding and Recommendation – Joint Fundraising Committees	5
Part IV. Findings and Recommendations for the General Committee	
Finding 1. Campaign Travel Billing for Press	6
Finding 2. Expenditure Limitation	14
Part V. Finding and Recommendation for the Compliance Fund	
Failure to File 48-Hour Notices	16
Part VI. Finding and Recommendation for the Joint Fundraising Committees	
Based upon the limited examination of the reports and statements filed and the records presented, the Audit staff discovered no material non-compliance.	18
Part VII. Attachment	
Statement of Net Outstanding Qualified Campaign Expenses	19

Part I

Background

Authority for Audit

This report is based on audits of McCain-Palin 2008 Inc. (General Committee), McCain-Palin Compliance Fund, Inc. (Compliance Fund), and seven joint fundraising committees affiliated with the Compliance Fund, undertaken by the Audit Division of the Federal Election Commission (the Commission) as mandated by Section 9007(a) of Title 26 of the United States Code. That section states that "after each presidential election, the Commission shall conduct a thorough examination and audit of the qualified campaign expenses of the candidates of each political party for President and Vice President." This includes joint fundraising committees authorized by the candidates. Also, Section 9009(b) of Title 26 of the United States Code states, in part, that the Commission may conduct other examinations and audits as it deems necessary.

Scope of Audit

The audits of the General Committee and Compliance Fund examined:

1. The receipt of excessive contributions and loans.
2. The receipt of contributions from prohibited sources.
3. The receipt of transfers from other authorized committees.
4. The disclosure of contributions and transfers received.
5. The disclosure of disbursements, debts and obligations.
6. The recordkeeping process and completeness of records.
7. The consistency between reported figures and bank records.
8. The accuracy of the Statement of Net Outstanding Qualified Campaign Expenses.
9. The campaigns' compliance with spending limitations.
10. Other campaign operations necessary to the review.

The audits of the seven joint fundraising committees affiliated with the Compliance Fund examined:

1. The receipt of excessive contributions and loans pertaining to the Compliance Fund.
2. The proper allocation of contributions among joint fundraising participants.
3. The proper allocation of expenses and net amounts transferred to the Compliance Fund.
4. The consistency between reported figures and bank records.

Inventory of Records

The Audit staff routinely conducts an inventory of campaign records before it begins the audit fieldwork. The records for each of the audited committees were complete and the fieldwork began immediately.

Part II

Overview of Campaign

Campaign Organization

	General Committee	Compliance Fund
Important Dates		
• Date of Registration	08/12/08	02/25/08
• Audit Coverage Dates	09/01/08 thru 12/31/08	03/24/08 thru 12/31/08
Headquarters	Arlington, VA	Arlington, VA
Bank Information		
• Bank Depositories	3	4
• Bank Accounts	8 Bank Accounts	8 Bank Accounts
Treasurer	Salvatore A. Pupura (08/12/08 – 08/18/08); Joseph Schmuckler (08/19/08 – Present)	Salvatore A. Pupura (02/25/08 – 03/20/08); Joseph Schmuckler (03/21/08 – Present)

Joint Fundraising Committees

The audit included seven joint fundraising committees affiliated with the Compliance Fund. Four of the joint fundraising committees registered with the Federal Election Commission in April 2008 and three registered in August 2008. These committees are headquartered in Alexandria, Virginia and Lisa Lisker is the Treasurer for each committee. Six of the joint fundraising committees each maintained a single bank account, and the seventh joint fundraising committee maintained two bank accounts.

Overview of Financial Activity

(Audited Amounts)

	General Committee	Compliance Fund
Opening Cash on Hand	\$0	\$0
Receipts		
• Contributions		\$ 9,679,490
• Federal Funds Received	\$84,103,800	
• From Other Authorized Committees		25,046,453
• Offsets to Operating Expenditures	9,318,570	1,131,139
• Loan Received	17,076,880	
• Other Receipts	1,154,733	12,471,782
Total Receipts	\$111,653,983	\$48,328,864
Disbursements		
• Operating Expenditures	\$92,083,836	\$11,675,642
• Transfers to Other Authorized Committees		222,502
• Loan Repayment	17,076,880	
• Refunds to Contributors		551,599
• Other Disbursements	1,491,107	12,338,136
Total Disbursements	\$110,651,823	\$24,787,879
Closing Cash Balance @12/31/2008	\$1,002,160	\$23,540,985

Overview of Financial Activity

(Audited Amounts)

<u>Joint Fundraising Committees</u>	McCain Victory 2008	McCain Palin Victory 2008	McCain Victory Ohio	McCain Palin Victory Ohio	McCain Victory California	McCain Palin Victory California	McCain Victory Florida
Opening Cash on Hand	\$0	\$0	\$0	\$0	\$0	\$0	\$0
Receipts							
• Individual Contributions	\$76,290,438	\$100,038,158	\$4,462,440	\$1,790,913	\$15,194,747	\$5,175,926	\$3,128,210
• Political Committee Contributions	\$603,884	\$529,183	\$82,850	\$42,000	\$200,795	\$49,581	\$31,000
• Transfers from Other Authorized Committees	\$366,165	\$301,310	\$4,300	\$0	\$77,350	\$40,800	\$22,400
• Offsets	\$14,402	\$102,077	\$100	\$0	\$41,983	\$270	\$1,094
Total Receipts	\$77,274,889	\$100,970,729	\$4,549,690	\$1,832,913	\$15,514,875	\$5,266,576	\$3,182,704
Disbursements							
• Operating Expenditures	\$7,400,078	\$18,983,527	\$499,768	\$283,642	\$1,705,448	\$895,640	\$606,800
• Transfers to Other Authorized Committees	\$66,642,154	\$74,097,252	\$3,597,748	\$1,418,627	\$13,154,796	\$3,871,179	\$2,326,750
• Refunds to Contributors	\$403,974	\$611,376	\$91,285	\$21,200	\$350,951	\$379,600	\$120,900
• Other Disbursements	\$28,500	\$0	\$0	\$0	\$0	\$0	\$0
Total Disbursements	\$74,474,706	\$93,692,155	\$4,188,801	\$1,723,469	\$15,211,195	\$5,146,419	\$3,054,450
Closing Cash Balance @12/31/2008	\$2,800,183	\$7,278,574	\$360,889	\$109,444	\$303,680	\$120,157	\$128,255

Part III

Summaries

General Committee

Finding 1. Campaign Travel Billing for Press

The General Committee apparently received reimbursement from the Press for campaign travel that was above the maximum amount billable to the Press. The Commission's regulations provide that a 10 percent markup on the actual cost of transportation and services may be billed to the Press. The General Committee believes the excess reimbursement from the Press for travel is a misallocation of billing proceeds, requiring the General Committee to pay John McCain 2008, Inc. (the Primary Committee) for the overage collected. The Audit staff recommends the General Committee refund \$344,892 to the Press for reimbursements received in excess of the maximum amount billable. (For more detail, see p. 6.)

Finding 2. Expenditure Limitation

The expenditure limitation for the 2008 general election for the office of President of the United States was \$84,103,800. Based on the Audit staff's review of financial activity through March 31, 2011 and estimated winding down costs, the General Committee has not exceeded the limitation. (For more detail, see p. 14.)

Compliance Fund

Failure to File 48-Hour Notices

The Compliance Fund failed to file 48-hour notices for 169 contributions totaling \$240,700 received prior to the general election. The Audit staff recommends that the Compliance Fund provide evidence that 48-hour notices were timely filed or submit any written comments it considers relevant. (For more detail, see p. 16.)

Joint Fundraising Committees

Based upon the limited examination of the reports and statements filed, and the records presented by seven joint fundraising committees, the Audit staff discovered no material non-compliance. (For more detail, see p. 18.)

Part IV

Findings and Recommendations for the General Committee

Finding 1. Campaign Travel Billing for Press

Summary

The General Committee apparently received reimbursement from the Press for campaign travel that was above the maximum amount billable to the Press. The Commission's regulations provide that a 10 percent markup on the actual cost of transportation and services may be billed to the Press. The General Committee believes the excess reimbursement from the Press for travel is a misallocation of billing proceeds, requiring the General Committee to pay John McCain 2008, Inc. (the Primary Committee) for the overage collected. The Audit staff recommends the General Committee refund \$344,892 to the Press for reimbursements received in excess of the maximum amount billable.

Legal Standard

A. Expenditures for Transportation and Services Made Available to Media Personnel and Secret Service. Expenditures by an authorized committee for transportation, ground services or facilities (including air travel, ground transportation, housing, meals, telephone service and computers) provided to media personnel, Secret Service personnel or national security staff will be considered qualified campaign expenses, and, except for costs relating to Secret Service personnel or national security staff, will be subject to the overall expenditure limitations of 11 CFR 9003.2(a)(1) and (b)(1). 11 CFR §9004.6.

B. Billing Media Personnel for Transportation and Services. The committee shall provide each media representative, no later than 60 days from the campaign travel or event, an itemized bill that specifies the amounts charged for air and ground transportation for each segment of the trip, meals and other billable items specified in the White House Press Corps Travel Policies and Procedures issued by the White House Travel Office. 11 CFR §9004.6(b)(3).

C. Reimbursement Limits for Transportation and Services of Media Personnel. The amount of reimbursement sought from media personnel shall not exceed 110 percent of the media representative pro rata share (or a reasonable estimate of the media representative's pro rata share) of the actual cost of transportation and services made available. Any reimbursement received in excess of this amount shall be returned to the media representative. 11 CFR §9004.6(b) and (d)(1).

D. Pro Rata Share Definition. A media representative's pro rata share shall be calculated by dividing the total actual cost of the transportation and services provided by the total number of individuals to whom transportation and services were made available (to include committee staff, media personnel, Secret Service staff). 11 CFR §9004.6(b)(2).

E. Administrative Costs for Transportation and Services of Media Personnel. The committee may deduct from the amount of expenditures subject to the overall limitation the reimbursements paid by media representatives for transportation and services, up to the actual cost of the transportation and services provided to the media representatives. The committee may deduct an additional amount of the reimbursements received from media representatives, representing the incurred administrative costs of 3 percent. The committee may deduct an amount in excess of 3 percent representing the administrative costs actually incurred by the committee in providing services to the media, provided that the committee is able to document the total amount of administrative costs actually incurred.

For the purposes of the above paragraph, administrative costs include all costs incurred by the committee in making travel arrangements and seeking reimbursement, whether these services are performed by committee staff or independent contractors. 11 CFR §9004.6(c).

F. Attribution of Travel Costs. Expenditures for campaign-related transportation, food and lodging by any individual, including a candidate, shall be attributed according to when the travel occurs. If the travel occurs on or before the date of the candidate's nomination, the cost is a primary election expense. Travel to and from the conventions shall be attributed to the primary election. Travel by a person who is working exclusively on general election campaign preparations shall be considered a general election expense, even if the travel occurs before the candidate's nomination. 11 CFR §9034.4(e)(7).

G. Travel Support Documentation. For each trip, an itinerary shall be prepared and made available by the committee for Commission inspection. The itinerary shall show the time of arrival and departure and the type of events held.

For trips by government conveyance or by charter, a list of all passengers, along with a designation of which passengers are and which are not campaign-related, shall be made available for Commission inspection. When required to be created, a copy of the government's or charter company's official manifest shall also be maintained and made available by the committee. 11 CFR §9004.7(b)(3) and (4).

H. Assets Purchased from the Primary Election Committee. If capital assets are obtained from the candidate's primary election committee, the purchase price shall be considered to be 60 percent of the original cost of such assets to the candidate's primary election committee. 11 CFR §9004.9(d)(1)(ii).

Facts and Analysis

A. Facts

In 2008, the Press covering the campaign of the Presidential candidate (John McCain) and the Vice Presidential candidate (Sarah Palin) travelled predominately on two aircraft chartered by the campaign. The aircraft for the Presidential candidate was the same aircraft used by John McCain 2008, Inc. (the Primary Committee) and was chartered through Swift Air, LLC (Swift Air). The aircraft for the Vice Presidential candidate was chartered through JetBlue Airways Corporation shortly before the Republican National

Convention. The Press also occasionally travelled on aircraft chartered by the General Committee through CSI Aviation Services (CSI) and via ground transportation throughout the campaign.

As cited above, the amount of reimbursement sought from media personnel shall not exceed 110 percent of the media representative's pro rata share (or a reasonable estimate of the media representative's pro rata share) of the actual cost of transportation and services made available. Any reimbursement received in excess of this amount shall be returned to the media representative. 11 CFR §9004.6(b) and (d)(1).

