

RECEIVED
FEDERAL ELECTION
COMMISSION
SECRETARIAT



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

2007 MAR 15 P 1:33

March 14, 2007

MEMORANDUM

AGENDA ITEM

For Meeting of: 03-22-07

To: The Commissioners

Through: Patrina M. Clark
Staff Director

Margarita Maisonet
Chief Compliance Officer

From: Joseph F. Stoltz
Assistant Staff Director
Audit Division

Alex Boniewicz
Audit Manager

Tesfai Asmamaw
Lead Auditor

Subject: Final Audit Report - Bush-Cheney '04, Inc. (General Committee) and the Bush-Cheney '04 Compliance Committee, Inc.

Attached for your approval is the subject report along with the legal analysis prepared by the Office of General Counsel.

In its legal analysis, Counsel has suggested the Commission consider the following regulatory structures in determining the rate the General Committee should have paid for air travel reimbursed at the first class rate instead of the charter rate, and that this memorandum bring the issues to the Commission's attention:

- The Commission asked the General Committee for additional information about the operating authority or certificate for the specific flights, but the Commission did not determine what rate to apply in this audit;
- The Audit staff applied the rate based on the operating authority or certificate the airplanes flew under on the flights at issue. Counsel notes that the regulations and the Explanation and Justification for the regulations (more specifically the bright

line rule adopted in the regulations), suggest that the rate is determined based on the general operating authority or certificates of the airplanes, regardless of the purpose of the flights. However, given the facts here (i.e., complex ownership structures involving airplanes with multiple owners), the Commission should consider some policy issues, both in favor and against the application in the audit report.

- In favor of the audit report's application of the rate are two considerations:
 - (1) Fairness issues of applying the bright line rule to these complex ownership structures, when each owner potentially has a different use of the plane from the others, and does not know how other owners might operate the airplane; and
 - (2) The Explanation and Justification did not fully contemplate these complex ownership structures in the facts at hand.
- Against the application of the rate as presented in the audit report are two other considerations:
 - (1) This application of the rate moves away from a bright line rule and more towards a "use" test, in which the actual certificate or operating authority "used" on the flight determines the rate, which requires further examination beyond that contemplated in the bright line rule; and
 - (2) Such an application could require the expenditure of resources when attempting to abide by the travel regulations.

For a full discussion of these issues, please refer to the attached Legal Analysis.

Recommendation

The Audit staff recommends that the report be approved.

It is recommended that the report be considered at the open session meeting of March 22, 2007. If you have any questions, please contact Alex Boniewicz or Tesfai Asmamaw at 694-1200.

Attachments:

Report of the Audit Division on Bush-Cheney '04, Inc. and the Bush-Cheney '04 Compliance Committee, Inc.

Legal Analysis prepared by the Office of General Counsel



Report of the Audit Division on Bush-Cheney '04, Inc. and the Bush-Cheney '04 Compliance Committee, Inc.

July 2, 2003 – December 31, 2004

Why the Audits Were 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 audits determine 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 Campaign

Bush-Cheney '04, Inc. (General Committee) is the principal campaign committee for President George W. Bush, the Republican Party's nominee for the office of President of the United States. The Bush-Cheney '04 Compliance Committee, Inc. (Compliance Fund) was established to accept contributions to be used solely for legal and accounting services to ensure compliance with Federal election laws. Both are headquartered in Arlington, VA. For more information, see chart on the Campaign Organization, p 2.

Financial Activity (p. 2)

Receipts

	<u>General Committee</u>	<u>Compliance Fund</u>
• Federal Funds Received	\$ 74,620,000	
• From Individuals		\$ 11,146,198
• From Political Committees		50,995
• From Authorized Committees		7,171,380
• Offsets	275,751	308,346
• Loan Received	6,500,000	
• Other Receipts	15	123,977
Total Receipts	\$ 81,395,766	\$ 18,800,896

Disbursements

• Operating Expenditures	\$ 72,192,685	\$ 2,643,597
• All Other Disbursements	6,500,015	309,245
Total Disbursements	\$ 78,692,700	\$ 2,952,842

Findings and Recommendations – General Committee

(p. 3)

- Potential In-kind Contributions from Air Charter Providers (Finding 1)
- Expenditure Limitation (Finding 2)

Additional Issues – General Committee (p. 3)

- In-kind Contributions - Republican National Committee Hybrid Ads (Issue 1)
- Interest Income (Issue 2)

Findings and Recommendations – Compliance Fund (p. 3)

Based upon our examination of the reports and statements filed by the Compliance Fund, and the records presented, no material non-compliance was discovered.

¹ 26 U.S.C. §9007(a).

