Docket Nos. RP88-262-000, CP89-917-000, TA89-1-28-000, TA90-1-28-000, RP88-88-002 and RP87-103-000, Panhandle Eastern Pipe Line Company. Initial decision.

PR-4.

Docket Nos. RP88-44-011, 016, 018, RP76-12-000, RP79-12-000, RP85-58-012, 017, 021, 022, 023, 026, 032, RP88-184-002, 004, 005, 006, 010, RP88-185-002, 003, RP88-202-001, 002, RP89-57-001, 003, RP88-184-011, RP88-185-004, RP89-132-004, 005, 007, 009, 011, 012, RP89-230-004, RP90-81-000, 001, 003, 004, TA84-1-33-005, 011, TA84-2-33-013, TA85-1-33-004, 015, 016, 017, TA88-1-33-000, 003, 004, TA88-3-33-003, TA89-1-33-000, 001, 003, TQ89-1-33-002, TM90-3-33-003, 004, TQ91-2-33-002, TQ89-1-33-002, CI81-290-000, CI87-290-002, CI88-605-005, CP87-44-001, CP87-553-001, 002, CP88-77-000, CP88-203-000, 003, CP88-244-001, CP88-270-001, CP88-433-002, CP88-434-003, 004, 005, CP88-700-002, CP89-483-001, CP89-896-001, CP89-1540-002, CP89-1722-001, CP90-1034-001, CP90-1084-002, CP90-1269-002, CP90-1281-002 and CP90-1600-001, El Paso Natural Gas Company. Order on rehearing.

PR-5.

Docket Nos. Docket Nos. RP89-48-011, 013, CP89-1126-001, RP89-222-005, RP89-254-004, CP88-133-002 and CP89-886-002, Transwestern Pipeline Company. Order on rehearing.

PR-6.

Docket Nos. RP91-109-001, CP90-2026,-001, RP90-136-002, RP91-104-002 and RP91-106-002, Transwestern Pipeline Company. Order on rehearing.

PR-7.

Docket Nos. CP91-687-000 and CP90-2275-000, ANR Pipeline Company. Order on certificate.

II. Producer Matters

PF-1.

Reserved

III. Pipeline Certificate Matters

PC-1.

Docket No. RM90-1-001, Revisions to Regulations Governing Authorizations for Construction of Natural Gas Facilities. Final Rule.

PC-2.

Docket No. RM90-7-000, Revisions to Regulations Governing Transportation Under Section 311 of the Natural Gas Policy Act of 1978 and Blanket Transportation Certificates

Docket No. GP88-11-002, Hadson Gas Systems, Inc.

Docket No. CP88-286-004, Cascade Natural Gas Corporation v. Northwest Pipeline Corporation, *et. al.*

Docket Nos. RP88-81-014, RP88-67-033 and RP88-175-002, Texas Eastern Transmission Corporation. Final Rule.

PC-3.

Docket Nos. CP90-1372-000, 001, CP90-1373-000, 001, CP90-1374-000, 001, CP90-1375-000 and 001, Altamont Gas Transmission Company. Order on application for certificate.

PC-4.

Docket Nos. CP89-460-003, 000, 001, 006, 007 and CP90-1-001, Pacific Gas Transmission Company. Order on application for certificate.

PC-5.

Docket No. CP90-2214-001, El Paso Natural Gas Company. Order on application for certificate.

PC-6.

Docket Nos. CP90-2294-000 and 001, Transwestern Pipeline Company. Order on application for a certificate.

PC-7.

Docket Nos. CP88-433-002 and 003, El Paso Natural Gas Company. Order on requests for rehearing.

PC-8.

Docket No. CP91-1379-000, Kern River Gas Transmission Company. Order on application for rehearing.

PC-9.

Docket Nos. CP91-2284-000 and RP91-153-002, East Tennessee Natural Gas Company. Declaratory order regarding transportation under section 311 of the Natural Gas Policy Act.

Lois D. Cashell,

Secretary.

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Part II

Federal Election Commission

11 CFR Part 100, et al.

Public Financing of Presidential Primary and General Election Candidates; Final Rule

FEDERAL ELECTION COMMISSION

[Notice 1991-11]

11 CFR Parts 100, 102, 106, 110, 116, 9001-9007, 9012, and 9031-9039

Public Financing of Presidential Primary and General Election Candidates

AGENCY: Federal Election Commission.

ACTION: Final rule; transmittal of regulations to Congress.

SUMMARY: The Commission has revised its regulations governing publicly financed Presidential primary and general election candidates. These regulations implement the provisions of 26 U.S.C. chapters 95 and 96, the "Presidential Election Campaign Fund Act" and the "Presidential Primary Matching Payment Account Act." The principal changes involve allocation of expenses to the state-by-state spending limits. Other areas in which changes are being made include candidate agreements, the matching fund process, media travel costs, joint fundraising, transfers to compliance funds, and repayment determinations. Further information on these revisions is provided in the supplementary information which follows.

DATES: Further action, including the announcement of an effective date, will be taken after these regulations have been before Congress for 30 legislative days pursuant to 2 U.S.C. 438(d) and 26 U.S.C. 9009(c) and 9039(c). A document announcing the effective date will be published in the **Federal Register**.

FOR FURTHER INFORMATION CONTACT: Ms. Susan E. Propper, Assistant General Counsel, 999 E Street, NW., Washington, DC 20463, (202) 376–5690 or (800) 424–9530.

SUPPLEMENTARY INFORMATION: The Commission is publishing today the final text of revisions to its regulations at 11 CFR 106.2, and Parts 9001–9007, 9012, and 9031–9039, which concern the public financing process for Presidential primary and general election candidates. The Commission is also publishing conforming amendments to §§ 100.8(b), 102.17, 110.1, 110.8, and 116.5. On January 2, 1991, the Commission issued a Notice of Proposed Rulemaking (NPRM) in which it sought comments on proposed revisions to these regulations. 56 FR 106. Written comments were received from the Internal Revenue Service, the Democratic National Committee, and the Gephardt for President Committee in response to the Notice.

Section 438(d) of title 2, United States Code, and 26 U.S.C. 9009(c) and 9039(c) require that any rules or regulations prescribed by the Commission to carry out the provisions of titles 2 and 26 of the United States Code be transmitted to the Speaker of the House of Representatives and the President of the Senate 30 legislative days before they are finally promulgated. These regulations were transmitted to Congress on July 19, 1991.

Explanation and Justification

The Commission has revised its regulations governing publicly financed Presidential primary and general election candidates in several respects. The principal changes involve the allocation of expenses to the state-by-state spending limits, and the exclusion of certain costs from state allocation. Other areas in which changes are made include candidate agreements, media travel costs, joint fundraising, transfers to compliance funds, and repayment determinations.

The Commission has initiated a separate rulemaking to consider possible changes to its matching fund submission and certification procedures set forth at 11 CFR 9034.1, 9034.5, 9036.2, 9036.4, 9036.5, 9036.6, 9037.1 and 9037.2. See notice of proposed rulemaking, 56 FR 29372 (June 26, 1991). A new rulemaking is necessitated by the Department of the Treasury's recent promulgation of new rules regarding payments to candidates, which it adopted to address the possible shortage in the Presidential Election Campaign Fund. See 26 CFR parts 701 and 702, 56 FR 21596 (May 10, 1991).

In the course of this rulemaking, the Commission considered proposals for change that it did not ultimately incorporate into the revised rules. For example, the Commission sought comments on ways to streamline the audit and repayment processes and to encourage quicker termination of committee activity. One possibility considered was to set winding down costs as a fixed percentage of a candidate's total expenditures during the campaign, or as a percentage of total matching funds certified for that candidate. However, the Commission has decided not to change the current approach to winding down costs at this time because other changes in the primary election regulations, such as the revisions to the state allocation rules, should result in quicker completion of the audit and repayment processes.

In addition, two changes have been made throughout these regulations. First, the term "committee assets" is used instead of "campaign assets." Secondly, the cross-references to the convention regulations at 11 CFR part 9008 have been changed back to the current citations, since the reorganization and revision of the convention rules has been suspended until after the 1992 conventions. See 56 FR 14319 (April 9, 1991).

Part 100—Scope and Definitions (2 U.S.C. 431)

Section 100.8 Expenditure (2 U.S.C. 431(9))

The Commission is now revising and simplifying the way in which the 20% fundraising exemption from the overall spending limit for primary candidates is determined. Under the new method set out in § 100.8(b)(21), the amounts excluded at the state level are added to an amount excluded at the national level to permit committees to claim the full benefit of the 20% fundraising exemption established by the FECA. These changes correspond with changes in the method set out in § 110.8(c)(2) for determining the amount of fundraising costs exempt from the state spending limits.

Part 102—Registration, Organization, and Recordkeeping by Political Committees (2 U.S.C. 433)

Section 102.17 Joint Fundraising by Committees Other Than Separate Segregated Funds

The Commission is revising the joint fundraising rules set out at 11 CFR 102.17 in several respects. First, paragraph (a)(1) now specifies that if committees participating in a joint fundraiser elect to form a separate committee to serve as the fundraising representative, the separate committee cannot be a participant in any other joint fundraising efforts but may conduct more than one joint fundraising effort for the participating committees. This change corrects two problems. First, in cases where this has occurred, there was no explicit allocation formula for determining the amounts to be distributed to each of the participating original committees. Secondly, there has been confusion as to the amount that may be contributed to the fundraising representative for distribution among the participating committees. Under new paragraph (c)(7)(i)(C) the expenses for a series of fundraising events or activities must be allocated on a per event basis. This provision parallels language in current § 9034.8(c)(8)(i)(C).

New language is also being added to paragraph (c)(1) to require the allocation formula to indicate the amount or percentage of each contribution that will be allocated to each participant. Thus, the formula may not state that a fixed amount of the proceeds will be allocated to a specific participant, or that contributions will be allocated to one participant because the contributions are matchable. Section 9034.8(c)(7)(i) does not permit the committee to use a joint fundraiser to maximize the matchability of contributions. However, the formula may state, for example, that the first $250 of each contribution will be allocated to a particular candidate. The new rules also delete the previous language in paragraph (c)(1) indicating that the joint fundraising participants must use the formula to allocate fundraising expenses. This change was necessary because paragraph (c)(7) indicates that the joint fundraising representative allocates expenses based on the percentage of total receipts allocated to each participant. Please note that corresponding changes are included in the joint fundraising rules applicable to presidential candidates. See 11 CFR 9034.8.