According to the General Committee, it did not receive Press travel reimbursement above the 110 percent allowed by the regulations. The General Committee calculated total transportation costs for the Press to be \$4,501,658. The total billing to the Press equals 106 percent of the cost calculated by the General Committee. The General Committee actually received \$4,476,728 from the Press as reimbursement for travel.

During fieldwork, the Audit staff calculated that the General Committee received Press travel reimbursement in excess of the 110 percent allowed by the regulations. The Audit staff calculated the total pro rata transportation cost for the Press to be \$3,756,215 and a maximum amount billable to the Press (110 percent of cost) of \$4,131,836.² Based on the Audit staff's calculation of transportation costs, the General Committee is required to refund to the Press \$344,892 (\$4,476,728 - \$4,131,836).

The main difference between the General Committee's figure and the Audit staff's figure is the calculation for total transportation costs. The General Committee disagreed with the Audit staff's cost calculation methods with respect to charter flights associated with the aircraft used by the Presidential candidate. The General Committee also did not agree with the Audit staff's initial application of aircraft reconfiguration costs.

The Audit staff calculated transportation costs based on actual hours used only by the General Committee during the general campaign. The General Committee, in contrast, calculated transportation costs based on the life of the charter contract, which covered both the primary and general campaign periods.

Applying Cost on Aircraft for Presidential Candidate

The Primary Committee and the General Committee chartered a Boeing 737-400 from Swift Air for use by the presidential candidate. The Swift Air contract covered the period from June 30, 2008 through November 15, 2008. The contract stipulated payments totaling \$6,384,000 to be paid in 19 weekly installments of \$336,000. The contract covered nine weeks for the Primary Committee and ten weeks for the General Committee. The contract also required the General Committee and Primary Committee to pay costs for fuel, catering, passenger taxes, and ground handling fees. There was also an aircraft reconfiguration cost of \$650,000 that was paid initially by the Primary

² The General Committee billed at 106 percent, but was able to document administrative costs of 110 percent for all modes of transportation. In determining the amount billable to the Press, the Audit staff credited the General Committee for any under billing of the Press associated with any one aircraft or mode of transportation. In other words, any under billing of the Press for travel on the aircraft for the Vice Presidential candidate, CSI chartered aircraft, and ground transportation was applied to any overbilling of the Press that may have occurred for travel on the Presidential aircraft.

Committee. The General Committee correctly reimbursed the Primary Committee \$390,000 (\$650,000 less 40 percent depreciation) for these aircraft reconfiguration costs.

The contract allowed 22.4 flight hours per week, or a total of 425.6 flight hours for the life of the contract. If the full flight hours per week were not flown, the hours rolled over to subsequent week(s). If the contracted 22.4 flight hours per week were exceeded and no accumulated unused hours were available, there was a charge of \$15,000 per additional hour. Neither the Primary nor General Committee ever exceeded the 22.4 flight hours in a week. The General Committee used 140.3 flight hours and the Primary Committee used 111.8 flight hours during the contract.

The General Committee made its first weekly instalment payment of \$336,000 on August 29, 2008, and made total payments of \$4,047,402 to Swift Air. This amount included charges for fuel, catering, passenger taxes, and ground handling fees.

For the first week of the campaign, the General Committee used the total cost of the contract (primary and general) and divided it by the remaining number of hours available under the contract, including unused hours paid for by the Primary Committee. Later weeks were calculated using the amount yet to be paid on the contract and dividing it by the estimated flight hours that would be used in the future, based on weekly averages. The calculation included reconfiguration costs. This method caused a fluctuation of the hourly charter rate calculated from as low as \$11,569 to as high as \$39,715. Using this rate, the segment cost was calculated and divided by the number of passengers.

The Audit staff calculated the charter rate per flight hour for Swift Air by taking the contract weekly installment (\$336,000) and dividing that by the actual weekly hours flown. The cost for fuel, catering, passenger taxes, ground handling, and certain reconfiguration costs were then added to determine the total segment cost. The cost per passenger was then calculated by dividing the total segment cost by the total number of passengers on the segment.

Applying Reconfiguration Costs

The Audit staff and the General Committee did not initially agree on the amount of aircraft reconfiguration costs billable to the Press. Historically, the Commission has allowed the Press to be billed only for the aircraft reconfiguration costs that could be reasonably considered as having benefited the Press. The General Committee believes all costs for reconfiguring an aircraft at the beginning and at the end of the campaign should be considered when calculating the billable amount for the Press. The General Committee also stated that part of the aircraft reconfiguration cost was to bring the aircraft into compliance with FAA safety standards that ultimately benefited the safety of all passengers including the Press.

B. Preliminary Audit Report & Audit Division Recommendation

The issue of press travel reimbursement was presented at the exit conference. In response, the General Committee submitted the following points for the Commission's consideration.

Cost Calculation

The General Committee made a comparison between the Swift Air contract, which spanned both the primary and general election periods, and similar aircraft contracts that were analyzed during previous presidential audits: Dole-Kemp in 1996, Bush-Cheney in 2000, and Kerry-Edwards in 2004. The General Committee specifically referenced the Audit staff's calculation of the hourly rate for each aircraft from the 1996 Dole-Kemp audit, which accumulated all operating costs and divided that total by the actual number of hours flown by each aircraft. By applying the same calculation to the entire amount of the Swift Air contract (\$6,384,000 divided by 252.1 hours flown), the General Committee contends its cost calculations used for billing the Press were accurate.

The Audit staff agrees that when using the *total* Swift Air contract amount for both the primary and general election periods, as well as the full aircraft reconfiguration costs, the General Committee did not receive travel reimbursement from the Press that exceeded the maximum allowed by the regulations. However, as in Dole-Kemp only those costs attributable to the General Committee should be used in determining the travel cost the General Committee may bill to the Press. This conclusion is consistent with travel cost calculations in past presidential audits and supported by 11 CFR §9034.4(e)(7), which states, in part, that expenditures for campaign-related transportation shall be attributed according to when the travel occurs. As in Dole-Kemp, the Audit staff used only the general election operating cost (\$4,047,402) and the actual weekly hours flown by the General Committee when calculating the billable cost to the Press. This is a more appropriate method when calculating costs and billing for campaign travel during the general election period.

The General Committee provided a spreadsheet that spanned the primary and general election periods and relied on adjusting the per hour billing rates on a segment-by-segment basis due to using fewer flight hours than available in the Swift Air contract. The General Committee made the spreadsheet available to demonstrate that the Primary and General Committees' billing allocation was based on total costs (\$6,354,859) that were lower than the contract amount (\$6,384,000). The General Committee contends that no overbilling of the Press could have occurred since the difference (\$29,141) was never billed to the Press by the Primary committee during week eight. However, it appears that the General Committee billed this difference to the Press³. Therefore, the General Committee included the total contract amount in calculating the billing allocation.

The Audit staff used the weekly \$336,000 installment divided by the actual weekly hours flown during the general election period for billing calculations (plus the fuel, catering, taxes, and ground handling fees). The General Committee explained that the Audit staff's calculations had the benefit of hindsight because during the fast pace of the election campaign the actual flying hours were unknown at the time of billing. Therefore, estimates of pro rata share had to be used in order to be in compliance of the regulations to bill media representatives within 60 days of travel. The General

³ During the second week of the general campaign, the General Committee calculated Press billing by using the total cost of the contract (\$6,384,000) and subtracting the amount of the contract already billed (\$2,140,752) to arrive at the remaining balance of the contract. The helicopter cost (\$29,141) was included in the \$2,140,752 already billed. The remaining balance of the contract was then divided by the average estimated flight hours remaining on the contract to determine the adjusted charter rate for the week.

Committee believes the Audit staff's methodology would be in conflict with 11 CFR §9004.6(b)(3), which says, in part, that media representatives should be given a bill that specifies amounts charged for air and ground for each segment.

The Audit staff's methodology does not conflict with 11 C.F.R. §9004.6(b)(3), given that the actual flight hours are known soon after flights occur and thereby falling within the required 60 days to provide the Press an itemized bill that specifies the amounts charged for air transportation for each segment of the trip. It appears the General Committee invoiced the Press on average 12 days after completion of each travel week, allowing time to use the actual flight hours for the week. Other billable travel costs known at the time of billing also could have been added to determine the cost per passenger. This method would incorporate adjusting for weekly flight hours.

The General Committee also referenced the 2000 Bush-Cheney audit and explained that it used the same billing methodology and personnel in that audit, which did not include an adverse audit finding or any informal advice from the Audit staff suggesting a correction to the accounting methods was necessary. The Audit staff acknowledges that the same billing methodology was used in 2000 Bush-Cheney however, the amount of the overbilling of the Press was not material. Furthermore, there is no indication that cost associated with the Bush Primary Committee was included in the calculation of travel cost of the 2000 Bush-Cheney General Committee.

Generally Accepted Accounting Principles

The General Committee explained several accounting principles and standards under Generally Accepted Accounting Principles (GAAP) to support its methodology for billing the Press. The General Committee believes that the Audit staff did not apply the appropriate accounting basis in its analysis. Specifically, the General Committee believes the Audit staff incorrectly applied a cash-basis of accounting instead of an accrual-basis in its analysis of Press billing. Under cash-basis accounting, revenue is recorded when cash is received and an expense is recorded when cash is paid. In accrual-basis accounting, revenue is recognized when it is earned (or when services are performed) and expenses recognized when incurred.⁴ The General Committee explains that under accrual-basis accounting, the objective is to ensure that events that change an entity's financial statements are recorded in the periods in which the events occur, rather than only in the periods the entity receives or pays cash. The General Committee also states the matching principle under GAAP dictates that expenses are recognized when the revenue is recognized, and therefore the entire cost of the contract should be used when calculating billing for travel.

The Audit staff agrees that the matching principle dictates that expenses are recognized when the revenue is recognized. In turn, the revenue recognition principle recognizes revenue in the *period* in which it is earned. Since the *period* and activity audited was the general election period, the Audit staff correctly applied the \$4,047,402 cost for the general election portion of the Swift Air contract and related expenses.

The issue is not whether the cash or accrual-basis of accounting is applied to the transportation costs and revenue generated from the billing of the Press for travel; nor is

⁴ "Accounting Principles 7th Edition", Jerry J. Weygandt PhD, CPA, Donald E. Kieso PhD, CPA, Paul D. Kimmel PhD, CPA, page 90

there a question of the matching principle under GAAP. At issue is whether the activity of a separate reporting and corporate entity (the Primary Committee) should be recognized by the General Committee and by this audit. An underlying assumption to GAAP is that every entity is separate and, therefore, the revenues and expenses of each entity should be recognized as such. As previously noted, recognizing the activity of the two entities separately is further supported by 11 CFR §9034.4(e)(7), which states in part that expenditures for campaign-related transportation shall be attributed according to when the travel occurs. Therefore, the General Committee should recognize only those transportation costs from September 1, 2008 through November 4, 2008 in the calculation for billing the Press.

Reconfiguration

The General Committee believes that aircraft reconfiguration costs are a part of placing the asset in service and reconfiguration costs were included in the value of the asset when it was purchased from the Primary Committee. Therefore, the General Committee contends that all reconfiguration costs could be billed to the Press pro rata since the Press used the asset.

In response to the Exit Conference and after discussions with the Audit staff, the General Committee stated that all reconfiguration costs incurred, with the exception of decals and any item that benefited only campaign staff, such as dividing curtain expenses, should be included in the billable amount. After considering the General Committee's response, the Audit staff revised its calculation of aircraft reconfiguration costs billable to the Press. The Audit staff did not include costs for painting and applying logos totaling \$161,386 and the cost for a divider curtain totaling \$1,167 in the calculation for billable reconfiguration costs since the General Committee indicated that these items benefited only the campaign. As a result, the Audit staff calculated \$487,447 (\$650,000 – \$161,386 – \$1,167) in reconfiguration costs billable for all travelers for both the primary and general periods. After taking 60 percent of the accepted reconfiguration cost because the aircraft was purchased from the Primary Committee, the Audit staff calculated \$292,468 (\$487,447 x 60%) of aircraft reconfiguration costs as billable during the general period. The Audit staff divided this amount by the total 140.3 flight hours flown by the General Committee to determine the amount of aircraft reconfiguration costs attributed to each segment.