**Report of the Audit Division on
Bush-Cheney '04, Inc. and the
Bush-Cheney '04 Compliance
Committee, Inc.**

July 2, 2003 – December 31, 2004



Table of Contents

	Page
Part I. Background	
Authority for Audits	1
Scope of Audits	1
Inventory of Campaign Records	1
Part II. Overview of Campaign	
Campaign Organization	2
Overview of Financial Activity	2
Part III. Summaries	
Findings and Recommendations – General Committee	3
Additional Issues – General Committee	3
Findings and Recommendations – Compliance Fund	3
Part IV. Findings and Recommendations - General Committee	
Finding 1. Potential In-kind Contributions from Air Charter Providers	4
Finding 2. Expenditure Limitation	7
Part V. Additional Issues - General Committee	
Issue 1. In-kind Contributions – Republican National Committee Hybrid Ads	10
Issue 2. Interest Income	11
Part VI. Findings and Recommendations - Compliance Fund	
Based upon our examination of the reports and statements filed by the Compliance Fund, and the records presented, no material non-compliance was discovered.	12
Part VII. Attachment	
Statement of Net Outstanding Qualified Campaign Expenses	13

Part I

Background

Authority for Audits

This report is based on audits of Bush Cheney '04, Inc. (General Committee) and Bush-Cheney '04 Compliance Committee, Inc. (Compliance Fund). The audit is 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." 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 Audits

These audits 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 campaign's compliance with spending limitations.
10. Other campaign operations necessary to the review.

Inventory of Campaign Records

The Audit staff routinely conducts an inventory of campaign records before it begins the audit fieldwork. The General Committee's and the Compliance Fund's records were materially complete and the fieldwork began immediately.

Part II

Overview of Campaign

Campaign Organization

	General Committee	Compliance Fund
Important Dates		
• Date of Registration	08/04/2004	07/17/2003
• Audit Coverage Dates	09/1/2004 thru 12/31/2004	07/02/2003 thru 12/31/04
Headquarters	Arlington, VA	Arlington, VA
Bank Information		
• Bank Depositories	1	1
• Bank Accounts	6 Checking Accounts	7 Checking Accounts and 1 Investment Account
Treasurer	David Herndon 08/04/2004 – 01/17/06 Salvatore Purpura 01/18/06 - present	David Herndon 07/17/2003 – 01/17/06 Salvatore Purpura 01/18/06 - present

Overview of Financial Activity (Audited Amounts)

	General Committee	Compliance Fund
Opening Cash on Hand	\$ 0	\$ 0
Receipts		
• From Individuals		\$ 11,146,198
• Federal Funds Received	\$ 74,620,000	
• From Political Committees		50,995
• From Authorized Committees		7,171,380
• Offsets	275,751	308,346
• Loan Received	6,500,000	
• Other Receipts	15	123,977
• Total Receipts	\$ 81,395,766	\$ 18,800,896
Disbursements		
• Operating Expenses	\$ 72,192,685	\$ 2,643,597
• Transfers to Other Authorized Committees		100
• Loan Repayments Made	6,500,015	
• Refunds to Contributors		246,107
• Other Disbursements		63,038
• Total Disbursements	78,692,700	2,952,842
Closing Cash Balance @12/31/2004	\$ 2,703,066	\$ 15,848,054

Part III

Summaries

Findings and Recommendations – General Committee

Finding 1. Potential In-kind Contributions from Air Charter Providers

It appeared that the General Committee may have reimbursed for the use of private aircraft at an amount less than that required potentially resulting in the receipt of in-kind contributions of \$69,678. In response to the Preliminary Audit Report recommendation, the General Committee provided documentation demonstrating that the amount it paid for each aircraft was the correct reimbursement as a matter of law or fact. (For more detail, see p. 4)

Finding 2. Expenditure Limitation

The expenditure limitation for the 2004 general election for the office of President of the United States was \$74,620,000. Based on the Commission's actions regarding the Findings and issues contained in this Report, the Audit staff's review of financial activity through December 31, 2006 and estimated winding down costs indicates that the General Committee has not exceeded the limitation. (For more detail, see p. 7)²

Additional Issues – General Committee

Issue 1. In-kind Contributions – Republican National Committee Hybrid Ads

See discussion at page 10.

Issue 2. Interest Income

Interest accrued on funds transferred from the General Committee to two media accounts totaled \$19,745. (For more detail, see p. 11)

Findings and Recommendations – Compliance Fund

Based upon our examination of the reports and statements filed by the Compliance Fund, and the records presented, no material non-compliance was discovered. (For more detail, see p. 12)

² As discussed in Part V, below, some Commissioners are of the opinion that the 50% allocation of the cost of hybrid ads between the RNC and the General Committee was not in compliance with the Act and Commission regulations and that, therefore, the General Committee should have paid more than 50% of these costs. Approval of this audit report does not reflect approval by those Commissioners of a 50% allocation. The Audit staff notes that, had the Commission taken action on the issues raised in Part V, such action would have resulted in an adjustment of the expenditure limit calculations, and therefore, an Audit staff finding of expenditures over the allowable limits. Some Commissioners considered the 50% allocation to be in accord with past precedent and relevant Commission regulations, so there was no adjustment required against the expenditure limits applicable to the General Committee.