Part 106—Allocation of Candidate and Committee Activities

Section 106.2 State Allocation of Expenditures Incurred by Authorized Committees of Presidential Primary Candidates Receiving Matching Funds

As in the past, many of the issues arising in the 1988 election cycle involved the allocation of expenses to particular states for purposes of the statutory state-by-state spending limitations for Presidential primary candidates receiving matching funds. 2 U.S.C. 441a(b)(1) and 441a(g). In practice, the state limits have the greatest impact in the states holding the first primaries because the spending limits are based on voting age population and do not recognize that the national importance of these primaries extends well beyond the relatively small numbers of delegates at stake. The national significance of the first primary campaigns is shown by their focus on national issues, their coverage by the national and international press, the candidates' appeals to voters nationwide, and the effect these primaries have in winnowing the field of candidates able to continue to campaign in subsequent primaries. The importance of the early primaries has resulted in creative attempts to reduce the amounts allocated to these states for various activities. This, in turn, has necessitated extensive review of committees' allocation practices during the post-primary audits.

For these reasons, the Commission has now decided to make substantial changes in its regulations to try to resolve some of the current problems and to simplify state allocation. One of the two comments received stated that proposals designed to simplify allocation and to treat these as national primaries "makes eminent sense in the light of experience." As discussed below, the other commenter urged the Commission to take several additional steps in this direction.

Under the new state allocation rules, the detailed list of allocable expenditures and exemptions set out in previous 11 CFR 106.2 is replaced with a more limited set of allocable expenditures that are directly related to the campaigns in particular states. All other expenditures are exempted from state allocation, but not from the overall spending limits. The following expenditures are subject to state allocation:

(1) Expenses for campaign advertising distributed through the broadcast media and print media in a particular state, but excluding production costs, national advertising costs and commissions for media purchases. For broadcast and print media buys distributed to more than one state, allocation is based on the proportion of viewers or readers in each state.

(2) Expenditures for mass mailings where more than 500 pieces are sent to a given state and expenditures for shipping other campaign materials to the state.

(3) Expenditures for special telephone programs targeted at a particular state, such as voter registration, get out the vote, fundraising or telemarketing programs.

(4) Expenditures for public opinion polls, except those conducted on a nationwide basis. Allocable costs are based on the number of people interviewed in each state.

(5) Overhead expenses for state offices, but not for national campaign headquarters. Overhead expenses for regional offices are allocated to the next primary state in the region.

Under the new approach, presidential primary candidates are not required to allocate the following categories of expenditures to specific states:

(1) Interstate and intrastate travel and subsistence expenses for the candidate and his or her campaign staff;

(2) Salaries of campaign staff working in a given state; and

(3) Consulting fees for those consulting on national campaign strategy.

Finally, the new rules simplify the application of the fundraising exemption by allowing committees to treat up to 50% of expenditures allocable to each state as exempt fundraising costs, except that 100% of the costs of mass mailings may be treated as fundraising if the materials were mailed more than 28 days before the primary. This approach revises the 28 day rule previously set forth at 11 CFR 110.8(c)(2) so that the timing of fundraising activities is only significant for mass mailings. In addition, the new rules supersede AO 1988–6 in which the Commission concluded that 50% of the costs of broadcasting a particular advertisement may be excluded from state allocation under the fundraising exemption.

These changes also involve reorganizing § 106.2 in the following respects. Paragraph (a) now sets out the general rule that only the expenditures indicated in this section must be allocated to particular states. Previous paragraphs (b) and (c) have been combined into new paragraph (b) describing allocable expenses. The reporting provisions of former paragraph (d) are now located in paragraph (c). The recordkeeping requirements of previous paragraph (e) have been amended and placed in paragraph (d). The revised state allocation rules in § 106.2 address the following types of expenses:

1. *Media expenditures.* The new rules continue the previous approach requiring allocation of print and broadcast advertising, but excluding national advertising and media production costs from state allocation. However, one modification has been made regarding commissions. Under the old rules, § 106.2(b)(2)(i)(B) provided for state-by-state allocation of any commission charged for the purchase of broadcast media, using industry market data. The new rules specify that commissions, fees, and other compensation for the purchase of broadcast or print media need not be allocated to any State.

The NPRM indicated that the Commission has encountered situations in recent audits in which committees have sought to claim very low amounts as media commissions in comparison to the amounts claimed as production costs, and in comparison to the amounts of commissions in previous presidential election cycles. Consequently, comments were sought on how to determine whether the amount paid to the advertising firm or media consultant represents the usual and normal charge for the services provided. Questions may also arise as to whether media commissions are national or state expenditures. One commenter suggested that because of these difficulties, the

Commission should not allocate media commissions against the state spending ceilings. The Commission has decided to take the approach of not allocating media commissions to the state spending limits. The final rules also include new language to clarify that if industry market data is not available to support state allocation of media advertising costs, market data must be obtained from the media carrier.

2. *Mass mailings and shipping other campaign materials.* New § 106.2(b)(2)(ii) specifically requires the allocation of the costs associated with mass mailings of over 500 pieces to a state and the costs of shipping campaign materials to a state. Such costs were allocable under previous § 106.2, unless they could qualify as fundraising expenses. The new language parallels the concept of mass mailings used in the franked mail statute applicable to members of Congress. 39 U.S.C. 3210(a)(6). In contrast to the previous rules, the new language does not require allocation of the costs of producing materials that are subsequently shipped to a state for distribution. The new mass mailing provision operates in conjunction with the Commission's simplified approach to the fundraising exemptions from the state and overall spending limits set out in § 100.8(b)(21) and 110.8(c)(2). Under the new approach, a committee may treat 100% of mass mail expenses and 50% of campaign material shipping costs as counting against the state or overall fundraising exemptions.

3. *Overhead expenditures for state offices and regional offices.* The Commission is now revising § 106.2(b)(2)(iii) to provide further guidance as to how to allocate overhead expenses of regional offices. Overhead expenses will be allocated to the next primary state in the region. If two or more states in the region hold primaries on the same day, overhead expenses should be apportioned equally between these states.

As under the previous rules, allocation is required for state offices, but with certain exceptions, it is not required for national campaign headquarters. These provisions are also reorganized so that the definition of "overhead expenditure" only appears once. Please note that the State office overhead provision has been revised to clarify that the location of the State office is not controlling, and to clarify that allocable expenses include the costs of facilities used for campaign events in a State. Overhead also includes the cost of temporary offices established while the candidate is traveling in the State or in the final weeks before the primary election, as well as expenses paid by campaign staff and subsequently reimbursed by the campaign, such as miscellaneous supplies, copying, printing, and telephone expenses. See 11 CFR 116.5. However, overhead does not include the cost of vehicles leased for extended periods and used in a particular State, unless these costs are allocable for another reason, such as the use of vehicles for polling purposes.

One comment urged the Commission to exclude from allocation overhead expenses related to dealing with the press and organizing campaign trips and events for the candidate. This suggestion was not adopted because drawing distinctions for different categories of overhead is contrary to the Commission's new approach of creating broad categories of allocable expenses and exempt expenses. The newly created exemptions for travel and salary expenses will result in the exclusion of a substantial amount of expenses. In addition, the final rules concerning overhead permit committees to treat 10 percent of State office overhead expenditures as exempt compliance costs which are therefore excludable from the state spending limits.

4. *Expenditures for special telephone programs.* The Commission is now replacing its previous allocation rules for interstate and intrastate telephone calls with new language at § 106.2(b)(2)(iv) requiring allocation only if the intrastate or interstate telephone calls part of a special telephone programs targeted at a particular state. This includes special programs such as voter registration, get out the vote efforts, fundraising, or telemarketing calls designed to increase candidate recognition and support among voters in the state. These costs are allocable irrespective of whether the calls originated inside or outside the state called. The final rules indicate that "targeted at a particular state" means that 10 percent or more of the total telephone calls made in each month are made to that state. The final rules have been modified from the previous proposals to clarify that the allocable expenses for special telephone programs include consultants' fees, related travel costs, and the costs of office rental. This covers both the costs of renting office space for a limited period specifically for the purpose of conducting the program, as well as a *pro rata* portion of the campaign committee's state office or national headquarters if used to conduct the program. As explained below, consultants' fees are allocable if they relate to conducting special telephone programs or polling activity, but they are not allocable if they are charged for consulting on national campaign strategy.

5. *Public opinion polls.* Paragraph (b)(2)(v) of revised § 106.2 continues the previous approach regarding the allocation of polling expenses. Thus, expenditures incurred for public opinion polls covering one state are allocable to that state. Polls covering two or more states continue to be allocable to those states based on the number of people interviewed in each state, but polls conducted on a nationwide basis are not allocable. The revised rules also specify that allocable expenses include the costs of designing and conducting a poll, such as consultants' fees and travel costs.

6. *Costs excluded from allocation.* As indicated above, the revised allocation rules are intended to eliminate several problems encountered by the Commission and by committees under the previous rules. For example, the previous regulations required the allocation of intrastate travel and subsistence expenses, as well as salary expenses, for persons working in a particular state for five consecutive days or more. 11 CFR 106.2(b)(2)(ii) and (iii). The original purpose of these provisions was to simplify the allocation of travel and salary expenses. However, in administering these requirements, the Commission has found that the rule forced committees to create and maintain travel itineraries for many trips by candidates and campaign staff so that the Commission could determine the length of their stays in particular states. In addition, questions arose as to whether travel expenses of independent consultants, as well as travel and salary costs for a committee's vendors' employees, were also subject to this five day rule. Other questions involved the application of the exemption for interstate travel set out at 11 CFR 106.2(c)(4) in situations where campaign staff commuted on a regular basis to and from airports or hotels located across the border in a neighboring state. Consequently, the effects of the five day rule for salaries and intrastate travel, and the interstate travel exemption were to complicate, not to simplify, allocation.

To alleviate these difficulties, the Commission is now excluding all interstate and intrastate travel and salary expenses from state allocation. This will allow the Commission to devote its limited resources to monitoring other aspects of the Matching Fund Program. Moreover, now that salaries are excluded from state allocation, § 106.2 is being further simplified by eliminating the language that had permitted committees to exclude 10 percent or more of campaign workers' salaries from state allocation as exempt compliance costs. See previous 11 CFR 106.2(c)(5). Please note, however, that salaries continue to be counted against the overall spending limit for primary candidates, and campaigns may continue to deduct 10 percent of salary costs from the overall limits for compliance activities under 11 CFR 9035.1(c).

The Commission has also decided to expressly exclude national consulting fees from allocation. See 11 CFR 106.2(b)(3). This exemption applies to charges for consulting on national campaign strategy, but does not include consulting fees charged for conducting special telephone programs or public opinion polls in a particular state.