Other Considerations

The General Committee stated that the Audit staff and the Commission have allowed for transfers and repayments between primary and general election presidential committees with respect to other types of vendors. The General Committee believes that any excess funds from the Press for travel are no different than deposits related to other vendors such as those for telephone contracts, media placement refunds, or lease agreements, whereby repayments sometimes are necessary to ensure a primary committee does not subsidize the general committee.

The General Committee also contends it would not be reasonable to force campaigns to renegotiate and redraft every legal contract that exists to separate Primary and General activity. To refund the Press would involve more than 700 separate billing transactions and it would "go against many of the internal ethics policies of the various news

organizations...who are not allowed to receive passage at discounted rates on campaign transportation so as to not unduly influence their coverage of the candidates.”

The Audit staff acknowledges the administrative burden that may be involved with refunding the Press. Historically, the Commission has allowed refunds to the Press to be made on a pro rata basis, such as in the 1996 Dole-Kemp audit, rather than recalculating each billing to the Press. The alternative suggestion, refunding the Primary Committee, would be considered a non-qualified campaign expense subject to repayment. The regulations state that a general election committee cannot incur primary-related expenses because they are not in furtherance of the general election. 11 C.F.R. §9002.11(a).

The General Committee received reimbursements from the Press for campaign travel that were above the maximum amount billable to the Press. The Primary Committee appears to have billed an amount that was less than its cost. The Primary and General Committee each paid its share of the contract and billed the Press and Secret Service accordingly. Although the regulation limits how much can be billed, there is no requirement that any billing be made. Thus, the travel could be provided at no cost.

The General Committee is correct that there are transactions between the Primary and General Committees in many Presidential campaigns in which either the primary or general election is publicly funded. Assets, ranging from office equipment to service deposits to, as in this case, aircraft configuration, often are purchased. In each case, value is transferred between the two committees. For example, if the General Committee purchases security deposits, it gives cash for the right to continue the service and recover the deposit after the campaign. No such exchange is involved in the proposed transfer to the Primary Committee in this case.

The General Committee does not dispute that it received more reimbursements from the Press during the general election period, but the General Committee believes a more appropriate term is misallocation of Press travel reimbursement received between the General Committee and the Primary Committee. The General Committee's methodology may accurately reflect the comparative actual use of the aircraft between the Primary (111.8 flight hours) and General Committees (140.3 flight hours), but it does not reflect the comparative actual costs paid by each committee. As seen below in Finding 2, the General Committee did not exceed the overall expenditure limitation, even with the excessive Press reimbursements. However, the purpose is to match the cost of the campaign to the proper election and spending limit. For these reasons and those noted above, the General Committee received reimbursements totaling \$344,892 from the Press that were above the maximum amount billable under the regulations.

The Audit staff recommends that, within 60 calendar days of service of this report, the General Committee demonstrate it did not receive reimbursements from the Press for campaign travel that were above the maximum amount billable to the Press. Absent such evidence, the General Committee should return, on a pro rata basis, \$344,892 to Press representatives and provide documentation to support the refunds.

Finding 2. Expenditure Limitation

Summary

The expenditure limitation for the 2008 general election for the office of President of the United States was \$84,103,800. Based on the Audit staff's review of financial activity through March 31, 2011 and estimated winding down costs, the General Committee has not exceeded the limitation.

Legal Standard

A. Presidential Candidate Expenditure Limitation. No presidential candidate eligible under 2 U.S.C. 9003 to receive payments from the Secretary of the Treasury may make expenditures exceeding \$20,000,000 as adjusted for the increases in the Consumer Price Index. The expenditure limitation for the 2008 general election for the office of President of the United States was determined to be \$84,103,800. 2 U.S.C. §441a(b)(1)(B) and (c).

B. Repayments. If the Commission determines that the eligible candidate of a political party and his or her authorized committees incurred qualified campaign expenses in excess of the aggregate payments to which the eligible candidates of a major party were entitled under section 9005, it shall notify such candidates of the amount of such excess and such candidates shall pay to the Secretary of the Treasury an amount equal to such an amount. 2 U.S.C. §9007.2 (b)(2).

C. Net Outstanding Qualified Campaign Expenses (NOQCE). Within 30 days after the end of the expenditure reporting period, the candidate must submit a statement of net outstanding qualified campaign expenses. The statement must contain:

- the total of all committee assets including cash on hand, amounts owed to the committee and capital assets listed at their fair market value;
- the total of all outstanding obligations for qualified campaign expenses; and
- an estimate of necessary winding-down costs. 11 CFR §9004.9(a)(1) and (b).

D. Expenditure Report Period. In the case of a major party, the expenditure report period begins on September 1 before the election or the date on which the major party's nominee is chosen, whichever comes earlier. The period ends 30 days after the Presidential election. For the General Committee, the expenditure report period ran from September 1, 2008 to December 4, 2008. 11 CFR §9002.12(a).

E. Compliance Fund Pay Winding Down. Contributions to the General Election Legal and Accounting Compliance Fund (GELAC) shall be used to 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.

For purposes of this section, 100 percent of salary, overhead and computer expenses incurred after the end of the expenditure report period shall be considered winding down expenses payable from GELAC funds, and will be presumed to be made solely to ensure compliance with 2 U.S.C. 431 *et seq.* and 26 U.S.C. 9001 *et seq.* 11 CFR 9003.3(a)(2)(I).

Facts and Analysis

A. Facts

The expenditure limitation for the 2008 general election for the office of President of the United States was \$84,103,800. The following is the Audit staff's analysis of expenditures subject to the limitation.

Reported Operating Expenditures as of March 31, 2011	\$ 84,022,537
Add: Accounts Payable	
Payment to Press for Campaign Travel (Finding 1)	344,892
Less: Accounts Receivable	
Due from Compliance Fund for Winding Down Expenses	<u>(263,629)</u>
Net Expenditures Subject to the Limitation	\$ 84,103,800
Expenditure Limitation	<u>84,103,800</u>
Amount In Excess of the limitation	<u>\$ -0-</u>

As the chart demonstrates, the General Committee has not exceeded the limitation. The calculation assumes that the Compliance Fund will reimburse the General Committee for some winding down costs in accordance with 11 CFR §9003.3(a)(2)(I). This calculation is also contingent upon the Commission adoption of a payment to the Press of \$344,892 in Finding 1⁵. Further, a Statement of Net Outstanding Qualified Campaign Expenses (NOQCE) prepared by the Audit staff can be found at page 19 and supports the result of the limitation analysis above.

B. Preliminary Audit Report & Audit Division Recommendation

This matter was presented to the General Committee at the Exit Conference. In response, the General Committee submitted a narrative stating it concurs with the Audit staff that it did not exceed the spending limit, but believes further adjustments to the analysis may be necessary pending the matters discussed in Finding 1. As discussed, the General Committee does not agree with a payable to the Press for campaign travel and believes the Compliance Fund's reimbursement for winding down expenses may not be necessary because the General Committee would not have otherwise exceeded the limitation.

⁵ If it is determined that the \$344,892 is a payable to the Primary instead of the Press, the adjustment to the spending limit would be the same.

Part V

Finding and Recommendation for the Compliance Fund

Failure to File 48-Hour Notices

Summary

The Compliance Fund failed to file 48-hour notices for 169 contributions totaling \$240,700 received prior to the general election. The Audit staff recommends that the Compliance Fund provide evidence that 48-hour notices were timely filed or submit any written comments it considers relevant.

Legal Standard

48-Hour Notification of Contributions. An authorized committee of a candidate must file special notices regarding contributions of \$1,000 or more received less than 20 days but more than 48 hours before any election in which the candidate is running. This rule applies to all types of contributions to any authorized committee of the candidate. 11 CFR §104.5(f).

Facts and Analysis

A. Facts

The General election was held on November 4, 2008. Contributions of \$1,000 or more received by the Compliance Fund between October 16, 2008 and November 1, 2008 required the filing of 48-hour notices. (FEC Form 6 – 48-Hour Notice of Contributions/ Loans Received). The Audit staff isolated 589 contributions, totaling \$871,260, which required the filing of these 48-hour notices. A review of these records identified 169 contributions, totaling \$240,700, for which the Compliance Fund failed to file the 48-hour notices.

B. Preliminary Audit Report & Audit Division Recommendation

The Audit staff discussed this matter with Compliance Fund representatives at the Exit Conference and provided a schedule of the contributions requiring 48-hour notice filings. In response, Compliance Fund representatives stated the matter had been previously addressed in a letter to the Reports Analysis Division and reiterated that “48-Hour Notices were not required for many of the identified contributions, as they were merely redesignations or reattributions that took place during the 48-Hour Notice reporting period.” The Compliance Fund representatives also stated that “the Compliance Fund’s normal practice of filing a 48-Hour Notice was not followed for a remaining group of contributions, due to data-management errors made by its outside vendor. To elaborate, the Compliance Fund’s outside data-management vendor ‘tagged’ this group of contributions with an incorrect date in its database and consequently failed to locate the group in a subsequent, computerized search for contributions requiring a 48-Hour Notice. The Compliance Fund has now taken measures with this outside vendor to ensure that

this unintentional oversight is corrected, and Compliance Fund staff believes that this was a one-time occurrence.”

Additionally, Compliance Fund representatives emphasized that “48-Hour Notices are intended to bring to light any last-minute contributions that a candidate might deploy for campaign-related activities, such as advertising and get-out-the-vote efforts, during an election’s final days. Donations to the Compliance Fund, however, may not be used for any candidate’s election and may only support legal and accounting services to ensure compliance with Federal law. It should also be noted that the Compliance Fund today maintains a balance of over \$20 million, meaning that these funds received shortly before the 2008 general election still have not been spent for any purpose. The Compliance Fund was therefore not in material violation of the 48-hour notice requirement when its reliance on an outside vendor caused it to delay disclosure of donations that would only fund lawyers’ and accountants’ legal compliance activities. For these same reasons, the Compliance Fund should not be fined for this vendor failure even if the Commission somehow finds that a technical infringement of the 48-hour notice requirement occurred.”

The Audit staff recommends that, within 60 calendar days of service of this report, the Compliance Fund provide:

- documentation to demonstrate the contributions in question were properly included in 48-hour notices; or,
- documentation establishing the contributions were not subject to 48-hour notification; and/or,
- any further written comments it considers relevant.

Part VI

Finding and Recommendation for the Joint Fundraising Committees

Based upon the limited examination of the reports and statements filed, and the records presented by seven joint fundraising committees, the Audit staff discovered no material non-compliance.

Part VII Attachment

**McCain-Palin 2008 Inc.
Net Outstanding Qualified Campaign Expenses
As of December 4, 2008
As Determined on March 31, 2011**

Assets

Cash in Bank			\$3,693,508	
Accounts Receivable:				
Due from the Compliance Fund	\$2,661,927	(a)		
Due from the Primary Committee	\$339,056			
Due from other Vendors	<u>\$4,234,755</u>	(b)		
			<u>\$7,235,738</u>	
TOTAL ASSETS				\$10,929,246

Obligations:

Accounts Payable:				
For Qualified Campaign Expenses			\$8,448,103	
Due to the Compliance Fund			\$100,107	
Due to the Primary Committee			\$167,828	
Payment to Press for Campaign Travel			\$344,892	
Amount Due U.S. Treasury:				
Disgorgement of Interest Earned			\$58,319	(c)
Disgorgement of Stale-Dated Checks			\$2,882	(d)
Winding Down Costs:				
Actual: December 5, 2008 to March 31, 2011			<u>\$1,807,115</u>	(e)
TOTAL OBLIGATIONS				\$10,929,246
NET OUTSTANDING QUALIFIED CAMPAIGN EXPENSES (DEFICIT)				<u>(\$0)</u>

- (a) This amount represents repayments for expenditures paid by General, \$87,217 for Secret Service shortfall for campaign travel, \$76,841 for transfers, and \$2,399,908 for 5 percent allocable portion of media costs. A receivable for \$97,961 is also due for compliance-related winding down costs.
- (b) This amount represents Press and Secret Service receipts, media refunds, interest earned, capital assets sold, and capital assets in-house to be sold.
- (c) This amount represents disgorgement made on Jan. 2, 2009 for interest.
- (d) This amount represents disgorgement made on Jan. 2, 2010 for stale-dated checks.
- (e) The General Committee has not exceeded the winding down cost limitation at 11 CFR §9004.11(b).