Part IV

Findings and Recommendations – General Committee

Finding 1. Potential In-kind Contributions from Air Charter Providers

Summary

It appeared that the General Committee may have reimbursed for the use of private aircraft at an amount less than that required potentially resulting in the receipt of in-kind contributions of \$69,678. In response to the Preliminary Audit Report recommendation, the General Committee provided documentation demonstrating that the amount it paid for each aircraft was the correct reimbursement as a matter of law or fact.

Legal Standard

Contributions Not Permitted. In order to be eligible to receive any payments from the Presidential Election Campaign Fund, the candidate of a major party in a presidential election shall certify to the Commission that no contributions to defray qualified campaign expenses have been or will be accepted by such candidates or any of their authorized committees except to the extent necessary to make up any deficiency in payments received out of the fund. 26 U.S.C. §9003(b)(2).

Contribution defined. A gift, subscription, loan (except when made in accordance with 11 CFR §§100.72 and 100.73), advance, or deposit of money or anything of value made by any person for the purpose of influencing any election for Federal office is a contribution. The term anything of value includes all in-kind contributions.

The usual and normal charge for a service is the commercially reasonable rate that one would expect to pay at the time the services were rendered.

The provision of services at a charge less than the usual and normal charge results in an in-kind contribution. The value of such a contribution would be the difference between the usual and normal charge for the services and the amount the political committee was billed and paid. 11 CFR §100.52 (a) and (d).

Repayment for Contributions Accepted. If the Commission determines that an eligible candidate of a major party, the candidate's authorized committee(s) or agent(s) accepted contributions to defray qualified campaign expenses (other than contributions to make up deficiencies in payments from the fund, or to defray expenses incurred for legal and accounting services in accordance with 11 CFR §9003.3(a)), it shall notify the candidate of the amount of contributions so accepted, and the candidate shall pay to the United States Treasury an amount equal to such amount. 11 CFR §9007.2(b)(5).

Travel by Airplane – Prior to January 14, 2004. A candidate or person traveling on behalf of the candidate who uses an airplane owned or leased by a corporation not licensed to provide commercial service must reimburse the corporation the first class air fare for travel between cities with regular commercial service or the usual charter rate where no regular commercial service exists. 11 CFR §114.9(e).

Travel by Airplane – On or After January 14, 2004. Campaign travelers who use an airplane that is licensed by the Federal Aviation Administration to operate for hire under 11 CFR part 121, 129 or 135 are governed by the definition of a contribution at 11 CFR §100.52(a) and (d). 11 CFR §100.93(a)(2).

Contributions by a Limited Liability Company (LLC): An LLC not electing treatment as a corporation under federal tax law or not having publicly-traded shares will be considered as having been made from a partnership and governed by the rules pertaining to partnerships. 11 CFR §§110.1(b)(1) and (g)(2) and (4).

Facts and Analysis

Effective January 14, 2004, the Commission revised its air travel regulations. Prior to the rule change, air travel was governed by:

- 11 CFR §114.9 – for travel on airplanes *owned or leased* by a corporation or labor organization and *not licensed* to offer commercial services between locations served by regularly scheduled commercial service, the service providers would be paid first class airfare.
- 11 CFR §100.52 – for travel on airplanes *not owned or leased* by a corporation or labor organization, the service providers would be paid the usual and normal charge (the charter rate).

After the rule change, the regulations included a provision that dictated which reimbursed rate is applicable based on how the aircraft is licensed to operate, not on the ownership status:

- 11 CFR §100.93 – for travel on airplanes *not licensed* by the Federal Aviation Administration (FAA) to operate for compensation or hire under 14 CFR Part 121, 129 or 135, the service providers would be paid first class airfare.
- 11 CFR §100.52 – for travel on airplanes *licensed* by the FAA to offer commercial service, the service providers would be paid the usual and normal charge (the charter rate).

However, in promulgating these new aircraft regulations an inadvertent delay in the publication of the effective notice may have caused confusion as to which regulation was applicable to publicly funded candidates in the 2004 general election. As a result, if the General Committee complied with either the old or the new rules it was considered to be in compliance.

The General Committee reimbursed eight providers of ten flights at the first class rate, for a total of \$29,492. All flights occurred on separate days between September 2004 and

November 2004. The providers of these flights included individuals, LLCs³ and commercial charter companies.

All of these trips were flown on planes which were certified for commercial service by the FAA under 14 CFR parts 121, 129, or 135; and in addition, the service providers did not appear to be corporations or labor organizations. It was unclear if these planes were also certified by the FAA to fly under 14 CFR parts 91 or 125. More information was requested on the nature of the planes, the contracting arrangement, and what FAA certificate or operating authority the planes were flown under for these specific trips. However, given the information the Audit staff had, reimbursement for these flights should have been made at a charter rate.