7. *Recordkeeping and Allocation to the Next Primary State.* Specific recordkeeping requirements have been included in several sections to indicate particular kinds of records committees must maintain regarding allocable expenses such as direct mail, shipping costs, regional overhead expenses, special telephone programs and polling. See § 106.2(b)(2)(ii), (iii)(B), (iv), and (v). In addition, the final rules add new language at § 106.2(d) generally requiring the retention of all documents supporting allocations of expenditures to particular states and claims of exemption from allocation under this section. If a presidential campaign committee does not maintain these records, the regulations indicate that the expenditures will be considered to be allocable, and shall be allocated to the state holding the next primary election, caucus or convention after the expenditure is incurred. In an appropriate case, the Commission may also wish to pursue the failure to maintain records under 11 CFR 104.14. One commenter indicated that the purposes served by this provision could be accomplished in a less burdensome way, but did not indicate specifically how this could be accomplished.

Part 110—Contribution and Expenditure Limitations and Prohibitions

Section 110.1 Contributions by Persons Other Than Multicandidate Political Committees (2 U.S.C. 441a(a)(1))

The Commission's administration of the public financing laws has highlighted the need for modifications in the documentation requirements for reattributed and redesignated contributions, which are set forth in paragraph (1) of this section. For example, during the audits of several 1988 presidential campaign committees, problems were encountered in verifying that excessive contributions were reattributed to joint contributors or redesignated for compliance funds within the time periods established by 11 CFR 110.1(b) (5) and (k)(3)

To monitor compliance with the time periods established for obtaining reattributions and redesignations, § 110.1(1) is being revised to require committees to retain documentation demonstrating that redesignations and reattributions are received within 60 days. The new language gives committees a fair amount of flexibility as to the type of evidence they may choose to rely upon to demonstrate timely receipt.

Section 110.8 Presidential Candidate Expenditure Limitations

There are two changes in this section. First, in paragraph (f)(2), the citation to former § 141.2(c) has now been changed to current § 9003.2(c).

The other change involves the operation of the fundraising exemption from the state spending limits, which is set out at § 110.8(c)(2). This exemption has been the focus of a number of recent questions. For example, in Advisory Opinion 1988–6 the Commission was presented with the question of whether part of the costs of broadcasting a candidate's political advertisement in a particular state could be treated as an exempt fundraising expense if the advertisement concluded with a brief message urging the viewers to contribute to the candidate's campaign. On the basis of a previous decision made in one of the 1984 presidential audits, the Commission concluded that it would be reasonable for the candidate to allocate 50 percent of the costs of this advertisement to exempt fundraising, provided the advertisement was not broadcast within 28 days before the state's primary election. See previous 11 CFR 110.8(c)(2).

Since that time, presidential campaigns have tried to broaden the application of the fundraising exemption set forth in previous 11 CFR 106.2(c)(5)(ii) and 110.8(c)(2) in a variety of ways. For example, committees have sought to deduct 50 percent or more of the costs associated with candidate appearances at various political events designed to attract voters on the theory that the incidental distribution of solicitation materials is sufficient to qualify for the fundraising exemption. In other situations, committees have sought to apply the fundraising exemption to the costs of a telemarketing program targeted at voters in a key primary state. However, these telephone calls have tended to focus on voter education and garnering support, and have not always included a fundraising appeal. One committee claimed the fundraising exemption for such telephone calls because follow-up letters requesting contributions were sent to some of the voters contacted. Finally, some committees have sought to exclude part of their broadcast media costs from state allocation as exempt compliance costs incurred for including the disclaimer notice required by 2 U.S.C. 441d(a). They have based this allocation on an analogy to the principle set out in AO 1988–6.

To simplify the application of the fundraising exemption, 11 CFR 110.8(c)(2) is being revised to allow committees to treat up to 50 percent of their expenditures allocable to each state as exempt fundraising costs, and to permit these amounts to be excluded from the committees' total expenditures attributable to the spending limit for each state. The total amount excluded may not exceed 20 percent of the overall spending limit under 11 CFR 9035.1. This new approach revises the previous 28 day rule set forth in this section so that the timing of specific fundraising activities is only significant for mass mailings. The new rules implementing this method of calculating the fundraising exemption supersede AO 1988–6.

One reason for establishing a fundraising deduction of up to 50 percent of the state expenditures is that, as the commenters point out, there may be a fundraising component to many of the committee's campaign activities. Moreover, by adopting this change, the Commission will no longer need to examine disbursements claimed under the exemption to determine whether they are related to fundraising efforts.

The Commission decided to allow 100 percent of the cost of mass mailings to be treated as fundraising, unless the materials were mailed within 28 days before the election. Based on previous practice and experience, the Commission concluded that the primary purpose of mass mailings can be presumed to be fundraising until that point.

The NPRM sought comments regarding other ways to accommodate the special needs of candidates who must devote more time and effort to fundraising during the first two primaries to obtain enough money to be perceived as viable candidates for their party's nomination. One commenter urged the Commission to create an additional 20 percent across the board exemption from the spending limits for expenditures made in the early primary states on the grounds that a good portion of the campaign activities in the early primary states is directed at a national audience. The Commission believes that treating 50 percent of state expenditures as exempt fundraising costs will alleviate the commenter's concerns. In addition, the Commission expects that the revised state allocation categories will help to offset the amount of expenses previously allocable to the early primary states.

Part 116—Debts Owed by Candidates and Political Committees

Section 116.5 Advances by Committee Staff and Other Individuals

The definition of subsistence expenses, which was previously located in § 106.2(b)(2)(iii), has been moved to paragraph (b)(2) of § 116.5. Section 106.2 has been revised so that subsistence expenses are no longer allocable.

Part 9001—Scope

Section 9001.1 Scope

The references to the title 2 rules have been revised to reflect the addition of new 11 CFR part 116.

Part 9002—Definitions

There are no changes in §§ 9002.1 through 9002.8, § 9002.10, and § 9002.11.

Section 9002.9 Political Committee

The definition of "political committee" is revised by deleting the reference to former § 9012.6, which no longer exists.

Part 9003—Eligibility for Payments

There are no changes in §§ 9003.2 and 9003.6.

Section 9003.1 Candidate and Committee Agreements

Presidential candidates seeking federal funds for their general election campaigns must agree to comply with all of the conditions set forth in paragraph (b) of this section to be eligible to receive these funds. The Commission is now revising these conditions in two respects. First, the candidate agreement provisions are being revised to conform to the new magnetic media rules regarding the production of computerized information on magnetic diskettes or magnetic tapes in accordance with the new technical standards. See 11 CFR 9003.6, 55 FR 26392 (June 27, 1990).

The Commission also sought comments on requiring presidential candidates and their authorized committees to obtain and provide upon the Commission's request records regarding funds received and disbursements made on the candidate's behalf by other committees and organizations associated with the candidate. One commenter believed this requirement was unnecessary because the Commission already has authority to request and, if necessary, subpoena these records. Nevertheless, the Commission has concluded that inclusion of this requirement in the candidate agreements will ensure a more timely production of pertinent records that the Commission needs to audit the candidate's Presidential campaign committee or to make repayment determinations.

The Commission's proposed rules had included a requirement that candidates agree to file alphabetized schedules if their reports are generated from computerized files. One comment objected to the placement of such a requirement in the candidate agreements. The Commission has now decided not to require the filing of alphabetized schedules. Similarly, the Commission considered and rejected a proposal to add new language to the candidate agreement provisions to require committees to verify that they are not spending possibly illegal contributions while they are making inquiries as to the permissibility of these contributions. One commenter indicated that such a requirement would not add anything to existing law.

Section 9003.3 Allowable Contributions

Paragraphs (a)(1) (ii) and (iii) of § 9003.3 are being revised to resolve questions concerning the ability of campaign committees to seek redesignations to legal and accounting compliance funds of contributions properly received during the primary election campaign. The previous rules at 11 CFR 9003.3(a)(1)(iii) permit committees to seek redesignations to the compliance fund if they receive contributions that either exceed the primary election limits or that are made after the party's presidential nominee is chosen. Campaign committees may also transfer to the compliance fund amounts remaining in the primary election account that exceed the amount that must be reimbursed to the U.S. Treasury under 11 CFR 9038.2. See 11 CFR 9003.3(a)(1)(ii). The question presented was whether a campaign committee could obtain redesignations of contributions properly received during the primary election period. This situation only arises if a primary candidate becomes the nominee in the general election, since other rules apply to unsuccessful primary candidates. Accordingly, the Commission sought comments on revising paragraphs (ii) and (iii) of § 9003.3(a)(1) in the following respects. First, language was proposed to permit transfers to legal and accounting compliance funds only if such amounts are not needed to pay remaining primary obligations. In addition, the changes would have prevented committees from having nonexcessive primary contributions redesignated for the general election compliance fund if these primary contributions represent funds that are otherwise repayable to the Presidential Primary Matching Payment Account as surplus funds under 11 CFR 9038.2. The proposed revisions would also have clarified that redesignated contributions will be subject to the contribution limits for the general election, not the primary.

One comment opposed the redesignation restrictions on the grounds that contributions received late in the primary election season were probably intended for general election compliance purposes and should be so used. The Commission has now modified the proposed rule to permit redesignations for the compliance fund provided that the redesignations are received within 60 days of the Treasurer's receipt of the original contribution, and the committee follows the redesignation procedures set forth at 11 CFR 110.1(b) (5) and (1). In addition, the contributions redesignated must represent funds in excess of any amount needed to pay remaining primary expenses. If this requirement is not met, the committee would have to make a transfer back to the primary account to cover such expenses. Finally, contributions may not be redesignated if they have been submitted for matching.

Paragraph (a)(2) of this section is also being revised to permit contributions to a legal and accounting compliance fund to be used to defray the committee's unreimbursed costs incurred in providing transportation and services for the Secret Service and national security staff.

Section 9003.4 Expenses Incurred Prior to the Beginning of the Expenditure Report Period or Prior to Receipt of Federal Funds

This section generally follows previous § 9003.4.

Section 9003.5 Documentation of Disbursements

Section 9003.5(b)(1)(iv) is being revised to indicate that collateral evidence documenting qualified campaign expenses may include evidence that the disbursement is covered by a preestablished written campaign committee policy, such as a daily travel expense policy. The previous rules had indicated that collateral evidence of a per diem policy would be acceptable. The new, more specific wording is intended to resolve the difficulties surrounding broad per diem policies that do not always provide adequate evidence that the expenses claimed are qualified campaign expenses. The final wording of § 9003.5(b)(1)(iv) represents an improvement over the proposed rules in the NPRM which would simply have required committees to submit collateral evidence showing that "the expenditure is part of an identifiable program or project which is otherwise sufficiently documented." This proposal did not clearly specify what types of documentation would be acceptable. The Commission is also making corresponding revisions to the documentation requirements for primary election committees at 11 CFR 9033.11(b)(1)(iv).

Part 9004—Entitlement of Eligible Candidates to Payments; Use of Payments

There are no changes in §§ 9004.1 through 9004.3, § 9004.5, § 9004.7, or § 9004.8.