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

December 1, 2010

MEMORANDUM

TO: Joseph F. Stoltz
Assistant Staff Director

FROM: Christopher Hughey *ch*
Acting General Counsel

Lawrence L. Calvert, Jr. *LLC*
Associate General Counsel

Lorenzo Holloway *LH*
Assistant General Counsel
For Public Finance and Audit Advice

Delanie DeWitt Painter *DDP*
Attorney

SUBJECT: Preliminary Audit Report for McCain-Palin 2008, Inc. and McCain-Palin Compliance Fund, Inc. (LRA 759)

The Office of the General Counsel has reviewed the proposed Preliminary Audit Report ("PAR") for McCain-Palin 2008, Inc. (the "General Committee") and McCain-Palin Compliance Fund (the "GELAC").¹ Our comments primarily focus on Finding 1: Campaign Travel Billing for Press. We agree that the General Committee should refund the amounts of excess reimbursements to the press rather than transferring funds to the candidate's primary election committee. We concur with your calculation of the amount the media should reimburse to the General Committee for the actual costs of the air charter contract paid for and used by both the primary and general campaigns. We question, however, the legal basis for your calculation of reconfiguration costs billable to the press. We recommend that you raise the reconfiguration costs issue for the Commission's consideration.

Your cover memorandum also requests comments on two issues that are not included in the proposed PAR: Issue 1 -- Media Vendor Earned Interest and Issue 2 -- Hybrid Communications. We reiterate our informal advice concerning the interest issue

¹ We recommend that the Commission consider this document in Executive Session because the Commission may eventually decide to pursue an investigation of matters contained in the proposed Report. 11 C.F.R. §§ 2.4(a) and (b)(6).

Memorandum to Joseph F. Stoltz
Preliminary Audit Report McCain-Palin 2008, Inc. (LRA 759)
Page 2

to formalize our advice and inform the Commission. We also comment briefly on the hybrid communications issue. We recommend that you raise both of these issues for the Commission's consideration in the cover memorandum to the Commission. Finally, we concur with the remaining findings not specifically discussed in this memorandum. If you have any questions, please contact Delanie DeWitt Painter, the attorney assigned to this audit.

I. CAMPAIGN TRAVEL BILLING FOR PRESS (Finding 1)

A. Background

The draft PAR states that the auditors reviewed travel billing and press reimbursements and concluded that the General Committee must refund \$382,299 to the press for excessive reimbursements. The press traveled with the presidential candidate on a plane chartered through Swift Air LLC ("Swift Air"). John McCain 2008, Inc. ("Primary Committee") had used the same chartered airplane during the latter part of the primary campaign. The press traveled with the vice presidential candidate on a plane chartered through JetBlue Airways Corporation.² The auditors calculated the total actual transportation cost to the press was \$3,722,208. They determined that the maximum that the General Committee could bill the press was 110% of this actual cost, \$4,094,429. The General Committee billed the press \$4,503,698 and, in response to those bills, received reimbursements of \$4,476,728. Thus, the auditors conclude that the General Committee must refund the excessive amount of \$382,299 (\$4,476,728 - \$4,094,429) to the press. The excessive reimbursements were caused by the Committee's method of calculating the actual travel costs on the leased airplane from Swift Air and the costs of reconfiguring the leased Swift Air and JetBlue airplanes.

1. Swift Air Flight Costs

The Swift Air charter contract for the leased aircraft covered a portion of the primary campaign and the entire general campaign and ran between June 30, 2008 and November 15, 2008. The contract was signed on behalf of the Primary Committee, but the General Committee appears to have assumed the payments and terms of the contract and made weekly payments to Swift Air during the general election period. The total contract cost was \$6,384,000, to be paid in 19 weekly payments of \$336,000. The contract entitled the campaign to 22.4 flight hours per week for a total of 425.6 flight hours for the entire contract. Flight hours in excess of 22.4 hours per week were to incur additional charges and unused hours could be rolled over to later weeks, but if a total of fewer than 425.6 hours had been flown by the end of the contract, the campaign was to remain liable for the total contract cost of \$6,384,000. In other words, the campaign was

² The press also traveled on aircraft chartered through CSI Aviation Services, as well as by ground transportation, but the excessive reimbursements were primarily related to the air travel on, and costs of reconfiguring the Swift Air plane, and to a lesser extent, to the reconfiguration costs for the JetBlue plane.

Memorandum to Joseph F. Stoltz
Preliminary Audit Report McCain-Palin 2008, Inc. (LRA 759)
Page 3

entitled to no refund or rebate for flight hours that remained unused at the end of the contract.³

The Primary Committee paid Swift Air \$336,000 per week each week for nine weeks and the General Committee paid the same weekly amount each week for ten weeks during the general election period. The General Committee made its first weekly payment on September 8, 2008. Over the ten weeks it had the aircraft, the General Committee paid Swift Air a total of \$4,047,402, which included the contract cost of \$3,360,000 plus \$687,402 for fuel, catering, passenger taxes and ground handling fees. Neither the Primary Committee nor the General Committee used up the flight hours that they were entitled to use; the Primary Committee used 111.8 flight hours and the General Committee used 140.3 flight hours.

To determine the amount that the General Committee could receive in press reimbursements, the General Committee had to calculate the pro rata share of the actual cost of travel for each passenger. The General Committee and the Audit Division used two different methods to calculate this pro rata share.

The General Committee's calculation was based on the cost over the entire life of the contract and included the entire amount that the General Committee paid as well as a portion of the amount that the Primary Committee paid on the contract. Specifically, the General Committee's calculation is based on the combined actual flight hours that both committees used during the campaign. Since the contract price with Swift Air was fixed, the committees could develop the cost of operating the plane for each hour by dividing the contract price by the hours flown. The committees used the cost of operating the plane for each hour to determine the pro rata share for each passenger.⁴ During the course of the campaign, however, the committees could not have known the total actual hours. The committees, therefore, estimated the hours and adjusted the estimate on a

³ In addition to the contract cost, the Swift Air contract required the campaign to pay additional costs for fuel, catering, passenger taxes and ground handling fees. These costs are included in the auditors' calculation.

⁴ Here is a simplified example of how the General Committee's calculation worked. (These are not the actual figures, and do not reflect the continual re-estimation by the General Committee of the total cost over the entire life of the contract. They are simplified figures used to illustrate the principle at issue here). Assume that the Primary Committee and the General Committee are viewed as one entity. The fixed contract price with Swift Air is \$100,000. The Primary Committee and the General Committee have flown a total of 20 hours. The hourly operating cost would be \$5,000 per hour (\$100,000/20). If there were 50 passengers on the plane for each of the 20 hours flown, then the pro rata share for each passenger would be \$100 per hour (\$5,000/50). Further assume the Primary Committee used the plane for six hours, and the General Committee for 14 hours and all 50 passengers flew for each of the 20 hours. Under this example, the Primary Committee's passengers would be billed \$600 (\$100 x 6) and the General Committee's passengers would be billed \$1,400 (\$100 x 14). Now assume that the Primary Committee possessed the plane just under half the time and paid for just under half the cost of the plane, and the General Committee possessed the plane just over half the time and paid for just over half the cost. But \$600 is more than "just under" half the cost per passenger and \$1,400 is more than "just over" half. The Committee's method more accurately reflects the comparative use of the plane between the two committees; but it does not accurately reflect the comparative cost of the plane as paid by the two committees.

Memorandum to Joseph F. Stoltz
Preliminary Audit Report McCain-Palin 2008, Inc. (LRA 759)
Page 4

segment-by-segment basis. Using this method of calculating the pro rata share, the General Committee claims that it received press reimbursement of only 106% of the actual cost – less than the regulatory maximum of 110%.

The Audit Division took a different approach to calculate the pro rata share and concludes that the General Committee received reimbursements in excess of the maximum 110%. It looked only at the actual cost paid by the General Committee to Swift Air for travel during the general election portion of the contract, not the entire cost of the contract over its entire life during both the primary and general campaigns. The auditors' calculation was based on the \$336,000 weekly payments to Swift Air, as well as costs for fuel, catering, passenger taxes and ground costs and some reconfiguration costs (see below). Thus, the Audit Division concludes that the Primary Committee billed press travelers less than their pro rata share of the total amount the Primary Committee actually paid on the Swift Air contract, leaving an amount that the Primary Committee had paid on the contract but did not bill. Consequently, the General Committee billed press travelers *more* than their pro rata share – in fact, more than 110% of their pro rata share – of the amount the *General Committee* actually paid on the contract because the General Committee's calculation included a portion of the entire contract that had been paid by the Primary Committee.

2. Reconfiguration Costs

In addition to the Swift Air contract costs, the Committee and the auditors included different amounts for reconfiguration costs for the Swift Air plane in their calculations. The Swift Air aircraft total reconfiguration cost was \$650,000.⁵ The Primary Committee initially paid for the reconfiguration and the General Committee reimbursed the Primary Committee \$390,000, the total reconfiguration cost less 40% depreciation. The General Committee's calculation of the press's share of reconfiguration costs originally included the entire \$650,000 amount of reconfiguration costs, but it apparently later accepted the auditors' exclusion of \$162,657 in costs for logos, painting, and a divider curtain.

The auditors, however, accepted only \$422,620 in reconfiguration costs as actual costs of press travel, based on the costs the auditors concluded reasonably benefitted the press. The auditors determined that the General Committee could include in the actual cost of travel 100% of reconfiguration costs attributable primarily to the convenience and needs of the press; 78%, based on the proportion of press passengers to the number of total passengers, of reconfiguration costs attributable to the convenience and needs of all passengers; and zero percent of those costs that were allocable only to the convenience

⁵ This amount paid for goods and services including painting and application of decals and campaign logos to the aircraft; a portable satellite phone system; divider curtains for the cabin; seat parts; engineering and design work; repairs; labor; and the cost of returning the aircraft to its original condition once the campaign was over.

Memorandum to Joseph F. Stoltz
Preliminary Audit Report McCain-Palin 2008, Inc. (LRA 759)
Page 5

and needs of the campaign.⁶ The auditors then took 60% of \$422,620, because the General Committee had purchased the reconfiguration from the Primary Committee at 40% depreciation. The auditors concluded that \$253,572 was billable to the press by the General Committee. They then divided this by the 140.3 flight hours flown by the General Committee to determine the reconfiguration cost per flight segment. The auditors also accepted as actual travel costs billable to the press \$33,814 in reconfiguration costs for battery packs and satellite phones for the JetBlue aircraft, out of total reconfiguration costs of \$77,119 for that airplane, but did not accept the remaining reconfiguration costs for applying logos, repainting the plane and placement and removal of divider curtains.

B. Excessive Media Reimbursements Determined By Calculating Actual Travel Cost

1. General Committee and Audit Division Disagree on How to Calculate Actual Travel Cost

We understand that the center of the disagreement between the General Committee and the Audit Division is which accounting method should be used to calculate the actual cost for the passengers' pro rata share under 11 C.F.R. § 9004.6(a). The General Committee argues its accounting method, in combining the contract cost of both committees, was more reasonable than the auditors' accounting method given that the contract price was not directly proportional to the actual use of the aircraft over the period of the contract. While the auditors' method relied on the cost that each committee paid under the contract, the General Committee argues that the cost that the committees were paying for the contract was not directly reflective of the flight hours that they were using as they proceeded through the campaign.

As a legal matter, however, we question whether the Commission should apply the General Committee's approach because it requires the Commission to combine the contract cost and use of both the Primary Committee and the General Committee. The problem with the General Committee's argument is, as noted at footnote four above, its method may accurately reflect the comparative actual use of the aircraft between the two committees, and even may accurately reflect the combined pro rata shares of the actual cost to the Primary Committee and the General Committee, but is out of proportion to the comparative actual costs paid by the two committees. And because, of the two committees, the General Committee is the only one that is publicly financed and the only one that is the subject of this audit, it is the "actual cost," 11 C.F.R. § 9004.6(a), to the General Committee with which we are concerned here.

⁶ If both sides agree that \$161,490 for logos and painting and \$1,167 for a divider curtain could not be included in actual cost, then \$650,000 minus \$162,657 = \$487,343. Thus, the real difference between the General Committee's position and the auditors' position appears to be the difference between \$487,343 and the auditors' \$422,620. Presumably, that difference is accounted for by the costs that benefitted all passengers, which the Committee included at 100% and the auditors included at 78%.