The Audit staff used the 2004 Spring Charter Guide⁴ to determine rates for each flight. Based on the original information provided by the General Committee and other information provided by the FAA, the Audit staff calculated the charter rate cost of each trip using the hourly charter rate for each flight leg and the length of each flight. Thus, for the service provided, at the charter rate the General Committee should have paid \$99,170. By failing to pay a charter rate, the General Committee potentially received in-kind contributions of \$69,678 (\$99,170 - \$29,492).

At the exit conference and in subsequent emails, the Audit staff provided a work paper detailing these flights and discussed the matter with General Committee representatives.

Preliminary Audit Report Recommendation and Committee Response

The Preliminary Audit Report recommended that the General Committee provide documentation that:

- demonstrated that the amount it paid for each aircraft was the correct reimbursement as a matter of law or fact; or,
- demonstrated a lower charter rate is applicable.

Absent such a demonstration, the Audit staff would recommend that the Commission make a determination that \$69,678 is repayable to the United States Treasury.

The General Committee submitted documentation that demonstrated that all questioned flights were flown under 14 CFR Part 91 or the provider was a corporation; and, as such, the first class rate reimbursed by the General Committee is acceptable. The documentation provided is described below:

³ Documentation detailing some of the LLC's filing status election for federal tax purposes was not provided during audit fieldwork.

⁴ Audit staff used the 2004 Spring Charter Guide because the 2004 Fall Charter Guide was not available until December 2004.

- For two trips, NetJets⁵ provided Flight Itinerary Statements which included the flight rule or code, indicating these flights operated under 14 CFR Part 91, the date of the flight, passenger lists and departure and arrival information.
- For one trip, CitationShares provided a Flight Log which included the flight rule or code, indicating the flight operated under 14 CFR Part 91, the date of the flight, the number of passengers and the departure and arrival information.
- For one trip, a letter was provided from Flight Options that stated that the flights were flown under 14 CFR Part 91.
- For one flight, a letter from the Vice President of Operations for Bombardier stated that the flight was flown under 14 CFR Part 91.
- Stargazer Aviation, whose business was chartering flights, requested that its 135 certificate be suspended during the time that it provided two flights and, as such, would then be operating under 14 CFR Part 91. A letter was provided from the FAA's Flight Standards District Office in San Antonio, Texas noting that the suspension was accepted.
- Two flights were offered by an LLC which was formed by an incorporated entity to limit potential liability and is treated as a "disregarded entity" and does not file its own tax return. The LLC's income and expenses flow into the tax statements for the corporation. A signed letter noting this information was provided by the Assistant Treasurer for the LLC.
- For the remaining flight, a letter was provided from the Executive Assistant to the owner of the plane that attests that the flight was flown under 14 CFR Part 91. A "Trip Report" was also provided which stated "Own" under "Type Flight." The letter states that this is short for owner, which is how their flight department identifies a Part 91 flight.

Finding 2. Expenditure Limitation

Summary

The expenditure limitation for the 2004 general election for the office of President of the United States was \$74,620,000. Based on the positions of the Commission regarding the Findings contained in this Report, the Audit staff's review of financial activity through December 31, 2006, and estimated winding down costs, indicates that the General Committee has not exceeded the limitation.

⁵ Netjets, CitationShares, Flight Options and Bombardier offer fractional ownership of jets, and, in effect, operate as management companies for the provision of jet services.

Legal Standard

Expenditure Limitation. No candidate for the office of President of the United States eligible under 2 U.S.C. §9003 to receive payments from the Secretary of the Treasury may make expenditures in excess of \$20,000,000 as adjusted for the increases in the Consumer Price Index. The expenditure limitation for the 2004 general election for the office of President of the United States was determined to be \$74,620,000. 2 U.S.C. §441a(b)(1)(B) and (c).

Repayments. If the Commission determines that the eligible candidate of a political party and their 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 9004, 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(b)(2).

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).

Expenditure Report Period. In the case of a major party, the expenditure report period begins on the earlier of September 1 before the election or the date on which the major party's nominee is chosen. The period ends 30 days after the Presidential election. For President Bush, the expenditure report period ran from September 1, 2004 to December 2, 2004. 26 U.S.C. §9002(12).

Facts and Analysis

As noted above, the expenditure limitation for the 2004 general election for the office of President of the United States was \$74,620,000. Shown on the next page is the Audit staff's analysis of expenditures subject to the limitation.