Section 9004.4 Use of Payments

In AO 1988–5 questions were raised as to whether a current publicly-funded presidential campaign committee may contribute or loan or transfer funds to another federally funded committee of the same candidate for a previous election cycle for the purpose of paying debts from the earlier campaign. The opinion concluded that such payments are not qualified campaign expenses under 11 CFR 9034.4 and are not includable in the candidate's NOCO statement under 11 CFR 9034.5. However, such payments could be made from excess campaign funds once the audit process is concluded and any repayment or possible penalty obligations have been satisfied.

The attached final rules include new language in § 9004.4(b)(7) applying the conclusion reached in AO 1988–5 to general election candidates. Thus, similar payments from general election funds are nonqualified campaign expenses under § 9004.4(b). Accordingly, they could serve as a basis for a repayment determination under 11 CFR 9007.2. Please note that even though the question presented in AO 1988–5 was framed in terms of treating such payments as contributions, the Commission would regard such a flow of funds as a transfer, not a contribution. See H. Rept. No. 96–422, 96th Cong., 1st Sess. 7 (1979).

Section 9004.6 Reimbursements for Transportation and Services Made Available to Media Personnel

Under this section, candidates may seek reimbursement from media personnel for the costs of providing transportation and services to media representatives accompanying the candidate on campaign trips. These provisions also establish the method to be used in determining how much committees may receive from media personnel for such costs. The Commission is now making several changes to these rules. First, paragraph (a) is being revised to clarify that expenditures incurred for transportation or services made available to Secret Service and national security staff, less any reimbursements received, are qualified campaign expenses but not subject to the overall spending limit. This language allows the campaign to pay unreimbursed Secret Service expenses without having to count such payments toward the spending ceiling. Because such payments would otherwise deplete the public fund, and because such payments might otherwise cause a campaign to exceed the spending limit, legal compliance funds may be used. This approach addresses concerns expressed by one commenter who opposed treating the unreimbursed costs incurred by the campaign as subject to the spending limits. The new wording does not affect the amount that the Secret Service and national security staff pay for such transportation and services, since that is established by other federal agencies.

The second change in § 9004.6 pertains to the method for calculating each media representative's *pro rata* share of the actual cost of the transportation and services made available. Language is being added in paragraph (b) to explain that the total number of individuals to whom such transportation or services were made available includes committee staff, media personnel, Secret Service, national security staff and any other individuals traveling with the candidate.

Section 9004.6(b) permits campaign committees to bill the media 110 percent of the actual *pro rata* cost of providing transportation and services to media personnel. These provisions recognize the difficulties of administering a major transportation program in the midst of a campaign. However, under paragraph (d), committees may not deduct from the overall expenditure limitation amounts received that exceed the actual costs of providing transportation and services to the media plus an additional 3 percent for administrative costs. Paragraph (d) is now being revised to clarify that the amount deducted for the actual costs of providing the transportation and services may not exceed the amount the committee actually expended for such costs.

Another area in which questions have arisen concerns reimbursements from the media exceeding the committee's actual costs plus 3 percent for administrative costs. As noted above, the current rules permit billing the media for up to 110 percent of the actual *pro rata* cost, while allowing a deduction from the expenditure limit of no more than 103 percent of the actual cost. Previously, paragraph (d)(1) indicated that general election campaign committees were required to repay to the United States Treasury all amounts over 103 percent. This provision is now being revised to indicate that the amount to be repaid to the Treasury is the amount between 103 percent and 110 percent. Amounts received that exceed 110 percent will have to be returned to the media, since those amounts exceed the total that can permissibly be billed.

Section 9004.9 Net Outstanding Qualified Campaign Expenses

This section generally follows previous § 9004.9.

Section 9004.10 Sale of Assets Acquired for Fundraising Purposes

This section generally follows previous section 9004.10.

Part 9005—Certification by Commission

There are no changes in section 9005.1.

Section 9005.2 Payments to Eligible Candidates From the Fund

In paragraph (c), the previous references to accounts insured by the Federal Savings and Loan Insurance Corporation have been deleted because these accounts are now insured by the Federal Deposit Insurance Corporation.

Part 9006—Reports and Recordkeeping

There are no changes to § 9006.1 or § 9006.2.

Part 9007—Examination and Audits; Repayments

There are no changes in §§ 9007.3 through 9007.6.

Section 9007.1 Audits

During the course of the audits of certain 1988 campaign committees, the Commission issued subpoenas, and also sought information informally from committees and third parties. Accordingly, new language is now being added to 11 CFR 9007.1(b)(1)(v) to inform candidates that the investigative procedures set forth at 11 CFR 111.11 through 111.15, including the issuance of subpoenas, may be invoked in appropriate cases. Please note that the final rules have been modified to refer to the Commission's general authority to issue subpoenas and orders under 2 U.S.C. 437d(a)(1) and (3).

Section 9007.2 Repayments

The Commission's rules at 11 CFR 9007.2(a)(2) indicate that candidates will be notified of repayment determinations as soon as possible, but not later than three years after the end of the expenditure report period. New language is now included in the final rules to explain that the Commission considers the issuance of its interim audit report to constitute notification for purposes of the three year period.

Paragraph (b)(2)(iii) has been revised to clarify the amount representing total deposits under this section which is used to determine the repayment specified in 11 CFR 9007.2(b)(2). A similar clarification is included in 11 CFR 9038.2.

Part 9012—Unauthorized Expenditures and Contributions

There are no changes in part 9012.

Part 9031—Scope

Section 9031.1 Scope

The references to the title 2 rules have been revised to reflect the addition of new 11 CFR part 116.

Part 9032—Definitions

There are no changes in part 9032.

Part 9033—Eligibility for Payments

There are no changes in §§ 9033.2 through 9033.4, §§ 9033.6 through 9033.9 and § 9033.12.

Section 9033.1 Candidate and Committee Agreements

Presidential candidates seeking federal funds for their primary election campaigns must agree to comply with all of the conditions set forth in paragraph (b) of this section to be eligible to receive these funds. The Commission is now revising these conditions in several respects. First, the candidate agreement provisions are being revised to conform to the new magnetic media rules regarding the production of computerized information on magnetic diskettes or magnetic tapes in accordance with the new technical standards. See 11 CFR 9033.12, 55 FR 26392 (June 27, 1990).

The Commission also sought comments on requiring presidential candidates and their authorized committees to obtain and provide upon the Commission's request records regarding funds received and disbursements made on the candidate's behalf by other committees and organizations associated with the candidate. One commenter believed this requirement was unnecessary because the Commission already has authority to request and, if necessary, subpoena these records. Nevertheless, the Commission has concluded that inclusion of this requirement in the candidate agreements will ensure a more timely production of pertinent records that the Commission needs to audit the candidate's Presidential campaign committee or to make repayment determinations.

The Commission's proposed rules had included a requirement that candidates agree to file alphabetized schedules if their reports are generated from computerized files. One comment objected to the placement of such a requirement in the candidate agreements. The Commission has now decided not to require the filing of alphabetized schedules. Similarly, the Commission considered and rejected a proposal to add new language to the candidate agreement provisions to require committees to verify that they are not spending possibly illegal contributions while they are making inquiries as to the permissibility of these contributions. One commenter indicated that such a requirement would not add anything to existing law.

Section 9033.5 Determination of Ineligibility Date

Under the Matching Payment Account Act, a candidate's continued eligibility to receive matching funds is based upon receipt of at least 10 percent of the popular vote cast in the party's primary elections if the candidate has permitted or authorized his or her name to appear on the ballot, unless the candidate certifies to the Commission that he or she will not be an active candidate in a particular primary. 26 U.S.C. 9033(c). During the 1988 primary election cycle, a question arose regarding the effect of a candidate's certification that he or she will not be an active candidate in a primary if the candidate subsequently receives 10 percent or more of the popular votes cast in that primary. Consequently, the Commission is now revising 11 CFR 9033.5(b) to clarify that if a candidate certifies his or her nonparticipation in a particular election, that election will not be counted in determining the candidate's date of ineligibility regardless of whether he or she receives more or less than 10 percent of the popular vote. Thus the election will not be used to disqualify such candidates receiving less than 10 percent, and it will not count to the advantage of candidates exceeding the 10 percent cutoff.

Section 9033.10 Procedures for Initial and Final Determinations

This section generally follows previous § 9033.10.

Section 9033.11 Documentation of Disbursements

Section 9033.11(b)(1)(iv) is being revised to indicate that collateral evidence documenting qualified campaign expenses may include evidence that the disbursement is covered by a preestablished written campaign committee policy, such as a daily travel expense policy. The previous rules had indicated that collateral evidence of a per diem policy would be acceptable. The new, more specific wording is intended to resolve two difficulties. First, a canceled check in combination with a broad per diem policy does not always provide adequate evidence that the expenses claimed are qualified campaign expenses. In addition, a per diem policy does not always provide sufficient information to ascertain whether the committee allocated the expenses correctly for purposes of the state spending limits. By specifying a "daily travel expense policy," the new rules distinguish travel expenses from other campaign costs paid for by individuals that are allocable to a particular state. The second concern should no longer be problematic because the changes to § 106.2 no longer require state allocation of travel costs. The final wording of § 9033.11(b)(1)(iv) represents an improvement over the proposed rules in the NPRM which would simply have required committees to submit collateral evidence showing that "the expenditure is part of an identifiable program or project which is otherwise sufficiently documented to permit (state) allocation." One commenter expressed the concern that this proposal did not specify what types of documentation would be acceptable. The Commission is also making corresponding revisions to the documentation requirements for general election committees at 11 CFR 9003.5(b)(1)(iv).

Part 9034—Entitlements

Section 9034.1 Candidate Entitlements

The Commission has previously notified both the President and Congress of a projected shortage in the Presidential Election Campaign Fund for the 1992 presidential election cycle. The priorities established by the public financing statutes indicate that a shortfall would affect the availability of matching funds for primary candidates before it would affect general election or convention financing. See 26 U.S.C. 9006(c), 9008(a) and 9037. Accordingly, the Commission is adding to § 9034.1(a) of its regulations a cross-reference to 26 U.S.C. 9037 and 11 CFR part 9037 to alert candidates that their receipt of matching funds could be affected by the amount of funds available in the matching payment account. In addition, the Commission has been working with the Treasury Department on implementing the Secretary of the Treasury's statutory obligation to achieve an equitable distribution of the funds available. Now that the Treasury Department has promulgated final rules in this area, the Commission has initiated another rulemaking to make necessary conforming changes to its existing procedures. See Notice of Proposed Rulemaking, 56 FR 29372 (June 26, 1991).