Memorandum to Joseph F. Stoltz
Preliminary Audit Report McCain-Palin 2008, Inc. (LRA 759)
Page 6

The public financing rules allow general election committees to seek limited reimbursements from the media for travel expenses. See 11 C.F.R. § 9004.6(a)(2) and (3). “The amount of reimbursement sought from a media representative . . . shall not exceed 110% of the media representative’s pro rata share (or a reasonable estimate of the media representative’s pro rata share) of the actual cost of the transportation and services made available.” 11 C.F.R. § 9004.6(b)(1). The pro rata share is calculated by “dividing the total actual cost of the transportation and services provided by the total number of individuals to whom such transportation and services are made available.”⁷ 11 C.F.R. § 9004.6(b)(2). While we can apply this regulation to the travel expenses of one committee operating in one election, neither the regulation itself, nor its Explanation and Justification provide a formula for calculating the actual cost of air travel on a chartered airplane used by two committees in two different elections (primary and general).

The auditors’ calculation of the actual cost of the Swift Air contract and related costs is simple. The auditors determined that the actual cost was the amount paid by the General Committee to Swift Air for travel during the general election period. The calculation was based on the weekly installment payment of \$336,000 and additional costs, the weekly flight hours, and the number of passengers. Under the Audit Division’s method, the General Committee billed the press and received reimbursements from the press, not only for the amounts the General Committee paid to Swift Air during the general election period, but also for a portion of the travel costs that the Primary Committee paid to Swift Air for transportation attributable to the primary campaign.

The Audit staff’s calculation is appropriate because the cost of the Swift Air contract paid for and used by both the primary and general campaigns should be divided based on the amount each committee actually paid for travel during the primary or general campaign. The regulatory history provides no guidance about how to determine the “actual cost” in a case like this one, where a candidate’s primary and general committees shared a contract for use of the same leased *airplane*. But the Commission has noted, in addressing what types of costs could be charged to the media as the “actual cost” of *ground* transportation and facilities, that “campaigns should already be well aware that each media representative may only be charged his or her own pro rata share of costs” and “committees may not force the traveling press to absorb the costs” of services “used or consumed” by others. Explanation and Justification for 11 C.F.R. § 9004.6, 64 Fed. Reg. 42,581-2 (Aug. 5, 1999). *Id.* at 42,582. This reasoning would support the conclusion that media traveling with a candidate’s general election campaign should pay only for general election period travel and not be forced to absorb air travel costs more properly viewed as attributable to the candidate’s primary campaign, and specifically to the media who traveled with that campaign.

⁷ The travel reimbursement rule at section 9004.6 has changed in some ways over the years, but the Commission has consistently stated that committees should determine the media representative’s pro rata share of the “actual cost” of the transportation. See, e.g., Explanation and Justifications for 11 C.F.R. § 9004.6, 45 Fed. Reg. 43,376 (June 27, 1980); 56 Fed. Reg. 35903 (Jul. 29, 1991), 60 Fed. Reg. 31,858-59 (June 16, 1995), 64 Fed. Reg. 42,581 (Aug. 5, 1999).

Memorandum to Joseph F. Stoltz
Preliminary Audit Report McCain-Patin 2008, Inc. (LRA 759)
Page 7

2. General Committee's Actual Cost Should Be Based On Travel Cost Paid By General Committee

The General Committee's press billing and reimbursement calculation should be based only on the General Committee's payments for travel in furtherance of the general election campaign during the general election period. The General Committee cannot incur primary-related travel expenses because they are not in furtherance of the general election campaign. *See* 26 U.S.C. § 9002(11); 11 C.F.R. § 9002.11. As the General Committee cannot incur expenses for primary-related travel, it should not be able to effectively bill the press for those costs either. The publicly-funded General Committee and McCain's non-publicly funded Primary Committee should keep their expenses separate because the two campaigns operated under different rules, requirements and limitations. Senator McCain agreed to use only public funds for his general election campaign; to take no contributions; and to keep his spending within the general election expenditure limitation, which equals the amount of public funds he received. *See* 26 U.S.C. §§ 9002(11), 9003(b); 2 U.S.C. §§ 441a(b)(1) and (c); 11 C.F.R. § 9002.11. By contrast, Senator McCain opted not to participate in the primary matching payment program; his primary campaign was entirely privately funded.

Because primary and general election campaign expenditures must remain separate, the Commission created "bright line" rules for attributing expenses between the primary and general expenditure limitations after issues arose in prior election cycles about how to divide expenses that benefitted both campaigns between publicly funded primary and general committees. 11 C.F.R. § 9034.4(e); *see* Explanation and Justification for 11 C.F.R. § 9034.4(e), 60 Fed. Reg. 31,854 at 31,866-68 (Jun. 16, 1995). These rules were later revised to also apply to this situation, where the candidate received public funds in only one election. *Id.* Many of these bright line rules are based on timing. Under the bright line attribution rules, travel costs are attributed based on when the travel occurs. 11 C.F.R. § 9034.4(e)(7). If the travel occurs before the date of the nomination, the cost is a primary expense, unless the travel is by a person working exclusively on general election campaign preparations. *Id.* While these bright line rules are normally applied to situations to determine the attribution of travel cost to a primary and general campaign sharing expenses, we believe that it is appropriate for the Commission to use these same rules to determine the attribution of the travel costs between these committees and how much these committees should bill the press for travel cost.

Under the bright line attribution rules, the General Committee's weekly payments to Swift Air were for general expenses and the Primary Committee's weekly payments were for primary expenses because the weekly payments appear to be related to the weekly use of the leased plane. To the extent that the payments and the amounts billed to the press were related to travel occurring at the same time as the payments were made, those amounts were attributable to the Primary Committee prior to the date of the

Memorandum to Joseph F. Stoltz
Preliminary Audit Report McCain-Palin 2008, Inc. (LRA 759)
Page 8

candidate's nomination and to the General Committee after the date of the candidate's nomination. *See* 11 C.F.R. § 9034.4(e)(7).⁸

In addition, the separate reporting of expenditures by these separate committees supports the conclusion that General Committee and Primary Committee travel expenditures must remain separate. The General Committee and the Primary Committee file separate reports and are separate committees.⁹ Publicly funded authorized committees shall report all expenditures to further the candidate's general election campaign in reports separate from reports of any other expenditures made by those committees with respect to other elections. 11 C.F.R. § 9006.1.

3. Draft Preliminary Audit Report Requires Additional Explanations

The draft PAR addresses a number of the General Committee's arguments including arguments based on GAAP accounting principles, its contention that the auditors' methodology conflicts with section 9004.6(b)(3) of the Commission's regulations, and its interpretation of previous audits including Dole-Kemp 1996, Bush-Cheney 2000 and Kerry-Edwards 2004. We defer to the Audit Division's expertise in analyzing the correct application of accounting and auditing principles and procedures. We suggest, however, that you expand the explanation of why the Audit staff's approach is more appropriate and why the Committee's arguments and citations of precedent are not correct, if possible. The Committee raises complex accounting arguments and additional explanation would help clarify the auditors' analysis of those arguments for readers who do not have accounting expertise. In particular, the auditors may wish to address whether this issue arose in prior audits in such a way that the General Committee

⁸ The regulations allow a limited exception for qualified campaign expenses incurred prior to the general election expenditure report period for property, goods or services to be used during the expenditure report period in connection with the general election campaign. 11 C.F.R. § 9002.11(a)(2), 9003.4, 9004.4. The Commission explained that this exception is "designed to permit a candidate to set up a basic campaign organization before the expenditure report period begins." Explanation and Justification for 11 C.F.R. § 9003.4, 45 Fed. Reg. 43375 (Jun. 27, 1980). The rule lists examples of expenses such as establishing financial accounting systems and organizational planning. 11 C.F.R. § 9003.4(a). The General Committee has not demonstrated that the Primary Committee's weekly lease payments were related to travel after the date of nomination or were somehow pre-paying for the General Committee's use of the leased plane during the general election period. Nor is there any indication that travel during the primary period was by persons who were working exclusively to prepare for the general election. *See* 11 C.F.R. § 9034.4(e)(7). It would be difficult for the General Committee to make such a demonstration because both campaigns paid the same weekly amount for the leased plane and both campaigns used the leased plane. Although unused hours rolled over from week to week, neither committee used all of the flight hours they could have used under the contract. Nevertheless, if the General Committee is able to demonstrate that some portion of the Primary Committee's contract payments was to further the general election and should have been paid for by the General Committee, its actual cost of travel and the amount it may bill the press might increase.

⁹ Generally, publicly funded general election candidates set up a separate authorized committee for the general election, which they authorize to incur expenses on their behalf, as well as a separate legal and compliance fund. *See* 26 U.S.C. §§ 9002(1); 11 C.F.R. §§ 9002.1, 9002.2, 9003.3.

Memorandum to Joseph F. Stoltz
Preliminary Audit Report McCain-Palin 2008, Inc. (LRA 759)
Page 9

would have been on notice that its choice of accounting method might have negative consequences.

We also suggest that the PAR explain the Audit staff's response to the Committee's argument that the auditors' methodology is in conflict with section 9004.6(b)(3), which requires that media representatives be given a bill that specifies amounts charged for air and ground for each segment within 60 days. We understand from communications with the Audit staff that the auditors' approach is consistent with that regulation because the auditors used the number of travelers to calculate a pro rata amount of billable costs and accounted for varying numbers of travelers on each flight segment. The Committee could have used a similar calculation and timely billed the media. We suggest that the Audit staff explain this in the PAR.

With respect to the precedents cited by the Committee, the proposed PAR notes that the Bush-Cheney 2000 committee used a similar billing methodology to the General Committee, but that method did not result in any material overbilling of the press or audit finding in that audit. The absence of a finding in that audit is not a precedent, and does not indicate the approach or billings by the Bush-Cheney 2000 committee were correct. It merely indicates that the difference between the committee's and auditors' calculations in that audit was not large enough to raise an issue of material noncompliance. Here, the difference in the calculations is large enough to result in a finding. Moreover, according to the Audit staff, the General Committee seeks to apply the hourly calculation used in the Dole-Kemp 1996 audit to the total Swift Air costs over the life of the entire contract for both the General Committee and Primary Committee, and not, as in Dale-Kemp 1996, to a general election committee's portion of the costs for travel during the general election campaign.

The General Committee states in its response to the exit conference that there was no "overbilling" of any press traveler but, at most, a "misallocation" of the proceeds of press billings between the Primary Committee and the General Committee. Consequently, it concludes, it should not have to make any refunds to any press entities, but may simply transfer funds from the General Committee to the Primary Committee to correct the misallocation. The General Committee's proposed transfer of funds to the Primary Committee will not resolve the issue that the General Committee received reimbursements from the press in excess of its actual cost. If the General Committee's public funds are transferred to the Primary Committee and used to pay for primary campaign expenses, the payments would be non-qualified campaign expenses that may be subject to repayment because they would not be made to further McCain's campaign for the general election. See 26 U.S.C. §§ 9002(11), 9007(b)(4); 11 C.F.R. §§ 9002.11, 9004.4, 9007.2(b)(2). In the absence of any demonstration that the Primary Committee paid for general election travel, *see supra* note 8, the transfer would not resolve the excess press reimbursement problem. The amount of excess press reimbursements the General Committee received should be returned to the media representatives. 11 C.F.R. § 9004.7(d)(2).

Memorandum to Joseph F. Stoltz
Preliminary Audit Report McCain-Patin 2008, Inc. (LRA 759)
Page 10

Finally, we address the degree to which this finding matters. One of the principal benefits to publicly funded general election committees of the regulations' provisions permitting press reimbursements is that the committee may deduct properly received reimbursements from the overall expenditure limitation.¹⁰ 11 C.F.R. § 9004.6(a). Here, however, the auditors conclude that the Committee did not exceed the expenditure limitation, even when the excessive reimbursements are included.¹¹ Nevertheless, the General Committee's receipt of excessive press reimbursements is significant. The purpose of the travel reimbursement rules at section 9004.6 is to eliminate the possibility that a committee could effectively be subsidized by the media through charging the media higher amounts than their pro rata shares for transportation provided by the campaign. See Explanation and Justification for 11 C.F.R. § 9004.6, 45 Fed. Reg. 43,376 (June 27, 1980). The Commission has pursued press travel billing and reimbursement issues in the enforcement context. See MLIR 3385, Bush Quayle '88 (Committee agreed to a conciliation agreement with a \$10,000 civil penalty for a violation of section 9004.6).¹² In the 1996 cycle, the Dole-Kemp '96 ("DK96") audit resulted in a payment for expenses in excess of the expenditure limitation, which included press and Secret Service reimbursements collected in excess of actual costs, and the Commission pursued the issue in enforcement. See MURs 4670, 5170, 5171 (Commission and DK96 ultimately negotiated a Global Settlement and Release and a conciliation agreement with a \$75,000 civil penalty to resolve the payment and pending enforcement matters, but the final negotiated agreements do not address the press reimbursement issue or require that DK96 reimburse the press.) Thus, we believe that the facts surrounding the Swift Air flight costs and the press reimbursements for them merit inclusion in the PAR, notwithstanding that they have no impact in this particular case on the General Committee's compliance with the overall expenditure limit.