Reported Operating Expenditures at December 31, 2006	\$ 76,359,412
Add: Accounts Payable	6,944
Estimated Winding Down Costs (January 1, 2006 to May 31, 2007)	210,185
Less: Due from Bush-Cheney '04 (Primary), Inc.	(131,972)
Due from the Compliance Fund	(611,872)
Other Offsets to Operating Expenditures	(833,386)
Accounts Receivable	<u>(379,311)</u>
Net Expenditures Subject to the Limitation	\$ 74,620,000
Expenditure Limitation	<u>74,620,000</u>
Amount In Excess of the Limitation	<u>\$ -0-</u>

As the chart demonstrates, based on the positions of the Commission regarding the Findings contained in this Report, the Audit staff's review of financial activity through December 31, 2006, and estimated winding down costs, indicates that the General Committee has not exceeded the limitation.⁶

Further, the General Committee filed a Statement of Net Outstanding Qualified Campaign Expenses. The Statement of Net Outstanding Qualified Campaign Expenses, prepared by the Audit staff, can be found at page 13. It presents the General Committee's financial position as of December 2, 2004, the end of the expenditure report period; and is adjusted for the General Committee's financial activity through December 31, 2006. The NOQCE supports the result of the expenditures subject to the limitation analysis.

⁶ As discussed in Part V, below, some Commissioners are of the opinion that the 50% allocation of the cost of hybrid ads between the RNC and the General Committee was not in compliance with the Act and Commission regulations and that, therefore, the General Committee should have paid more than 50% of these costs. Approval of this audit report does not reflect approval by those Commissioners of a 50% allocation. The Audit staff notes that, had the Commission taken action on the issues raised in Part V, such action would have resulted in an adjustment of the above expenditure limit calculations, and therefore, an Audit staff finding of expenditures over the allowable limits. Some Commissioners considered the 50% allocation to be in accord with past precedent and relevant Commission regulations, so there was no adjustment required against the expenditure limits applicable to the General Committee.

Part V

Additional Issues – General Committee

Issue 1. In-kind Contributions – Republican National Committee Hybrid Ads

Facts and Analysis

The cost of media ads that identified President Bush and/or Senator Kerry by name and image and referred to other political figures in Congress as allied with President Bush or Senator Kerry without identifying specific candidates was allocated 50% to the General Committee and 50% to the RNC. Senator Kerry and President Bush were the only candidates clearly identified in the ads. Since these ads contained references such as “our leaders in Congress,” “Congressional leaders,” “liberals in Congress” and “liberal allies,” these ads are termed “hybrid ads.”

The Commission addressed whether a 50% allocation of the cost of these hybrid ads is consistent with Commission precedent and existing regulations:

First, the Commission considered the extent to which, if any, 11 CFR §106.1(a) provides guidance regarding the proper allocation for these hybrid ads. Section 106.1(a) of the Commission’s regulations provides that expenditures made on behalf of more than one clearly identified candidate should be attributed to each candidate according to the benefit reasonably expected to be derived (determined by the proportion of space or time devoted to each candidate as compared to the total space or time devoted to all candidates).

Second, the Commission considered the extent to which, if any, 11 CFR §106.8 provides guidance regarding the proper allocation for these hybrid ads. Section 106.8 of the Commission’s regulations provides that a flat 50% allocation is appropriate for the costs of a phone bank conducted by a political committee that refers to one clearly identified federal candidate and “generically refers to other candidates of the Federal candidate’s party without clearly identifying them,” regardless of the space or time devoted to the clearly identified Federal candidate.

Third, the Commission considered the extent to which, if any, the Commission’s advisory opinion issued to Washington State Democratic Central Committee (AO 2006-11) regarding mass mailings provides guidance regarding the proper allocation for these hybrid ads. In AO 2006-11, the Commission noted that although there are no Commission regulations specifically addressing cost allocation for “hybrid ads” (other than for phone banks), “nonetheless an appropriate method for allocating the costs of” such ads (involving mass mailing costs) is to “apply analogous ‘space or time’ principles” as set out in the Commission’s rules that address ads featuring more than one clearly identified candidate. In advising the Washington State Democratic Central Committee that a “space or time” analysis is relevant, the Commission explained that for mass mailing “hybrid ads” where only one candidate is clearly identified, the ad “serves in large measure the purpose of influencing the election of [that] clearly identified

candidate” and therefore the Commission set a floor, that is, a minimum, of 50 percent that must be attributed to the clearly identified candidate, “no matter how much of the space in the mailing is devoted to that candidate.” AO 2006-11 did not, however, involve a presidential candidate; additionally, AO 2006-11 was issued after the 2004 election.

Fourth, the Commission considered the application of 11 CFR §109.21 and AO 2004-01, issued to Bush-Cheney ‘04, Inc. and Alice Forgy-Kerr for Congress, which provided guidance on attribution of coordinated communications between two authorized committees.

There were not the minimum four affirmative votes among the Commissioners required to make a finding as to whether or not the 50% allocation complied with the Act and Commission regulations. Some Commissioners considered the 50% allocation to be in accord with past precedent and relevant Commission regulations, so there was no adjustment required to expenditures applied to the expenditure limits applicable to the General Committee. Some Commissioners were of the opinion that the Act and Commission regulations regarding hybrid ads require the General Committee to pay more than 50%, in which event any adjustment above 50% would apply against the expenditure limits applicable to the General Committee and would have resulted in an Audit staff finding of expenditures over allowable limits.