Section 9034.2 Matchable Contributions

New paragraph (c)(1)(iii) has been added to clarify that contributions reattributed to a joint contributor must meet the reattribution requirements of 11 CFR 110.1(k), and must be accompanied by the documentation described in 11 CFR 110.1(l).

Section 9034.3 Non-Matchable Contributions

New paragraph (k) states that contributions redesignated for a different election or redesignated for a legal and accounting compliance fund are not matchable. See 11 CFR 9003.3(a).

Section 9034.4 Use of Contributions and Matching Payments

A candidate's eligibility to receive federal matching funds is predicated upon his or her ability to receive at least 10 percent of the vote in each primary election. The Presidential Primary Matching Payment Account Act specifically recognizes that a candidate who has fallen below this level of support may reestablish eligibility by obtaining at least 20 percent of the votes cast in a subsequent primary. 26 U.S.C. 9033(c)(4)(B). However, the previous regulations did not provide a method for a candidate to use private funds to continue to campaign beyond the date of ineligibility without this affecting the candidate's entitlement to matching funds, since all funds in a publicly funded committee's accounts are considered to be commingled. See, *Kennedy for President Committee* v. *FEC*, 734 F.2d 1558, 1565 at n.11 (D.C. Cir. 1984); *See, also Reagan for President Committee* v. *FEC*, 734 F.2d 1569 (D.C. Cir. 1984). Moreover, under the previous rules, in calculating a candidate's statement of net outstanding campaign obligations ("NOCO"), a candidate's private contributions were applied to eliminate the pre-date of ineligibility debt before they were used to pay debts incurred in continuing to campaign. Thus, a candidate could not separate out private funds to be used to continue to campaign. As a result, a candidate who continued to raise private funds after the date of ineligibility may have been required to make a repayment based on matching funds received in excess of his or her entitlement or based on nonqualified campaign expenses associated with continuing to campaign.

The Commission has now revised § 9034.4(a)(3)(ii) to allow a candidate to use post-ineligibility contributions to continue campaigning after the date of ineligibility without such activity resulting in a repayment of funds in excess of entitlement or a repayment of funds used for nonqualified campaign expenses. Compare new 11 CFR 9038.2(b)(2)(ii)(D). Under the new approach, the candidate's NOCO is "frozen" as of the candidate's date of ineligibility. Contributions received after the date of ineligibility that are used to continue to campaign may be submitted for matching. The candidate may continue to receive the same proportion of matching funds to defray NOCO as the candidate received before the date of ineligibility. The amount of matching funds received will be added to the post-ineligibility contributions to determine the amount of the candidate's remaining entitlement. Post-ineligibility matching fund payments may be used to defray the candidate's NOCO, but may not be used to defray the costs of continuing to campaign unless the candidate is able to reestablish eligibility under 11 CFR 9033.8. Post-ineligibility contributions are subject to the limitations, prohibitions, recordkeeping and reporting requirements. As under the previous rules, the candidate is not eligible to receive matching funds for winding down costs until the candidate is no longer continuing to campaign. Expenditures made for purposes of continuing to campaign are still counted against the spending limits, since the candidate's previous acceptance of matching funds was based on his or her agreement to comply with the spending limits. One comment supported efforts to allow for the raising and spending of private funds to continue to campaign following a determination of ineligibility. The new provisions reflect the Commission's intention to treat candidates who continue to campaign as fairly as those who withdraw as of the date of ineligibility.

In AO 1988–5 questions were raised as to whether a current publicly-funded presidential campaign committee may contribute or loan or transfer funds to another federally funded committee of the same candidate for a previous election cycle for the purpose of paying debts from the earlier campaign. The opinion concluded that such payments are not qualified campaign expenses under 11 CFR 9034.4 and are not includable in the candidate's NOCO statement under 11 CFR 9034.5. However, such payments could be made from excess campaign funds once the audit process is concluded and any repayment or possible penalty obligations have been satisfied. The attached final rules include new language in section 9034.4(b)(6) reaffirming the conclusion reached in AO 1988–5 that these payments are not qualified campaign expenses. Accordingly, they could serve as a basis for a repayment determination under 11 CFR 9038.2. Please note that even though the question presented in AO 1988–5 was framed in terms of treating such payments as contributions, the Commission would regard such a flow of funds as a transfer, not a contribution. See H. Rept. No. 96–422, 96th Cong., 1st Sess. 7 (1979).

New paragraph (b)(7) indicates that payments for expenses subject to the state spending limits will not be treated as qualified campaign expenses if the committee's records do not provide sufficient information to accurately allocate the expenses to particular states. This new provision may apply, for example, if the records do not show when an allocable expense was incurred.

Finally, paragraph (d) of this section has been reorganized and a new sentence has been added to assist the reader in locating the provisions regarding transfers to a legal and accounting compliance fund. 11 CFR 9003.3(a)(1).

Section 9034.5 Net Outstanding Campaign Obligations

This section generally follows previous § 9034.5.

Section 9034.6 Reimbursements for Transportation and Services Made Available to Media Personnel

Under this section, candidates may seek reimbursement from media personnel for the costs of providing transportation and services to media representatives accompanying the candidate on campaign trips. These provisions also establish the method to be used in determining how much committees may receive from media personnel for such costs. The Commission is now making several changes to these rules. First, paragraph (a) is being revised to clarify that expenditures incurred for transportation or services made available to Secret Service and national security staff, less any reimbursements received, are qualified campaign expenses but not subject to the overall spending limits. This language allows the campaign to pay unreimbursed Secret Service expenses without having to count such payments toward the spending ceiling. This approach addresses concerns expressed by one commenter who opposed treating the unreimbursed costs incurred by the campaign as subject to the spending limits. The new wording does not affect the amount that the Secret Service and national security staff pay for such transportation and services, since that is established by other federal agencies.

The second change in § 9034.6 pertains to the method for calculating each media representative's *pro rata* share of the actual cost of the transportation and services made available. Language is being added in paragraph (b) to explain that the total number of individuals to whom such transportation or services were made available includes committee staff, media personnel, Secret Service, national security staff and any other individuals traveling with the candidate.

Section 9034.6(b) permits campaign committees to bill the media 110 percent of the actual *pro rata* cost of providing transportation and services to media personnel. These provisions recognize the difficulties of administering a major transportation program in the midst of a campaign. However, under paragraph (d), committees may not deduct from the overall expenditure limitation amounts received that exceed the actual costs of providing transportation and services to the media plus an additional 3 percent for administrative costs. Paragraph (d) is now being revised to clarify that the amount deducted for the actual costs of providing the transportation and services may not exceed the amount the committee actually expended for such costs.

Another area in which questions have arisen concerns reimbursements from the media exceeding the committee's actual costs plus 3 percent for administrative costs. As noted above, the current rules permit billing the media for up to 110 percent of the actual *pro rata* cost, while allowing a deduction from the expenditure limit of no more than 103 percent of the actual cost. New language is now being added to paragraph (d) to indicate that the amount between 103 percent and 110 percent of the actual cost must be repaid to the Treasury, and that amounts received that exceed 110 percent will have to be returned to the media on a *pro rata* basis. This approach is consistent with the media reimbursement rules for general election candidates, as set out at 11 CFR 9004.6(d). It recognizes that reimbursements from the media may cover actual transportation costs and the costs of administering the program, but should not result in a primary candidate's committee making a profit.

Section 9034.7 Allocation of Travel Expenditures

There are no changes in this section.

Section 9034.8 Joint Fundraising

The Commission is revising the joint fundraising rules set out at 11 CFR 9034.8 in several respects. First, paragraph (b)(1) now specifies that if committees participating in a joint fundraiser elect to form a separate committee to serve as the fundraising representative, the separate committee cannot be a participant in any other joint fundraising efforts but may conduct more than one joint fundraising effort for the participating committees. This change corrects two problems. First, in cases where this has occurred, there was no explicit allocation formula for determining the amounts to be distributed to each of the original participating committees. Secondly, there has been confusion as to the amount that may be contributed to the fundraising representative for distribution among the participating committees. If a series of fundraising events or activities is held, the expenses must be allocated on a per event basis under paragraph (c)(8)(i)(C) of this section.

New language is also being added to paragraph (c)(1) to require the allocation formula to indicate the amount or percentage of each contribution that will be allocated to each participant. Thus, the formula may not state that a fixed amount of the proceeds will be allocated to a specific participant, or that contributions will be allocated to one participant because the contributions are matchable. Section 9034.8(c)(7)(i) does not permit the committee to use a joint fundraiser to maximize the matchability of contributions. However, the formula may state, for example, that the first $250 of each contribution will be allocated to a particular candidate. The new rules also delete the previous language in paragraph (c)(1) indicating that the joint fundraising participants must use the formula to allocate fundraising expenses. This change was necessary because paragraph (c)(8) indicates that the joint fundraising representative allocates expenses based on the percentage of total receipts allocated to each participant. Similarly, paragraph (c)(7)(ii) is being amended to indicate that reallocation of contributions is the responsibility of the joint fundraising representative, not the participating candidates. Please note that corresponding changes are included in the joint fundraising rules applicable to nonpresidential candidates. See 11 CFR 102.17.

Part 9035—Expenditure Limitations

Section 9035.1 Campaign Expenditure Limitation

The compliance and fundraising exemptions set out in § 9035.1(c) are being revised to reflect the changes in §§ 100.8(b)(21) and 110.8(c)(2) in determining the amount excluded from the overall spending limit for exempt fundraising activity.

Section 9035.2 Limitation on Expenditures From Personal or Family Funds

There are no changes in § 9035.2.

Part 9036—Review of Submission and Certification of Payments by Commission

There are no changes in §§ 9036.3 through 9036.6.

Section 9036.1 Threshold Submission

New paragraph (b)(2) has been added to this provision to require all committees that have computerized their contributor lists to submit computerized magnetic media at the time they make their threshold submission for matching fund payments. See the Commission's Computerized Magnetic Media Requirements for Title 26 Candidates/Committees Receiving Federal Funding. Please note that these requirements also apply to additional submissions governed by § 9036.2. Previously, the submission of computerized information at the matching fund stage was optional. Now that the Commission has prepared new technical standards for the submission of computer tapes and diskettes, the Commission may be able to process all matching fund submissions more efficiently. See 11 CFR 9033.12. Please note that this change does not require presidential campaign committees to computerize part or all of their financial records if they do not wish to do so.

New paragraph (b)(6) requires all threshold submissions to include a list of refunded contributions, regardless of whether they were submitted for matching. One commenter expressed concerns regarding the burdensomeness of such a rule. This requirement is included in the final rules because the relevant information is needed to ensure that refunded contributions are not submitted for matching, and are properly reported.