¹⁰ Expenditures for transportation, ground services or facilities provided to media are qualified campaign expenses that count against the overall expenditure limitation, but committees may seek reimbursement from the media and may deduct the reimbursements received from the expenditures subject to the overall expenditure limitation. 11 C.F.R. § 9004.6(a).

¹¹ The auditors' calculation of the overall expenditure limitation includes a GELAC reimbursement that lowers the General Committee's total expenditures below the limitation. The GELAC may reimburse the General Committee for certain types of expenses such as winding down costs and compliance expenses initially paid by the General Committee. To the extent that the GELAC reimburses the General Committee for these expenses, the expenses no longer count against the General Committee's expenditure limitation. The auditors' calculation also assumes the General Committee will pay the excess reimbursement amount to the press or make a transfer to the Primary Committee.

¹² Also in the 1988 cycle, the Commission ordered the Robertson 1988 Committee to refund \$105,634.56 in press overpayments. In a judicial review of the repayment determination, the Robertson Committee argued that the Commission did not have the authority to order the refund, but the court noted that the "issue is not before us" in the review of the repayment because the Commission conceded "that any challenge would have to frame" Robertson's "press charges as impermissible corporate campaign contributions," enforceable through the procedures of section 437g. *Robertson v. FEC*, 45 F.3d 486, (D.C. Cir. 1995), n.4.

Memorandum to Joseph F. Stoltz
Preliminary Audit Report McCain-Palin 2008, Inc. (LRA 759)
Page 11

C. Reconfiguration Costs Issue Should be Raised for Commission Consideration

We recommend that you raise in the cover memo for the Commission's consideration the issue of which reconfiguration costs should be considered actual costs of travel and included in calculating the pro rata amounts billable to the press. The Audit staff's analysis is based on whether reconfiguration costs reasonably "benefitted" the press. You state: "Historically, the Commission has only allowed the Press to be billed for those aircraft reconfiguration costs that could be reasonably considered as having benefitted the Press." Draft PAR at 10. In contrast, the General Committee considered all costs for reconfiguring the Swift Air aircraft, except for decal painting and some cabin dividers, as actual costs of travel. Applying a reasonable benefit test to the reconfiguration costs, the auditors accepted that 100% of costs where there was "an association" with the press were actual costs of travel, but asserted that only 78% of costs that were "not clearly associated" with the press but were instead for the convenience and needs of all passengers were accepted as actual costs of travel permissibly factored into the press reimbursement calculation. The 78% figure was based on a percentage derived from the proportion of press seats on the plane. But the auditors did not include any amount of the reconfiguration costs for logos and painting as actual costs of travel. For the JetBlue aircraft, the auditors accepted as actual costs of travel only the costs of battery packs and satellite phones because the press benefitted from these items, but did not accept reconfiguration costs for applying logos, repainting the plane and a divider curtain.

We question the legal basis for this approach and believe this issue should be considered by the Commission.¹³ The regulations do not set forth a "reasonable benefit" test for including airplane reconfiguration costs as actual costs of travel in determining the amount of travel expenses for which a committee may seek reimbursement from the press. With respect to the Commission's past practice, the draft PAR does not cite any previous audits where the Commission applied a reasonable benefit test to press billings for airplane reconfiguration costs. We have been unable to locate any prior Title 26 audit report that directly addressed this issue one way or the other. If the Audit Division is aware of Commission precedent on point, you should cite that precedent in the proposed report. We note that 11 C.F.R. § 9004.6 allows for reimbursement of a pro rata share of the actual costs of travel and does not distinguish between actual costs for aircraft operating costs (such as flight costs) and reconfiguration costs. The regulation requires

¹³ While we question this approach, we agree that the Committee's reliance on the Kerry-Edwards 2004, Inc. audit for the reconfiguration issue is misplaced. The dispute in Kerry-Edwards concerned how to calculate the amount of leased airplane reconfiguration costs that would count against the expenditure limitation, not the amount included in "actual cost" in determining the amount of travel expenses for which reimbursement from the press may be sought. The Kerry-Edwards general committee, like the General Committee, purchased a leased plane reconfiguration at 40% depreciation from its primary committee, but the issue in that audit was different. The Kerry-Edwards audit did not concern the calculation of reconfiguration costs that could be billed to the press. Moreover, the Commission never definitively addressed the reconfiguration valuation in that audit because the expenditure limitation issue was resolved when adjustments to other expenditures brought the total expenditures below the limitation. See Statement of Reasons, Kerry-Edwards 2004, Inc. (November 14, 2007).

Memorandum to Joseph F. Stoltz
Preliminary Audit Report McCain-Palin 2008, Inc. (LRA 759)
Page 12

that the actual cost of travel be determined, and only then apportioned into pro rata shares for the press travelers. Thus, the part of the process where the number of press seats should be considered is not in calculating the actual costs of the reconfiguration (the 78%), but in apportioning the pro rata share of the actual travel costs for press passengers.

II. MEDIA VENDOR INTEREST

The cover memorandum to the draft PAR notes the issue of interest earned by the Committee's media vendors totaling \$14,499. The issue is not in the draft PAR and there is no repayment recommendation because the Committee did not benefit from the earned interest. This Office previously responded to your informal query about whether the interest earned by the media vendors must be repaid to the United States Treasury and whether this matter should appear in the PAR as a finding or issue. As we said in our response, we conclude that because the interest earned by media vendors did not benefit the Committee, the Audit Division should not recommend any repayment of the interest. This conclusion is based on the Commission's actions in the 2004 cycle general election committee audits. We recommend, however, that you raise this issue for Commission consideration in the cover memorandum forwarding the PAR to the Commission.

The Committee used a media consultant, MH Media, and three media vendor subcontractors including Smart Media Group ("SMG"), which did television media buys. The auditors found that MH Media (\$1,325) and SMG (\$13,174) earned interest totaling \$14,499.79 on Committee funds between August 29, 2008 and January 31, 2009. The interest remained in the media vendors' bank accounts and none of the interest was used for media buys, compensation, or any other campaign purpose. The Committee states that it advised the media vendors to keep all earned interest separate and not to use it for any media buys or compensation. SMG transferred the interest to another account and did not use the funds, while MH Media kept the interest in the deposit accounts. The media vendors provided documentation to the auditors including bank statements and general ledgers demonstrating that the earned interest was not spent. The Committee believes the media vendor interest need not be repaid.

Candidates must repay income earned from the investment or other use of public funds, less taxes paid on such income. See 11 C.F.R. §§ 9007.2(b)(4), 9004.5. This type of repayment "ensure[s] that any income received through the use of public funds benefits the public financing system." Explanation and Justification for 11 C.F.R. §§ 9004.5 and 9007.2, 60 Fed. Reg. 31858 and 31864 (June 16, 1995).

In the 2004 presidential audits, the Commission was unable to reach agreement on whether to seek repayment of interest earned by media vendors on public funds where the interest earned was not paid to the committees or used to pay for media buys, commissions or other campaign purposes that would benefit the committees. In the Bush-Cheney '04 audit, the Commission did not have four affirmative votes to seek repayment of \$19,745 in interest earned on media vendor accounts. See Report of the

Memorandum to Joseph F. Stoltz
Preliminary Audit Report McCain-Malin 2008, Inc. (LRA 759)
Page 13

Audit Division on Bush-Cheney '04, Inc. and the Bush-Cheney '04 Compliance Committee, Inc. (approved Mar. 22, 2007). Some Commissioners thought that "the standard for repayment should be whether the General Committee received or benefited from the interest earned by having the interest used to make media buys or offset commissions." *Id.* at 11-12. They concluded that because Bush-Cheney '04, Inc. "did not receive or benefit from the interest earned, no finding or repayment determination would be appropriate." *Id.* at 12. Other Commissioners, however, concluded that repayment "may be appropriate" and "that the purpose for payment of interest or income was to ensure that any income received through the use of public funds benefits the public financing system." *Id.* Subsequently, the Commissioners expressed similar views in the Kerry-Edwards 2004, Inc. audit, but agreed on repayment of interest where the interest benefited the committee and was used for campaign purposes. See Report of the Audit Division on Kerry-Edwards 2004, Inc. and the Kerry-Edwards 2004 Inc. General Election Legal and Accounting Compliance Fund (approved June 14, 2007). The Commission determined that Kerry-Edwards 2004, Inc. was required to repay \$41,277 for interest that was used to pay for media buys and/or to offset amounts owed to the media vendor. However, the Commission did not require repayment of \$159,446 in interest that was never paid to the committee or used for campaign purposes and was earned on loans from the media firm to its parent company. *Id.* at 33-34.

Based on the Commission's actions in the 2004 audits, this Office concludes that because the interest earned by the media vendors was not used for campaign purposes or otherwise to benefit the Committee, the Audit Division should not recommend any repayment of the interest. We recommend, however, that you raise this issue for Commission consideration in the cover memorandum forwarding the PAR to the Commission. The Commission's regulations remain unchanged and do not include any test of benefit or use for campaign purposes for repayment of interest income. See 11 C.F.R. §§ 9007.2(b)(4), 9004.5. Nevertheless, the Commission's actions in the 2004 audits indicate lack of Commission consensus for repayment of interest beyond those payments that benefit the committee in some way. Some Commissioners may have concerns about whether interest income earned on public funds deposited with a third party vendor actually benefits a committee and is used for campaign purposes and may want to apply a benefit test for repayment of interest income. The Committee relied on the Commission's actions in the 2004 audits when it advised its media vendors to keep any interest income separate. We acknowledge that a benefit test for income repayments could be abused to circumvent the regulations if, for example, a campaign deposited large amounts of public funds with vendors to earn income as a way to enrich the vendors. That potential for abuse is not evident here. The amount of income at issue is minimal, and you have informed us that the Committee has already repaid a larger amount of interest it earned on public funds. Therefore, we conclude that raising this issue in the cover memorandum for Commission consideration but not recommending any repayment of the interest income is appropriate.

Memorandum to Joseph F. Stoltz
Preliminary Audit Report McCain-Palin 2008, Inc. (LRA 759)
Page 14

III. HYBRID COMMUNICATIONS

The cover memorandum to the draft PAR requests our comment on the issue of hybrid communications. Hybrid communications refer to a clearly identified candidate and make a generic reference to other party candidates without clearly identifying them. The Republican National Committee ("RNC") spent \$30,749,009 on hybrid media communications related to the general election. These expenses were not treated as coordinated party communications or counted against the Committee's expenditure limitation. We concur that this issue should be raised for the Commission's information in the cover memorandum to the PAR.

In 2004, the Commission did not pursue similar hybrid communications in the audits of both major party nominees. This Office commented that the auditors should not include the hybrid ad issue as a finding in the report or count the expenses against the candidates' expenditure limitations, but should raise the issue in the cover memorandum for the Commission's consideration. *See* Attachment 1. We also discussed several legal aspects of the issue the Commission could consider. *Id.* The Commission was divided on the issue and Commissioners issued Statements of Reasons for the audits. *See* Statement of Commissioners Lenhard, Walther and Weintraub, Audit of Bush-Cheney '04, Inc. (March 21, 2007), Statement of Commissioner Weintraub on Audit of Bush-Cheney '04, Inc. (March 21, 2007), Statement of Commissioners Mason and von Spakovsky, Final Audit Report on Bush-Cheney '04, Inc. (March 22, 2007), Statement of Commissioners Mason and von Spakovsky, Final Audit Report on Kerry-Edwards, 2004, Inc. (May 31, 2007). Our analysis of the issue remains the same, and we have attached our legal comments on this issue in the Bush-Cheney '04 audit for your information. Attachment 1. Subsequently, the Commission initiated a rulemaking on hybrid communications, which has not yet been completed and thus, is not applicable to this audit. The Commission considered expanding section 106.8, which applies to telephone banks, to address other types of "hybrid communications." *See* Notice of Proposed Rulemaking ("NPRM"), "Hybrid Communications," 72 Fed. Reg. 26569 (May 10, 2007).

Attachment 1.