Issue 2. Interest Income

Summary

Interest accrued on funds transferred from the General Committee to two media accounts totaling \$19,745.

Legal Standard

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.

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

Interest of \$19,745 was earned on two accounts maintained by media vendors engaged by the General Committee and retained by the vendors. The Commission discussed whether the \$19,745 in interest would be subject to repayment pursuant to 11 CFR §9007.2(b)(4). See 11 CFR §9004.5. After the discussion, there were not the required four affirmative votes among the Commissioners necessary to make a finding. Some Commissioners held

the view that the standard for repayment should be whether the General Committee actually received or benefited from the interest earned by having the interest used to make media buys or to offset commissions. They concluded that because the General Committee did not receive or benefit from the interest earned, no finding or repayment determination would be appropriate. Other Commissioners considered 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. They concluded that repayment under these circumstances may be appropriate.

Part VI.

Findings and Recommendations – Compliance Fund

Based upon our examination of the reports and statements filed by the Compliance Fund, and the records presented, no material non-compliance was discovered.

**Part VII.
Attachment**

**Bush-Cheney '04, Inc.
Statement of Net Outstanding Qualified Campaign Expenses
At December 2, 2004
As Determined on December 31, 2006**

Assets

Cash in Bank			\$4,028,400	
Accounts Receivable:				
Due from the Compliance Fund	\$611,872	(a)		
Due from the Bush-Cheney '04 (Primary), Inc.	131,972	(b)		
Due from other Vendors	<u>1,124,717</u>		1,868,561	
TOTAL ASSETS				\$5,896,961

Obligations:

Accounts Payable:				
For Qualified Campaign Expenses			\$4,747,421	
Due to the Compliance Fund			140,281	(c)
Due to the Bush-Cheney '04 (Primary), Inc.			196,972	(d)
				5,084,674
Winding Down Costs:				
Actual: December 3, 2004 to December 31, 2006	\$602,102	(e)		
Estimated: January 1, 2007 to May 31, 2007	<u>210,185</u>	(f)		812,287
TOTAL OBLIGATIONS				\$5,896,961
NET OUTSTANDING QUALIFIED CAMPAIGN EXPENSES (DEFICIT)				<u>(\$ -0-)</u>

FOOTNOTES TO NOQCE

- (a) This amount represents Compliance Fund reimbursements for compliance related costs paid by the General Committee.
 (b) This amount represents Primary Committee reimbursements for primary expenses paid before December 2, 2004.
 (c) The General Committee owes the Compliance Fund for its portion of allocable expenses.
 (d) The General Committee owes the Primary Committee for its portion of the allocable expenses paid during the campaign.
 (e) The Compliance Fund has also directly paid \$4,186,243 of winding down costs.
 (f) The Audit staff will review the General Committee's disclosure reports and records to compare actual figures with estimates and prepare adjustments accordingly. Further, the General Committee has not exceeded the winding down cost limitation imposed by 11 CFR §9004.11(b).



FEDERAL ELECTION COMMISSION
WASHINGTON D.C. 20463

January 25, 2007

MEMORANDUM

TO: Joseph F. Stoltz
Assistant Staff Director
Audit Division

THROUGH: Patrina M. Clark *jm*
Staff Director *for*
PMC

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: 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 Audit Report ("Proposed Report") on Bush-Cheney '04, Inc. (the "Committee" or "Bush") and the Bush-Cheney '04 Compliance Committee ("GELAC") that you submitted to this Office on October 20, 2006. In this memorandum, we have comments on Finding 1, and concur with any findings not specifically discussed in this memorandum. If you have any questions, please contact Delanie DeWitt Painter or Margaret J. Forman, the attorneys assigned to this audit.¹

¹ The Office of General Counsel recommends that the Commission consider this document in open session since the Report does not include matters exempt from public disclosure. See 11 C.F.R. §§ 9007.1(e)(1), 2.3 and 2.4.

Finding 1. involves Bush's potential receipt of in-kind contributions resulting from air travel that Bush reimbursed at the first class rate instead of the charter rate. The Proposed Report concludes that Bush provided documentation in response to the Preliminary Audit Report demonstrating that the amount it paid for the air travel was correct as a matter of fact or law. We agree with this conclusion. Our conclusion for some of the flights, however, is based on the presumption that the rate is determined based on the operating authority or certificate the airplanes flew under on the actual and specific flights flown. Although the Preliminary Audit Report requested information about the operating authority for the specific flights, the Commission did not settle the issue of how to determine the rate. The regulations and the supporting *Explanation and Justification* suggest that the rate is determined by the general operating authority or certificate of the airplanes, regardless of the purpose of the specific flights. We, therefore, examine this issue below and recommend that the auditors raise this issue in the cover memorandum that forwards the Proposed Report to the Commission. We also recommend that the auditors include more information to support their conclusions in the Proposed Report.