Section 9036.2 Additional Submissions for Matching Fund Payments

New paragraph (b)(1)(iv) has been added to require nonthreshold submissions to include a list of refunded contributions, regardless of whether they were submitted for matching. Although one commenter expressed concerns regarding the burdensomeness of such a rule, the requirement is included in the final rules to ensure that refunded contributions are not submitted for matching, and are properly reported.

The Commission has also decided that during limited periods of time, it will use a new procedure of rejecting matching fund submissions from review in cases where the projected dollar value of the nonmatchable contributions exceeded 15 percent of the amount required. Please note that the new rejection policy does not apply to submissions made on the last submission date in the year preceding the Presidential election year, or to submissions made during the Presidential election year before the candidate's date of ineligibility. At other times when the new policy is in operation, the entire submission will be returned to the committee for corrective action before any amount is certified for payment. If the committee is able to correct the submission and resubmit it within five business days, it will be reviewed before the next regularly scheduled submission date and an amount will be certified on the certification date for the original submission. However, if the resubmission is made after the five day period, it will be reviewed after the next regularly scheduled submission date, and an amount will be certified on the next regularly scheduled certification date. Corrected submissions may not contain new or additional contributions that were not previously submitted for matching. Similarly, under 11 CFR 9036.5(c)(5), resubmissions may not contain new or additional contributions that were not previously submitted. Submissions would not be considered to be corrected until the projected dollar value of nonmatchable contributions has been reduced to 15 percent or less of the amount requested. The new policy is not reflected in the final version of 11 CFR 9036.2 (c) and (d), and 9038.4(a), which follows, but is included in a separate draft of those sections found in the Commission's Notice of Proposed Rulemaking, which proposes broader changes to the Commission's matching fund submission and certification procedures. See 56 FR 29372 (June 26, 1991).

Part 9037—Payments

There are no changes in §§ 9037.1 and 9037.2.

Section 9037.3 Deposits of Presidential Primary Matching Funds

This section has been slightly modified to update the language regarding campaign depositories. It now parallels the revised general election provisions at 11 CFR 9005.2(c).

Part 9038—Examination and Audits

There are no changes in §§ 9038.4 through 9038.6.

Section 9038.1 Audit

During the course of the audits of certain 1988 campaign committees, the Commission issued subpoenas, and also sought information informally from committees and third parties. Accordingly, new language is now being added to 11 CFR 9038.1(b)(1)(v) to inform candidates that the investigative procedures set forth at 11 CFR 111.11 through 111.15, including the issuance of subpoenas, may be invoked in appropriate cases. Please note that the final rules have been modified to refer to the Commission's general authority to issue subpoenas and orders under 2 U.S.C. 437d(a) (1) and (3).

Section 9038.2 Repayments

The Commission has decided to revise several aspects of the repayment process for presidential primary candidates set forth at 11 CFR 9038.2. First, the Commission's rules at 11 CFR 9038.2(a)(2) indicate that candidates will be notified of repayment determinations as soon as possible, but not later than three years after the end of the matching payment period. New language is now included in the final rules to explain that the Commission considers the issuance of its interim audit report to constitute notification for purposes of the three year period.

The Commission's regulations at 11 CFR 9038.2(b)(1) require primary candidates to repay matching funds received which are in excess of the amount to which the candidates are entitled. A candidate's committee may receive matching funds in excess of the amount to which it is entitled if, for example, it receives matching funds after the candidate's date of ineligibility and the candidate had no net outstanding campaign obligations to justify the amount of a post-ineligibility payment. This can occur if the candidate includes on his or her NOCO statement accounts payable for nonqualified campaign expenses. In such a situation, the Commission's audit may result in the correction of the NOCO statement and a dollar for dollar repayment of the amount determined to exceed the candidate's entitlement.

In addition to the (b)(1) repayment, paragraph (b)(2) of § 9038.2 requires repayment of a portion of all nonqualified campaign expenses incurred and paid between the campaign's date of inception and the date on which the committee's accounts no longer contain any matching funds. Thus, concerns have been raised that if a candidate's entitlement was artificially increased as a result of nonqualified campaign expenses, and a 100 percent repayment is sought under (b)(1), these nonqualified campaign expenses should be excluded when calculating the amount repayable under (b)(2), to avoid seeking repayment twice for the same funds, or "double counting" them.

The Commission has now concluded that the public funding statutes establish separate bases for seeking repayments of payments in excess of a candidate's entitlement and repayments of amounts spent for nonqualified campaign expenses. Accordingly, new language has been added to the final rules to indicate that repayment determinations will be sought under § 9038.2(b)(2) for nonqualified campaign expenses paid before the point when the committee's accounts no longer contain matching funds, regardless of whether a separate repayment determination is sought under § 9038.2(b)(1).

The final rules also address situations in which primary candidates have exceeded both the spending limits for a particular state and the overall spending limit. 11 CFR 9038.2(b)(2)(v). Disbursements in excess of these spending limits are considered nonqualified campaign expenses. The Commission sought comments on two possible methods for calculating the candidate's repayment obligations under 11 CFR 9038.2(b)(2) in this situation. The first approach treats the state expenditure limitations and the overall expenditure limitation as separate for repayment purposes, but avoids dual repayment for disbursements that exceed both limits. Thus, this method operates by assuming that expenditures should count against the spending limits in the order in which they are paid. This permits identification of those particular expenditures that exceed both limits. To avoid double counting, the total amount of disbursements exceeding both limits are then subtracted from the excessive amount repayable under one limit or the other. Although these disbursements are considered nonqualified campaign expenses for two reasons, they are subject to repayment only once.

In contrast, the second approach considered by the Commission simply calculates the repayment using only the larger of the two excessive amounts. The Commission has used the second method in an audit from the 1984 Presidential election cycle. This method assumes that the same disbursements cause both overages, since few, if any, committees that exceed the overall spending limit are able to stay within the state-by-state spending limits. For example, where the amount in excess of the overall limit is larger than the amount in excess of the state limits, the second approach operates by denoting the amount in excess of the state-by-state limitations as a subset of the overall expenditure limitation, regardless of when the expenditures were paid by the committee. To avoid the possibility of double counting, the expenditures that exceed the state-by-state limits are subsumed into the expenditures that exceed the overall limit. Conversely, if the amount of expenditures exceeding the overall limits is the lesser amount, it would be subsumed into the amount of expenditures exceeding the state limits.

The Commission has now concluded that the second method is the better approach. Accordingly, new § 9038.2(b)(2)(v) incorporates this method.

New paragraph (b)(2)(ii)(D) has also been added to indicate that the use of federal funds for continuing to campaign after a candidate's date of ineligibility will be considered nonqualified campaign expenses. See revised 11 CFR 9034.4(a)(3)(ii).

The Commission is now adding language to 11 CFR 9038.2(b)(4) to specifically require the repayment of net income received from the investment of surplus public funds after the candidate's date of ineligibility. The Commission's rules at 11 CFR 9004.5, which pertain to general election candidates, already provide for the repayment of interest and other forms of income derived from the investment of public funds. Please note, however, that the receipt of such investment income before a primary candidate's date of ineligibility simply reduces the candidate's net outstanding campaign obligations and increases the amount of any surplus repayment.

The new rules also clarify that the amount representing total deposits under 11 CFR 9038.3(c)(2) is used to determine the repayment specified in 11 CFR 9038.2(b)(2)(iii). A similar clarification has been included in 11 CFR 9007.2(b)(2)(iii). Finally, § 9038.2(b)(2)(iii) is amended to clarify that the last-in, first-out method of determining when a committee's account no longer contains matching funds only applies to committees that received matching funds after the candidate's date of ineligibility.

Section 9038.3 Liquidation of Obligations; Repayment

This section generally follows previous § 9038.3.

Part 9039—Review and Investigation Authority

There are no changes in this part.

List of Subjects

11 CFR Part 100

Elections, Political committees and parties.

11 CFR Part 102

Campaign funds, Political candidates, Political committees and parties, Reporting requirements.

11 CFR Part 106

Campaign funds, Political candidates, Political committees and parties.

11 CFR Part 110

Campaign funds, Elections, Political candidates, Political committees and parties, Reporting and recordkeeping requirements.

11 CFR Part 116

Administrative practice and procedure, Business and industry, Credit, Elections, Political candidates, Political committees and parties.

11 CFR Parts 9001–9005

Campaign funds, Elections, Political candidates.

11 CFR Part 9006

Campaign funds, Elections, Political candidates, Reporting requirements.

11 CFR Part 9007

Administrative practice and procedure, Campaign funds, Political candidates.

11 CFR Part 9012

Elections, Political candidates, Political committees and parties.

11 CFR Parts 9031–9035

Campaign funds, Elections, Political candidates.

11 CFR Part 9036

Administrative practice and procedure, Campaign funds, Political candidates.

11 CFR Part 9037

Campaign funds, Political candidates.

11 CFR Parts 9038–9039

Administrative practice and procedure, Campaign funds, Political candidates.

Certification of no Effect Pursuant to 5 U.S.C. 605(b) (Regulatory Flexibility Act)

The attached final rules will not, if promulgated, have a significant economic impact on a substantial number of small entities. The basis for this certification is that few, if any, small entities are affected by these rules. Further, any small entities affected are already required to comply with the requirements of the Act in these areas.

For the reasons set out in the preamble, subchapters A, E and F, chapter I of title 11 of the Code of Federal Regulations are amended as follows:

PART 100—SCOPE AND DEFINITIONS (2 U.S.C. 431)

1. The authority citation for part 100 continues to read as follows:

Authority: 2 U.S.C. 431, 438(a)(8).

2. 11 CFR part 100 is amended by revising paragraph (b)(21) of § 100.8 to read as follows:

§ 100.8 Expenditure (2 U.S.C 431(9)).

* * * * *

(b) * * *

(21)(i) Any costs incurred by a candidate or his or her authorized committee(s) in connection with the solicitation of contributions are not expenditures if incurred by a candidate who has been certified to receive Presidential Primary Matching Fund Payments, or by a candidate who has been certified to receive general election public financing under 26 U.S.C. 9004 and who is soliciting contributions in accordance with 26 U.S.C. 9003(b)(2) or 9003(c)(2) to the extent that the aggregate of such costs does not exceed 20 percent of the expenditure limitation applicable to the candidate. These costs shall, however, be reported as disbursements pursuant to 11 CFR part 104.

(ii) For a candidate who has been certified to receive general election public financing under 26 U.S.C. 9004 and who is soliciting contributions in accordance with 26 U.S.C. 9003(b)(2) or 9003(c)(2), "in connection with the solicitation of contributions" means any cost reasonably related to fundraising activity, including the costs of printing and postage, the production of and space or air time for, advertisements used for fundraising, and the costs of meals, beverages, and other costs associated with a fundraising reception or dinner.