Memorandum to the Commission, Preliminary Audit Report of the Audit Division on Bush-Cheney '04, Inc. and the Bush-Cheney '04 Compliance Committee (LRA # 664)" (May 26, 2006)



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

May 26, 2006

MEMORANDUM

TO: Joseph F. Stoltz
Assistant Staff Director
Audit Division

THROUGH: Robert J. Costa *RJ*
Acting Staff Director

FROM: James A. Kahl *JK*
Deputy General Counsel

Thomasenia P. Duncan *TD*
Associate General Counsel

Lorenzo Holloway *LH*
Assistant General Counsel
for Public Finance and Audit Advice

Delanie DeWitt Painter *DDP*
Attorney

Margaret J. Forman *MJF*
Attorney

SUBJECT: Preliminary Report of the Audit Division on Bush-Cheney '04, Inc. and the
Bush-Cheney '04 Compliance Committee (LRA #664)

I. INTRODUCTION

The Office of General Counsel has reviewed the Preliminary Audit Report ("proposed Report") of the Audit Division on Bush-Cheney '04, Inc. (the "Committee" or "Bush") and the Bush-Cheney '04 Compliance Committee ("GELAC") that you submitted to this Office on February 1, 2006. This is the second of two memoranda discussing our comments on the proposed Report. In this memorandum, we comment on the issue of possible in-kind contributions Bush received from the Republican National Committee ("RNC") when the RNC and Bush divided media expenses for broadcast advertisements that clearly identified the candidate and/or his opponent and made vague references to other political figures (Findings 1. B. and 2). If you have any questions, please contact Delanie DeWitt Painter or Margaret J. Forman, the attorneys assigned to this audit.

Preliminary Audit Report -- Bush-Cheney '04
(LRA # 664)
Page 2

II. ATTRIBUTION OF MEDIA COSTS (AUDIT REPORT FINDING 1.B. AND 2.)

The Audit Division found that Bush received in-kind contributions from the RNC for media expenses. The RNC and Bush equally divided media expenses for broadcast advertisements that clearly identified President Bush and/or John Kerry and made vague references to other political figures in Congress. The divided media expenses totaled \$81,418,812. The RNC also paid \$1.7 million in commissions. The proposed Report concludes that Bush should have paid for all of the media and commissions. Since the RNC paid for half of the media expenses and \$1.7 million in commissions, the proposed Report concludes that the RNC made in-kind contributions of \$42,409,406 ($\$81,418,812/2 = \$40,709,406 + \$1,700,000$) to Bush. The proposed Report recommends that, unless Bush demonstrates that it did not receive these in-kind contributions from the RNC, the Audit staff will recommend a repayment of \$42,409,406. *See* 26 U.S.C. § 9007(b)(3).

This Office recommends that you delete this issue and the related findings from the Report and not count these expenses against Bush's expenditure limitation. In light of recent Advisory Opinion ("AO") 2006-11, this Office believes that the Commission would approve the 50% attribution of these media expenses between Bush and the RNC. Instead, we recommend that you raise the issue in the Audit Division's cover memorandum when the Report is circulated for Commission approval so that the Commission can consider the issue.

In considering this issue, the Commission should note that neither the Federal Election Campaign Act ("FECA") nor the Commission's regulations definitively address the allocation of broadcast advertisements referencing only one clearly identified federal candidate (and/or his opponent) and a vague reference to their political allies in Congress. The Commission's regulations at part 106 address the allocation of similar types of expenses. The regulations at part 106 include both general allocation rules and specific rules for allocating specific types of expenses in particular circumstances. Section 106.1(a) provides the general rule that expenditures made on behalf of more than one clearly identified candidate shall be attributed to each candidate according to the benefit reasonably expected to be derived. 11 C.F.R. § 106.1(a). For a broadcast communication, the "attribution shall be determined by the proportion of space or time devoted to each candidate as compared to the total space or time devoted to all candidates." *Id.* A candidate is clearly identified if his or her name or likeness appears or if his or her identity is apparent by unambiguous reference.¹ 2 U.S.C. § 431(18); 11 C.F.R. §§ 106.1(d) 100.17. However, the advertisements at issue here clearly identify only the party nominees – the references to leaders, liberals or allies in Congress do not clearly identify any specific candidates. *See also* Advisory Opinion ("AO") 2004-33 (Ripon Society) (Commission stated that reference to "Republicans in Congress" in an advertisement did "not constitute an unambiguous reference to any specific Federal candidate" under section 100.29(b)(2)). Thus, section 106.1 does not apply.

¹ In 1995, the Commission considered adopting a broader definition of "clearly identified candidate" that would have included groups of candidates but declined to do so after receiving comments that it could be difficult to determine the identities of the candidates in a group, for example, based on a reference to "pro life" candidates. *See Explanation and Justification of 11 C.F.R. § 100.17*, 60 Fed. Reg. 35,292, 35,293-94 (July 6, 1995).

Preliminary Audit Report -- Bush-Cheney '04
(LRA # 664)
Page 3

Section 106.8, which sets forth a flat 50% attribution rule for party committee phone banks, also does not apply here. The language of that section applies only to one narrow category of campaign communications costs: phone banks. Section 106.8 "applies to the costs of a phone bank conducted by . . . a political party" under certain delineated circumstances, which include, *inter alia*, that the communication refers to a clearly identified federal candidate and "generically refers to other candidates of the Federal candidate's party without clearly identifying them." 11 C.F.R. § 106.8(a). When the Commission promulgated section 106.8, the Commission considered whether to "include other forms of communications such as broadcast or print media" but "decided to limit the scope of new section 106.8 to phone banks at this time because each type of communication presents different issues that need to be considered in further detail before establishing new rules." *Explanation and Justification for 11 C.F.R. § 106.8, "Party Committee Telephone Banks," 68 Fed. Reg. 64,517, 64,518 (Nov. 14, 2003).*

The Commission, nevertheless, has approved the attribution of expenditures for communications that refer to one clearly identified candidate and make a generic reference to other party candidates under certain circumstances. Most recently, in Advisory Opinion 2006-11, the Commission considered attribution of the cost of a mass mailing that expressly advocated the election of one clearly identified federal candidate and the election of other party candidates who were referred to generically. The Commission recognized that sections 106.1 and 106.8 do not directly apply, but applied analogous "space or time" principles set forth in section 106.1(n) to measure the "benefit reasonably expected to be derived" by the clearly identified federal candidate. The Commission concluded that *at least* 50 percent of the cost of the mailing must be attributed to the clearly identified candidate even if the space in the mailing attributable to him is less than that attributable to other candidates. However, if the space of the mailing devoted to the clearly identified candidate exceeded the space devoted to the generic party candidates, the costs attributed to the clearly identified candidate must exceed 50 percent and reflect at least the relative proportion of the space devoted to the candidate. Thus, the Commission approved a minimum 50% attribution to the clearly identified candidate, not an automatic 50/50% split.

This Office recognizes that the Commission could follow two attribution principles set forth in AO 2006-11 when it considers Bush's proposed media attribution. We recommend that the Commission take note of the distinctions between AO 2006-11 and this audit, and (2) the policy considerations for a candidate who receives public financing that were not present in AO 2006-11 when it considers whether to apply the attribution method of AO 2006-11 here. As discussed in greater detail below, this audit concerns broadcast advertisements rather than mass mailings and, it is questionable whether some of the advertisements generically refer to other candidates. Indeed, the advertisements appear to be primarily focused on furthering the election of a publicly-financed presidential candidate. Moreover, unlike AO 2006-11, the allocation principles of section 106.1 would be applied in the context of a publicly-financed presidential election. If the amount that is allocated to Bush is improper because it does not include all of the expenses that are in furtherance of his campaign for election to the office of President, 11 C.F.R. § 9002.11(a)(1), this would result in the introduction of private contributions into a publicly funded general election campaign through payment of media costs by the party, and those payments would not count against the candidate's expenditure limitations. *Compare* 11 C.F.R.

Preliminary Audit Report -- Bush-Cheney '04
(LRA # 664)
Page 4

§ 9002.11(a)(1)(expenditures that further the election to the Office of President) *with* 11 C.F.R. § 9002.11(b)(3)(expenditures that further the election of other candidates).

If the Commission decides to apply the attribution method of AO 2006-11, it would attribute *at least* 50% of the media costs to Bush, but there is the potential to attribute *more than* 50% to Bush. In AO 2006-11, the Commission by analogy applied the principles set forth in section 106.1(a)(1) of the "proportion of space or time devoted to each candidate as compared to the total space or time devoted to all candidates" to measure the "benefit reasonably expected to be derived" by the clearly identified candidate. If the Commission applies AO 2006-11 and those principles here, we recommend that the Commission consider three issues. See 11 C.F.R. § 106.1(a)(1); AO 2006-11.

First, the content of the advertisements appears to be primarily focused on promoting the election of the clearly identified candidate and does not make clear that references to other individuals allied with Bush were "devoted" to promoting the election of any other candidates. In fact, some of the vague references in the advertisements do not even rise to the level of "generic" party references that the Commission considered in approving attributions in AO 2006-11 and section 106.8.² The advertisements refer to Congressional allies of Bush or Kerry using vague descriptions such as "our leaders in Congress," "Congressional leaders," "liberals in Congress" and "liberal allies" rather than stating the party names "Democrats" or "Republicans" (except in one Spanish advertisement) or making clear that these officials were party candidates. The ambiguous references address whether legislators supported the plans of Bush or Kerry rather than their status as candidates of a party -- many Senators were not up for re-election and non-incumbent candidates are not included in the references. The references may have had a political purpose of associating Bush or Kerry with groups of Congressional incumbents as a way to increase support for Bush rather as a way to benefit any other unidentified party candidates.

Second, even assuming, *arguendo*, that each reference to a Congressional ally or leader was devoted to other party candidates, the amount of space and time devoted to Bush in the advertisements still may exceed 50 percent. In addition to the repeated references to Bush and his allies or leaders in Congress, all of the advertisements contain several seconds of pictures or footage of Bush alone, stating that he approved the advertisement as required by 2 U.S.C. § 441d(d) and 11 C.F.R. § 110.11(c).³ An attribution based on space and time could treat this portion of the advertisements as solely devoted to Bush and conclude that Bush's attribution

² The Commission explained in the section 106.8 rulemaking that "[g]eneric references to 'our great Republican team' or 'our great Democratic ticket' would satisfy" the requirement for a generic reference to other party candidates. 68 Fed. Reg. 64,518. AO 2006-11 provided "Vote John Doe and our great Democratic team" as an example of a message referencing a clearly identified candidate and generically referring to other party candidates. Nothing in the media advertisements is similar to these generic references.

³ Television advertisements must include a statement identifying the candidate and stating that the candidate approves the communication. 2 U.S.C. § 441d(d)(1); 11 C.F.R. § 110.11(c). The candidate statement shall be an unobscured full screen view of the candidate making the statement or the candidate in voice-over accompanied by a photo or image and shall also appear in writing at the end of the communication in a clearly readable manner with reasonable color contrast for a period of at least 4 seconds. *Id.*

Preliminary Audit Report -- Bush-Cheney '04
(LRA # 664)
Page 5

should be higher than 50%. Conversely, the fact that this disclaimer is legally required might support not considering this portion of the advertisement in calculating an attribution. 2 U.S.C. § 441d(d)(1); 11 C.F.R. § 110.11(c).

Finally, the Commission may not have enough documentation from Bush to determine if the allocation to Bush should not be greater than 50%. The Commission could address this issue by including the finding in the Preliminary Audit Report and requesting additional information from Bush in Bush's response to the Preliminary Audit Report. To receive public funds, the candidate agreed that he had the burden of proving that disbursements are qualified campaign expenses, to meet the documentation requirements for disbursements and to provide an explanation, at the Commission's request, of the connection between any disbursement and the campaign. 11 C.F.R. §§ 9003.1(b), 9003.5. Since Bush disbursed public funds as a part of the joint allocation with the RNC, Bush has the burden of demonstrating that its proposed attribution of the media expenses is appropriate and that only 50% of these media expenses were qualified campaign expenses attributable to Bush.⁴ See 11 C.F.R. §§ 9003.1(b)(1), 9003.5; see also 26 U.S.C. § 9002(11); 11 C.F.R. § 9002.11(b)(3); Cf. *Statement of Reasons in Support of Repayment Determination After Administrative Review for Keyes 2000, Inc.* (approved March 8, 2004) at 24-25 (when a publicly-financed committee engages in dual activities it must be able to document the expenses for each type of activity).