II. POTENTIAL IN-KIND CONTRIBUTIONS FROM AIR CHARTER PROVIDERS

A. Commission should consider regulatory structure in determining the rate the Committee should have paid

We recommend that the Commission consider the following points before it decides the issue of how to determine the rate. The Commission promulgated new travel regulations in 2004 to ensure "a readily discernible bright line" rule, based on existing Federal Aviation Administration ("FAA") regulations, that determines the rate applied to travel on private airplanes. *Explanation and Justification for Section 100.93*, 68 Fed. Reg. 69,583, 69,584 (Dec. 15, 2003). The regulations outline the bright line rule: if an airplane's legal operating authority exists exclusively under part 91 of the FAA regulations (general operating authority), the Committee pays the first class rate pursuant to 11 C.F.R. § 100.93. 11 C.F.R. § 100.93(a)(1); *see* 68 Fed. Reg. at 69,585. If, however, the airplane is certificated to fly under part 135 of the FAA regulations (commuter and on demand operations), the charter rate pursuant to 11 C.F.R. § 100.52(a) and (d) applies. 11 C.F.R. 100.93(a)(2); 68 Fed. Reg. at 69,585.² These regulations focus on how the airplane was licensed at the time of the flights, and do not address how specific flights were operated.

The recordkeeping component of the rule also focuses on how the airplane was licensed at the time of the flights. The Commission structured the rule so that the Committee had a recordkeeping duty to maintain the tail numbers on airplanes flown so that the certification of the airplane (not individual flights) could be verified. 68 Fed. Reg. at 69,592.

² This bright-line rule has been followed in the preliminary audit report for another Title 26 audit, approved by the Commission. This other committee also reimbursed flights flown on private airplane at the first class rate that were certificated by the FAA under 14 C.F.R. part 121, 129 or 135 for commercial service. As a result, the auditors concluded that the committee received an in-kind contribution even though the entity providing the airplanes may not have been operating the airplanes under the commercial certification for the flights in question in that preliminary audit report.

We recognize that the bright line rule, however, is more difficult to apply when there is more than one operating authority of the airplane at the time of the flight. When an airplane's legal operating authority is under more than one part of the FAA regulations, we must then derive which certificate or operating authority determines the rate. For example, when looking up the tail number of an airplane in the FAA's records for the airplanes at issue in Bush, we discovered that the operating authority of these airplanes is derived from both 14 C.F.R. part 91 and part 135.³ We then must decide whether to apply the first class rate (because the airplane is authorized to fly under part 91) or the charter rate (because the airplane is certificated under part 135).

To address this question, we turn to the *Explanation and Justification* and the regulatory history of the bright line rule. The *Explanation and Justification* states that the bright line rule applies "to private jets and other airplanes that are not normally held out to the public, such as airplanes operated *exclusively* under 14 C[.]F[.]R[.] parts 91 or 125." 68 Fed. Reg. at 69,585 (emphasis added). If an airplane is authorized to fly under part 91 and part 135, then it is not operated exclusively under part 91. Therefore, even in instances where the airplane has more than one operating authority, the bright line rule, as written, remains focused on the operating authority at the time of the flight, and, strictly followed, suggests that the charter rate would apply.

The regulatory history of the bright line rule suggests that the Commission should focus on the legal operating authority of the airplane at the time of the flight. The bright line rule replaced the previous rule, which "focused on the use of the airplanes owned by corporations or labor organizations not 'licensed to offer commercial services for travel in connection with a Federal election.'" 68 Fed. Reg. 69,583-69,584 (quoting 11 C.F.R. § 114.9(e) (Jan. 1, 2004)). In the rulemaking for the current regulation, the Commission considered, but rejected applying a test that would require a determination of the normal use for the airplane. The Commission's regulations specifically rejected the "normal use" or normal operation of the airplane and instead focused on the "legal operating authority for the airplane" in determining the rate. 68 Fed. Reg. at 69,584-69,585. Under a "normal use" rule, if an airplane was normally used, or operated, for passenger service for a fee, the charter rate (section 100.52) would apply. *Id.* If the airplane was not normally used in such a manner, then the first class rate (section 100.93) would apply. *Id.* The Commission rejected the "normal use" test because it would unnecessarily make the regulation too complicated. *Id.*; see also *Federal Election Commission v. Specter*, 150 F.Supp. 2d 797 (2001) (case cited in *Explanation and Justification*; new travel regulation intended as a remedy to the ambiguity described in *Specter* in the wording of the old travel regulations of section 114.9(e)). Instead, the bright line rule was designed to make determining which rate to apply easily verifiable. *Id.*

The Commission, however, may wish to consider some policy issues pertaining to the application of the bright line rule to complex ownership structures that require airplanes with multiple operating authorities. There is a fairness question in the context of an ownership

³ Part 91 of the FAA regulations applies as a basic operating authority for all airplanes flying in the United States. 14 C.F.R. § 91.1. Any certificates, such as under part 135 of the FAA regulations, are in addition to part 91 operating authority. See 14 C.F.R. §§ 91.1, 91.1007, 119.1, 135.1.