(iii) For a candidate who has been certified to receive Presidential Primary Matching Fund Payments, the costs that may be exempted as fundraising expenses under this section shall not exceed 20% of the overall expenditure limitation under 11 CFR 9035.1, and shall equal the total of:

(A) All amounts excluded from the state expenditure limitations for exempt fundraising activities under 11 CFR 110.8(c)(2), plus

(B) An amount of costs that would otherwise be chargeable to the overall expenditure limitation but that are not chargeable to any state expenditure limitation, such as salary and travel expenses. See 11 CFR 106.2.

* * * * *

PART 102—REGISTRATION, ORGANIZATION, AND RECORDKEEPING BY POLITICAL COMMITTEES (2 U.S.C. 433)

3. The authority citation for part 102 continues to read as follows:

Authority: 2 U.S.C. 432, 433, 438(a)(8), 441d.

4. 11 CFR 102.17 is amended by revising paragraphs (a)(1)(i), (c)(1) and (c)(6)(ii) and by adding paragraph (c)(7)(i)(C) to read as follows:

§ 102.17 Joint fundraising by committees other than separate segregated funds.

(a) *General.* (1)(i) Political committees may engage in joint fundraising with other political committees or with unregistered committees or organizations. The participants in a joint fundraising effort under this section shall either establish a separate committee or select a participating committee, to act as fundraising representative for all participants. The fundraising representative shall be a reporting political committee and an authorized committee of each candidate for federal office participating in the joint fundraising activity. If the participants establish a separate committee to act as the fundraising representative, the separate committee shall not be a participant in any other joint fundraising effort, but the separate committee may conduct more than one joint fundraising effort for the participants.

* * * * *

(c) * * *

(1) *Written agreement.* The participants in a joint fundraising activity shall enter into a written agreement, whether or not all participants are political committees under 11 CFR 100.5. The written agreement shall identify the fundraising representative and shall state a formula for the allocation of fundraising proceeds. The formula shall be stated as the amount or percentage of each contribution received to be allocated to each participant. The fundraising representative shall retain the written agreement for a period of three years and shall make it available to the Commission on request.

* * * * *

(6) * * *

(ii) Designated contributions which exceed the contributor's limit to the designated participant under 11 CFR part 110 may not be reallocated by the fundraising representative absent the prior written permission of the contributor.

* * * * *

(7) * * *

(i) * * *

(C) The expenses from a series of fundraising events or activities shall be allocated among the participants on a per-event basis regardless of whether the participants change or remain the same throughout the series.

* * * * *

PART 106—ALLOCATIONS OF CANDIDATE AND COMMITTEE ACTIVITIES

5. The authority citation for part 106 continues to read as follows:

Authority: 2 U.S.C. 438(a)(8), 441a(b), 441a(g).

6. 11 CFR part 106 is amended by revising § 106.2 to read as follows:

§ 106.2 State allocation of expenditures incurred by authorized committees of presidential primary candidates receiving matching funds.

(a) *General*—(1) This section applies to Presidential primary candidates receiving or expecting to receive federal matching funds pursuant to 11 CFR parts 9031 *et seq.* The expenditures described in 11 CFR 106.2(b)(2) shall be allocated to a particular State if incurred by a candidate's authorized committee(s) for the purpose of influencing the nomination of that candidate for the office of President with respect to that State. An expenditure shall not necessarily be allocated to the State in which the expenditure is incurred or paid. In the event that the Commission disputes the candidate's allocation or claim of exemption for a particular expense, the candidate shall demonstrate, with supporting documentation, that his or her proposed method of allocation or claim of exemption was reasonable.

(2) Disbursements made prior to the time an individual becomes a candidate for the purpose of determining whether that individual should become a candidate pursuant to 11 CFR 100.7(b)(1) and 100.8(b)(1), i.e., payments for testing the waters, shall be allocable expenditures under this section if the individual becomes a candidate.

(b) *Method of allocating expenditures among States*—(1) *General allocation method.* Unless otherwise specified under 11 CFR 106.2(b)(2), an expenditure described in 11 CFR 106.2(b)(2) and incurred by a candidate's authorized committee(s) for the purpose of influencing the nomination of that candidate in more than one State shall be allocated to each State on a reasonable and uniformly applied basis. The total amount allocated to a particular State may be reduced by the amount of exempt fundraising expenses for that State, as specified in 11 CFR 110.8(c)(2).

(2) *Specific allocation methods.* Expenditures that fall within the categories listed below shall be allocated based on the following methods. The method used to allocate a category of expenditures shall be based on consistent data for each State to which an allocation is made.

(i) *Media expenditures*—(A) *Print media.* Except for expenditures exempted under 11 CFR 106.2(b)(2)(i) (E) and (F), allocation of expenditures for the publication and distribution of newspaper, magazine and other types of printed advertisements distributed in more than one State shall be made using relative circulation percentages in each State or an estimate thereof. For purposes of this section, allocation to a particular State will not be required if less than 3% of the total estimated readership of the publication is in that State.

(B) *Broadcast media.* Except for expenditures exempted under 11 CFR 106.2(b)(2)(i) (E) and (F), expenditures for radio, television and similar types of advertisements purchased in a particular media market that covers more than one State shall be allocated to each State in proportion to the estimated audience. This allocation of expenditures, shall be made using industry market data. If industry market data is not available, the committee shall obtain market data from the media carrier transmitting the advertisement(s).

(C) *Refunds for media expenditures.* Refunds for broadcast time or advertisement space, purchased but not used, shall be credited to the States on the same basis as the original allocation.

(D) *Limits on allocation of media expenditures.* No allocation of media expenditures shall be made to any State in which the primary election has already been held.

(E) *National advertising.* Expenditures incurred for advertisements on national networks, national cable or in publications distributed nationwide need not be allocated to any State.

(F) *Media production costs.* Expenditures incurred for production of media advertising, whether or not that advertising is used in more than one State, need not be allocated to any State.

(G) *Commissions.* Expenditures for commissions, fees and other compensation for the purchase of broadcast or print media need not be allocated to any State.

(ii) *Expenditures for mass mailings and other campaign materials.* Expenditures for mass mailings of more than 500 pieces to addresses in the same State, and expenditures for shipping campaign materials to a State, including pins, bumperstickers, handbills, brochures, posters and yardsigns, shall be allocated to that State. For purposes of this section, "mass mailing" includes newsletters and other materials in which the content of the materials is substantially identical. Records supporting the committee's allocations under this section shall include: For each mass mailing, documentation showing the total number of pieces mailed and the number mailed to each state or zip code; and, for other campaign materials acquired for use outside the State of purchase, records relating to any shipping costs incurred for transporting these items to each State.

(iii) *Overhead expenditures*—(A) *Overhead expenditures of State offices and other facilities.* Except for expenditures exempted under 11 CFR 106.2(b)(2)(iii)(C), overhead expenditures of committee offices whose activities are directed at a particular State, and the costs of other facilities used for office functions and campaign events, shall be allocated to that State. An amount that does not exceed 10% of office overhead expenditures for a particular State may be treated as exempt compliance expenses, and may be excluded from allocation to that State.

(B) *Overhead expenditures of regional offices.* Except for expenditures exempted under 11 CFR 106.2(b)(2)(iii)(C), overhead expenditures of a committee regional office or any committee office with responsibilities in two or more States shall be allocated to the State holding the next primary election, caucus or convention in the region. The committee shall maintain records to demonstrate that an office operated on a regional basis. These records should show, for example, the kinds of programs conducted from the office, the number and nature of contacts with other States in the region, and the amount of time devoted to regional programs by staff working in the regional office.

(C) *Overhead expenditures of national campaign headquarters.* Expenditures incurred for administrative, staff, and overhead expenditures of the national campaign headquarters need not be allocated to any State, except as provided in paragraph (b)(2)(iv) of this section.

(D) *Definition of overhead expenditures.* For purposes of 11 CFR 106.2(b)(2)(iii), overhead expenditures include, but are not limited to, rent, utilities, equipment, furniture, supplies, and telephone service base charges. "Telephone service base charges" include any regular monthly charges for committee phone service, and charges for phone installation and intrastate phone calls other than charges related to a special program under 11 CFR 106.2(b)(2)(iv). Inter-state calls are not included in "telephone service base charges." Overhead expenditures also include the costs of temporary offices established while the candidate is traveling in the State or in the final weeks before the primary election, as well as expenses paid by campaign staff and subsequently reimbursed by the committee, such as miscellaneous supplies, copying, printing and telephone expenses. See 11 CFR 116.5.

(iv) *Expenditures for special telephone programs.* Expenditures for special telephone programs targeted at a particular State, including the costs of designing and operating the program, the costs of installing or renting telephone lines and equipment, toll charges, personnel costs, consultants' fees, related travel costs, and rental of office space, including a *pro rata* portion of national, regional or State office space used for such purposes, shall be allocated to that State based on the percentage of telephone calls made to that State. Special telephone programs include voter registration, get out the vote efforts, fundraising, and telemarketing efforts conducted on behalf of the candidate. A special telephone program is targeted at a particular State if 10% or more of the total telephone calls made each month are made to that State. Records supporting the committee's allocation of each special telephone program under this section shall include either the telephone bills showing the total number of calls made in that program and the number made to each State; or, a copy of the list used to make the calls, from which these numbers can be determined.

(v) *Public opinion poll expenditures.* Expenditures incurred for the taking of a public opinion poll covering only one State shall be allocated to that State. Except for expenditures incurred in conducting a public opinion poll on a nationwide basis, expenditures incurred for the taking of a public opinion poll covering two or more States shall be allocated to those States based on the number of people interviewed in each State. Expenditures incurred for the taking of a public opinion poll include consultant's fees, travel costs and other expenses associated with designing and conducting the poll. Records supporting the committee's allocation under this section shall include documentation showing the total number of people contacted for each poll and the number contacted in each State.

(3) *National consulting fees.* Expenditures for consultants' fees need not be allocated to any State if the fees are charged for consulting on national campaign strategy. Expenditures for consultants' fees charged for conducting special telephone programs and public opinion polls shall be allocated in accordance with paragraphs (b)(2) (iv) and (v) of this section.

(c) *Reporting.* All expenditures allocated under this section shall be reported on FEC Form 3P, page 3.

(d) *Recordkeeping.* All assumptions and supporting calculations for allocations made under this section shall be documented and retained for Commission inspection. In addition to the records specified in paragraph (b) of this section, the treasurer shall retain records supporting the committee's allocations of expenditures to particular States and claims of exemption from allocation under this section. If the records supporting the allocation or claim of exemption are not retained, the expenditure shall be considered allocable and shall be allocated to the State holding the next primary election, caucus or convention after the expenditure is incurred.