⁴ A qualified campaign expense must, *inter alia*, be incurred "to further" a candidate's election to the office of President or Vice President. 26 U.S.C. § 9002(11); see 11 C.F.R. § 9002.11(a)(1). If a committee also incurs expenses to further the election of one or more individuals to federal or non-federal public office, expenses incurred "which are not specifically to further the election of such other individual or individuals shall be considered as incurred to further the election" of the publicly-financed candidates "in such proportion as the Commission prescribes by rules and regulations." 26 U.S.C. § 9002(11). The regulations state that expenditures that further the election of other candidates for public office shall be allocated and paid in accordance with 11 C.F.R. § 106.1(a) and will be considered qualified campaign expenses "only to the extent that they specifically further the election of the candidate for President or Vice President." 11 C.F.R. § 9002.11(b)(3).

Media Vendor Earned Interest

Summary

Two media vendors earned interest totaling \$14,499 from McCain-Palin 2008 Inc.'s (General Committee) funds. The interest was maintained in the media vendors' accounts and was not used to purchase media buys or to offset commissions. There is no recommendation for payment to the U.S. Treasury since the General Committee did not benefit from the earned interest.

Legal Standard

A. Investment of Public Funds: Other Uses Resulting in Income. Investment of public funds or any use of public funds that results in income is permissible, provided that an amount equal to all net income derived from such use, less Federal, State and local taxes paid on such income, shall be paid to the Secretary. 11 CFR §9004.5.

B. Income on Investment or Other Use of Payments from the Fund. If the Commission determines that a candidate received any income as a result of an investment or other use of payments from the fund pursuant to 11 CFR §9004.5, it shall so notify the candidate, and such candidate shall pay to the United States Treasury an amount equal to the amount determined to be income, less any Federal, State or local taxes on such income. 11 CFR §9007.2(b)(4).

Facts and Analysis

A. Facts

The General Committee used four media vendors during the general election campaign: one main media consultant and three media subcontractors. Two of the subcontractors did not have interest-bearing accounts, but the main media consultant, MH Media, and one subcontractor, Smart Media Group (SMG), did have accounts that earned interest.

MH Media maintained two separate accounts for the General Committee and the Republican National Committee (RNC) and the funds were not comingled. The General Committee and the RNC deposited funds in its respective MH Media account. Both accounts then wired money to the subcontractors for media buys. Each MH Media account had a corresponding sweep account that earned interest. MH Media transferred the General Committee's funds from the deposit account to the corresponding sweep account. The funds earned interest and then were transferred back into the deposit account. The same procedure was performed between the two RNC accounts. The sweep account for the General Committee earned interest totaling \$1,325 between September 1, 2008 and November 1, 2008.

SMG was the subcontractor responsible for most television media buys. SMG set up three different accounts in order to differentiate between the types of media buys:

- o Smart Media Group McCain Palin 2008 Hybrid Account (only General funds deposited)

- Smart Media Group McCain Palin General Account (only General funds deposited)
- Smart Media Group RNC Account (only RNC funds deposited)

Each SMG account had a corresponding overnight sweep account and a master note account that earned interest:

- Hybrid Account: McCain Automated Sweep Advantage; McCain Palin 2008 Hybrid Master Note Sweep
- General Account: McCain Palin 2008 General Sweep Advantage; McCain Palin 2008 General Account Master Note Sweep
- RNC Account: RNC Sweep Advantage; RNC Master Note Sweep

The overnight sweep accounts would transfer monies in and out over a one-day span and the master note accounts would transfer monies over an eight to nine-day span. An SMG representative stated that the reason for the sweep accounts was added security of funds. The total interest earned on the four sweep and master accounts that maintained the General Committee funds was \$13,174 from August 29, 2008 through January 31, 2009.

The combined interest earned by the two media vendors with the General Committee's funds is \$14,499 (as presented below). The General Committee representative stated that the media vendors were advised to keep all earned interest separate and not to use earned interest for media buys or any compensation. Smart Media Group transferred its interest to another account and did not use the funds. Smart Media Group also paid taxes on the interest. MH Media kept its earned interest in the deposit accounts. Both media vendors provided documentation such as bank statements and general ledgers to demonstrate the earned interest was not consumed. The following displays the interest earned in each account.

MH Media McCain General Sweep	\$1,325
SMG McCain Palin 2008 General Account Master Note Sweep	\$2,581
SMG McCain Palin 2008 General Sweep Advantage	\$3,025
SMG McCain Palin 2008 Hybrid Master Note Sweep	\$3,266
SMG McCain Automated Sweep Advantage	<u>\$4,302</u>
Total Interest Earned General Committee Funds	\$14,499

Interest earned by media vendors was an issue in the 2004 Presidential General Election. The Commission discussed whether the interest would be subject to repayment pursuant to 11 CFR §9007.2(b)(4). *See* 11 CFR §9004.5. Some Commissioners held the view that the standard for repayment should be whether the committee actually received or benefited from the interest earned by having the interest used to make media buys or to offset commissions. In the Report of the Audit Division on Kerry-Edwards 2004, Inc., the Commission approved a finding that recommended a repayment to the U.S. Treasury for media interest that apparently was used to pay for media buys or to offset commissions. Interest earned by media vendors that the committee did not actually receive or benefit from did not receive the required four affirmative votes among Commissioners necessary to make a finding.

B. Committee Response to Audit Fieldwork

The Audit staff presented this matter to the General Committee representatives. In response, the General Committee provided a narrative stating the interest earned by the media vendors was not used to buy media time, offset commission and fees or subsidize any Campaign activity. The General Committee made the point that the media vendors were independent subcontractors.

“They were not created by any member of the Campaign’s staff for the purpose of doing business with the Campaign. These companies’ purpose was to purchase advertising time on thousands of radio and TV station vendors and supervise production of our ads. They ensured that paid services – in this case, media placement and production - were actually rendered and delivered to local media outlets and other vendors. After the campaign delivered payment to these vendors’ accounts for ordered items, the Campaign relinquished all access to, control of, and interest in the funds. Disbursed monies belonged solely to the vendor.”

The General Committee also stated that it pre-paid other vendors for goods and services, and the vendors may have earned interest on the payments. The media vendors should not be held to a different standard.

The Audit staff believes that interest totaling \$14,499 earned on these accounts is not subject to repayment to the U.S. Treasury since the General Committee did not receive or benefit from the interest earned. As a result, there is no finding or recommendation in the preliminary audit report for repayment to the U.S. Treasury.

Hybrid Communications

Summary

The Republican National Committee spent \$30,749,009 on hybrid media ad communications related to the General election that were not applied to the coordinated spending limitation or the General Committee’s spending limitation. Excessive in-kind contributions resulting from hybrid communications did not receive the four affirmative votes necessary for a finding in the audit reports of both 2004 general election candidates. Therefore, the following facts are provided for informational purposes only.

Legal Standard

A. Allocation of Expenses for Political Party Committee Phone Banks. Allocation of expenses for political party committee phone banks that refer to a clearly identified Federal candidate can be paid 50 percent by the Federal candidate and 50 percent by the national party with Federal funds subject to the limitations, restrictions and requirements of 11 CFR 109.32 and 109.33 without coordination if:

- (1) The communication refers to a clearly identified Federal candidate;
- (2) The communication does not refer to any other clearly identified Federal or non-Federal candidate;

- (3) The communication includes another reference that generically refers to other candidates of the Federal candidate's party without clearly identifying them;
- (4) The communication does not solicit a contribution, donation, or any other funds from any person; and
- (5) The phone bank is not exempt from the definition of "contribution" under 11 CFR 100.89 and is not exempt from the definition of "expenditure" under 11 CFR 100.149. 11 CFR §106.8.

B. Coordinated Party Expenditures in Presidential Elections.

- (1) The national committee of a political party may make coordinated party expenditures in connection with the general election campaign of any candidate for President of the United States affiliated with the party.
- (2) The coordinated party expenditures shall not exceed an amount equal to two cents multiplied by the voting-age population of the United States, 11 CFR 110.18. This limitation shall be increased in accordance with 11 CFR 110.17.
- (3) The coordinated party expenditures shall be in addition to:
 - Any expenditure by a national committee of a political party serving as the principal campaign committee of a candidate for President of the United States; and
 - Any contribution by the national committee to the candidate permissible under 11 CFR 110.1 or 110.2.
- (4) Any coordinated party expenditures made by the national committee of a political party pursuant to paragraph (a) of this section or made by any other party committee under authority assigned by a national committee of a political party under 11 CFR 109.33, on behalf of that party's Presidential candidate shall not count against the candidate's expenditure limitations under 11 CFR 110.8. 11 CFR §109.32(a).

C. Expenditure Limitation for President. The national party committees have an expenditure limitation for their general election nominee for President. The formula used to calculate the Presidential expenditure limitation considers not only the price index but also the total state voting-age population (VAP) of the United States. The Department of Commerce also publishes the total VAP of the United States annually in the Federal Register. 11 CFR §110.18.

The formula used to calculate this expenditure is two cents multiplied by the total VAP of the United States (227,719,424), multiplied by the price index. Amounts are rounded to the nearest \$100. 2 U.S.C. §441a(d)(2) and 11 CFR §109.32(a). Based upon this formula, the expenditure limitation for 2008 Presidential nominees is \$19,151,200. Federal Register/Vol. 73, No. 31/Thursday, February 14, 2008/Notices.

Facts and Analysis

A. Facts

The Republican National Committee (RNC) spent \$30,749,009 on its share of media ads considered to be "hybrid communications." Such communications referenced Senator John McCain or his general election opponent, then-Senator Barack Obama, and made

references to one of the two major parties. These hybrid communications were paid 50/50 between the RNC and the General Committee. The General Committee's portion of the hybrid expenditures (50 percent) was applied to the spending limitation. The RNC's portion of the hybrid expenditures (50 percent) was not applied to its coordinated spending limit (2 U.S.C. §441a(d)).

National party committees each had a coordinated spending limit of \$19,151,200 for their respective 2008 general election candidates. As noted below, the RNC applied expenditures totaling \$18,834,336 toward its coordinated spending limit. Therefore, without applying any costs associated with hybrid communications, the RNC had \$316,864 remaining under the coordinated spending limitation for Senator McCain's presidential campaign.

441a(d) Coordinated Activity :

Media Ads	\$11,262,437
Calls/Surveys	\$1,559,472
Consultant Travel/Other	\$178,409
Printed Mailers/Postage	\$5,648,706
Campaign Accessories	\$135,048
Media Radio Buys	<u>\$50,264</u>
Total 441a(d) Coordinated	\$18,834,336

B. Spending Limitation Analysis

The General Committee accepted public funds of \$84,103,800 and therefore agreed to a spending limitation of the same amount. If the Commission were to consider the RNC's portion of hybrid communications as in-kind contributions to the General Committee by the RNC, then an excessive in-kind contribution totaling \$30,432,145 (\$30,749,009 - \$316,864) would result since the RNC had spent more than its 441a(d) limitation. The potential excessive amount received by the General Committee would be repayable to the U.S. Treasury. It is noted that possible excessive in-kind contributions resulting from hybrid communications did not receive the four affirmative votes necessary for a finding in the audit reports of both 2004 presidential candidates in the general election.

Summary of Previous Audits

Name of Committee: McCain 2000, Inc.
Election Cycle Audited: 1999-2000 (Presidential Primary)
Final Audit Report Release Date: April 24, 2002

Finding 1- Apparent Non-Qualified Campaign Expenses

The Audit staff identified non-campaign related disbursements totaling \$6,038 and lost equipment with a Fair Market Value of \$23,983. As a result, the Commission determined that a pro-rata repayment to the U.S. Treasury in the amount of \$1,998 for the non-campaign related disbursements and \$7,934 for the lost equipment was warranted.

Finding 2- Determination of Net Outstanding Campaign Obligations

The Audit staff conducted an analysis of the Committee's financial position and concluded that the Committee did not receive matching funds in excess of its entitlement.

Finding 3- Stale-Dated Checks

The Audit staff identified checks issued by the Committee totaling \$85,017, which had not been negotiated. The Commission determined that this amount was payable to the U.S. Treasury.

Name of Committee: McCain 2000 Compliance Committee, Inc.
Election Cycle Audited: 1999-2000 (Presidential Primary)
Final Audit Report Release Date: April 24, 2002

Finding 1- Misstatement of Financial Activity

The Compliance Committee's reported receipts and ending cash balance for 2000 were misstated mainly due to \$3,000 of unreported contributions. The Compliance Committee refunded the contributions and filed amended disclosure reports, which materially corrected the misstatements.

Finding 2- Stale-Dated Checks

The Audit staff identified checks issued by the Compliance Committee totaling \$4,088, which had not been negotiated. The Commission determined that this amount was payable to the U.S. Treasury.