structure that consists of multiple, part-time owners, each purchasing shares in airplanes that hold multiple operating authorities and certificates. Each owner would potentially have a different use of the airplanes from other owners. A fairness issue arises, therefore, when an owner who operates an airplane exclusively under part 91 of the FAA regulations is required to seek reimbursement at the same charter rate as another owner, unknown to the other owner, who operates the airplane under part 135 of the FAA regulations. Additionally, the Commission's *Explanation and Justification* for the air travel regulations did not fully contemplate these complex ownership structures that, by their very nature, require airplanes holding multiple operating authorities and certificates.⁴

To accommodate the complexities and fairness concerns pertaining to flights flown on airplanes holding multiple operating authorities and certificates due to the requirements of these complex ownership structures, the Commission could consider applying the legal operating authority for each flight, rather than the operating authority for the airplane. There are, however, some policy considerations that support a test that is based on the legal operating authority of the airplane at the time of the flight.

Focusing on the legal operating authority for each flight is less straightforward than focusing on the operating authority for the airplane. If the Commission uses a test that focuses on each flight, then the Commission is moving more towards a "use" test, in which the Commission must examine the certificate or operating authority that was actually "used" on that flight rather than the certificate or operating authority of the airplane itself. This is a significant shift from a bright line rule to a "use" rule, and more similar to the previous "use" rule that applied to corporations and labor organizations, as well as the "normal use" rule specifically rejected in the *Explanation and Justification*. 68 Fed. Reg. at 69,584-69,585; see also 11 C.F.R. § 114.9(e) (Jan. 1, 2004). The Commission would no longer examine the tail number of the airplane to determine the operating authority for that airplane, but must further ascertain how that airplane was used, for each time that the airplane was used, by the campaign.

If the Commission is required to examine the legal operating authority for each flight, this could require an expenditure of more resources from both the Commission and the committees attempting to comply with the travel regulations. This is an important point that suggests that the Commission should not use a test that relies on the operating authority for each flight. As a legal matter, however, we believe that the conclusion that the Commission should use a test that only examines the airplane's operating authority is consistent with the *Explanation and Justification* and the history of the regulations. We understand, nevertheless, the policy arguments on both sides of the issue. These policy arguments require the Commission's

⁴ The *Explanation and Justification* addresses these ownership structures in two contexts, neither of which has direct application in our facts. First, when the Commission was considering the normal use rule, one commentator specifically stated that the Commission should not adopt the normal use rule because of "the varied ownership structures and shared users and uses of a single plane. 68 Fed. Reg. 69584 (Dec. 15, 2003). Second, the *Explanation and Justification* addresses these multi-ownership scenarios in the context of service providers. More specifically, the *Explanation and Justification* addresses the method of identifying the service provider, i.e., the person to be reimbursed for campaign travel, in these complex ownership and leasing structures by looking to the owner or lessee who makes the airplane available for the campaign traveler's use. *Id* at 69585-69586.

consideration. The Office of General Counsel, therefore, recommends that the Audit Division raise this issue in the cover memorandum that forwards the Proposed Report to the Commission.

B. Audit report should include information pertaining to the basis of the conclusion in the travel finding.

We also recommend that the auditors include the underlying information about the flights in question that support their findings and recommendations. In the Proposed Report, the auditors state that Bush "submitted documentation that demonstrated that all questioned flights were flown under 14 C.F.R. part 91 or the provider was a corporation." Proposed Report at 6. The auditors provide no supporting information about these flights. The supporting information is important, because it informs both Bush and the public what Bush has demonstrated to the Commission regarding this finding, and provides openness in the operation of Presidential campaigns. *See Reagan-Bush Committee v. FEC*, 525 F. Supp. 1330, 1340-41 (D.D.C. 1981) (openness and accountability to the public in Presidential campaigns). Specifically, we recommend that for each of the flights, the auditors summarize the information provided by Bush that is relevant to the finding.

CASE INDEX FORM

CASE NO. & NAME: Bush-Cheney '04, Inc. and the Bush-Cheney '04 Compliance Committee, Inc.

STAFF ASSIGNED: Alex Boniewicz, Audit Manager
Tesfai Asmamaw, Lead Auditor
Rhonda Gillingwater, Staff Auditor

TELEPHONE: Audit - 202-694-1200

<u>DATE</u>	<u>DOCUMENT</u>
8-24-05	10-Day Response to Exit Conference (Narrative portion only)
4-13-06	PAR Legal Analysis (Part 1)
5-26-06	PAR Legal Analysis (Part 2)
5-26-06	Preliminary Audit Report
9-28-2006	Response to Preliminary Audit Report (Narrative Only)
1-25-2007	FAR Legal Analysis
3-14-2007	Audit Report

For more information or to request any of the documents listed above, contact Alex Boniewicz at 694-1200.