PART 110—CONTRIBUTION AND EXPENDITURE LIMITATIONS AND PROHIBITIONS

7. The authority citation for part 110 continues to read as follows:

Authority: 2 U.S.C. 431(8), 431(9), 432(c)(2), 437d(a)(8), 438(a)(8), 441a, 441b, 441d, 441e, 441f, 441g, 441h and 441i.

8. 11 CFR part 110 is amended by revising paragraph (l) of § 110.1 to read as follows:

§ 110.1 Contributions by persons other than multicandidate political committees (2 U.S.C. 441a(a)(1)).

* * * * *

(l) *Supporting evidence.* (1) If a political committee receives a contribution designated in writing for a particular election, the treasurer shall retain a copy of the written designation, as required by 11 CFR 110.1(b)(4) or 110.2(b)(4), as appropriate. If the written designation is made on a check or other written instrument, the treasurer shall retain a full-size photocopy of the check or written instrument.

(2) If a political committee receives a written redesignation of a contribution for a different election, the treasurer shall retain the written redesignation provided by the contributor, as required by 11 CFR 110.1(b)(5) or 110.2(b)(5), as appropriate.

(3) If a political committee receives a written reattribution of a contribution to a different contributor, the treasurer shall retain the written reattribution signed by each contributor, as required by 11 CFR 110.1(k).

(4) If a political committee chooses to rely on a postmark as evidence of the date on which a contribution was made, the treasurer shall retain the envelope or a copy of the envelope containing the postmark and other identifying information.

(5) If a political committee does not retain the written records concerning designation required under 11 CFR 110.1(l)(2), the contribution shall not be considered to be designated in writing for a particular election, and the provisions of 11 CFR 110.1(b)(2)(ii) or 110.2(b)(2)(ii) shall apply. If a political committee does not retain the written records concerning redesignation or reattribution required under 11 CFR 110.1(l) (2), (3) or (6), the redesignation or reattribution shall not be effective, and the original designation or attribution shall control.

(6) For each written redesignation or written reattribution of a contribution described in paragraph (b)(5) or paragraph (k)(3) of this section, the political committee shall retain documentation demonstrating when the written redesignation or written reattribution was received. Such documentation shall consist of:

(i) A copy of the envelope bearing the postmark and the contributor's name, or return address or other identifying code; or

(ii) A copy of the written redesignation or written reattribution with a date stamp indicating the date of the committee's receipt; or

(iii) A copy of the written redesignation or written reattribution dated by the contributor.

* * * * *

9. 11 CFR part 110 is amended by revising paragraph (c)(2) of § 110.8 to read as follows:

§ 110.8 Presidential candidate expenditure limitations.

* * * * *

(c) * * *

(2) The candidate may treat an amount that does not exceed 50% of the candidate's total expenditures allocable to a particular State under 11 CFR 106.2 as exempt fundraising expenses, and may exclude this amount from the candidate's total expenditures attributable to the expenditure limitations for that State. The candidate may treat 100% of the cost of mass mailings as exempt fundraising expenses, unless the mass mailings were mailed within 28 days before the state's primary election, convention or caucus. The total of all amounts excluded for exempt fundraising expenses shall not exceed 20% of the overall expenditure limitation under 11 CFR 9035.1.

* * * * *

10. 11 CFR 110.8(f)(2) is amended by removing the citation to "§ 141.2(c)" and adding, in its place, a citation to "11 CFR 9003.2(c)."

PART 116—DEBTS OWED BY CANDIDATES AND POLITICAL COMMITTEES

11. The authority citation for part 116 continues to read as follows:

Authority: 2 U.S.C. 433(d), 434(b)(8), 438(a)(8), 441a, 441b and 451.

12. 11 CFR part 116 is amended by revising paragraph (b)(2) of § 116.5 to read as follows:

§ 116.5 Advances by committee staff and other individuals.

* * * * *

(b) * * *

(2) The individual is reimbursed within sixty days after the closing date of the billing statement on which the charges first appear if the payment was made using a personal credit card, or within thirty days after the date on which the expenses were incurred if a personal credit card was not used. For purposes of this section, the closing date shall be the date indicated on the billing statement which serves as the cutoff date for determining which charges are included on that billing statement. In addition, "subsistence expenses" include only expenditures for personal living expenses related to a particular individual traveling on committee business, such as food or lodging.

* * * * *

13. 11 CFR parts 9001 through 9007 is revised to read as follows:

PART 9001—SCOPE

Authority: 26 U.S.C. 9009(b).

§ 9001.1 Scope.

This subchapter governs entitlement to and use of funds certified from the Presidential Election Campaign Fund under 26 U.S.C. 9001 *et seq.* The definitions, restrictions, liabilities and obligations imposed by this subchapter are in addition to those imposed by sections 431–455 of title 2, United States Code, and regulations prescribed thereunder (11 CFR parts 100 through 116). Unless expressly stated to the contrary, this subchapter does not alter the effect of any definitions, restrictions, obligations and liabilities imposed by sections 431–455 of title 2, United States Code, or regulations prescribed thereunder (11 CFR parts 100 through 116).

PART 9002—DEFINITIONS

Authority: 26 U.S.C. 9002 and 9009(b).

§ 9002.1 Authorized committee.

(a) Notwithstanding the definition at 11 CFR 100.5, "authorized committee" means with respect to a candidate (as defined at 11 CFR 9002.2) of a political party for President and Vice President, any political committee that is authorized by a candidate to incur expenses on behalf of such candidate. The term "authorized committee" includes the candidate's principal campaign committee designated in accordance with 11 CFR 102.12, any political committee authorized in writing by the candidate in accordance with 11 CFR 102.13, and any political committee not disavowed by the candidate pursuant to 11 CFR 100.3(a)(3). If a party has nominated a Presidential and a Vice Presidential candidate, all political committees authorized by that party's Presidential candidate shall also be authorized committees of the Vice Presidential candidate and all political committees authorized by the Vice Presidential candidate shall also be authorized committees of the Presidential candidate.

(b) Any withdrawal of an authorization shall be in writing and shall be addressed and filed in the same manner provided for at 11 CFR 102.12 or 102.13.

(c) Any candidate nominated by a political party may designate the national committee of that political party as that candidate's authorized committee in accordance with 11 CFR 102.12(c).

(d) For purposes of this subchapter, references to the "candidate" and his or her responsibilities under this subchapter shall also be deemed to refer to the candidate's authorized committee(s).

§ 9002.2 Candidate.

(a) For the purposes of this subchapter, "candidate" means with respect to any presidential election, an individual who—

(1) Has been nominated by a major party for election to the office of President of the United States or the office of Vice President of the United States; or

(2) Has qualified or consented to have his or her name appear on the general election ballot (or to have the names of electors pledged to him or her on such ballot) as the candidate of a political party for election to either such office in 10 or more States. For the purposes of this section, "political party" shall be defined in accordance with 11 CFR 9002.15.

(b) An individual who is no longer actively conducting campaigns in more than one State pursuant to 11 CFR 9004.8 shall cease to be a candidate for the purpose of this subchapter.

§ 9002.3 Commission.

Commission means the Federal Election Commission, 999 E Street, NW., Washington, DC 20463.

§ 9002.4 Eligible candidates.

Eligible candidates means those Presidential and Vice Presidential candidates who have met all applicable conditions for eligibility to receive payments from the Fund under 11 CFR part 9003.

§ 9002.5 Fund.

Fund means the Presidential Election Campaign Fund established by 26 U.S.C. 9006(a).

§ 9002.6 Major party.

Major party means a political party whose candidate for the office of President in the preceding Presidential election received, as a candidate of such party, 25 percent or more of the total number of popular votes received by all candidates for such office. For the purposes of 11 CFR 9002.6, *candidate* means, with respect to any preceding Presidential election, an individual who received popular votes for the office of President in such election.

§ 9002.7 Minor party.

Minor party means a political party whose candidate for the office of President in the preceding Presidential election received, as a candidate of such party, 5 percent or more, but less than 25 percent, of the total number of popular votes received by all candidates for such office. For the purposes of 11 CFR 9002.7, *candidate* means with respect to any preceding Presidential election, an individual who received popular votes for the office of President in such election.

§ 9002.8 New party.

New party means a political party which is neither a major party nor a minor party.

§ 9002.9 Political committee.

For purposes of this subchapter, *political committee* means any committee, club, association, organization or other group of persons (whether or not incorporated) which accepts contributions or makes expenditures for the purpose of influencing, or attempting to influence, the election of any candidate to the office of President or Vice President of the United States.

§ 9002.10 Presidential election.

Presidential election means the election of Presidential and Vice Presidential electors.

§ 9002.11 Qualified campaign expense.

(a) *Qualified campaign expense* means any expenditure, including a purchase, payment, distribution, loan, advance, deposit, or gift of money or anything of value—

(1) Incurred to further a candidate's campaign for election to the office of President or Vice President of the United States;

(2) Incurred within the expenditure report period, as defined under 11 CFR 9002.12, or incurred before the beginning of such period in accordance with 11 CFR 9003.4 to the extent such expenditure is for property, services or facilities to be used during such period; and

(3) Neither the incurrence nor the payment of such expenditure constitutes a violation of any law of the United States, any law of the State in which such expense is incurred or paid, or any regulation prescribed under such Federal or State law, except that any State law which has been pre-empted by the Federal Election Campaign Act of 1971, as amended, shall not be considered a State law for purposes of this subchapter. An expenditure which constitutes such a violation shall nevertheless count against the candidate's expenditure limitation if the expenditure meets the conditions set forth at 11 CFR 9002.11(a) (1) and (2).

(b)(1) An expenditure is made to further a Presidential or Vice Presidential candidate's campaign if it is incurred by or on behalf of such candidate or his or her authorized committee. For purposes of 11 CFR 9002.11(b)(1), any expenditure incurred by or on behalf of a Presidential candidate of a political party will also be considered an expenditure to further the campaign of the Vice Presidential candidate of that party. Any expenditure incurred by or on behalf of the Vice Presidential candidate will also be considered an expenditure to further the campaign of the Presidential candidate of that party.

(2) An expenditure is made on behalf of a candidate if it is made by—

(i) Any authorized committee or any other agent of the candidate for the purpose of making an expenditure; or

(ii) Any person authorized or requested by the candidate, by the candidate's authorized committee(s), or by an agent of the candidate or his or her authorized committee(s) to make an expenditure; or

(iii) A committee which has been requested by the candidate, the candidate's authorized committee(s), or an agent thereof to make the expenditure, even though such committee is not authorized in writing.

(3) Expenditures that further the election of other candidates for any public office shall be allocated in accordance with 11 CFR 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. A candidate may make expenditures under this section in conjunction with other candidates for any public office, but each candidate shall pay his or her proportionate share of the cost in accordance with 11 CFR 106.1(a).

(4) Expenditures by a candidate's authorized committee(s) pursuant to 11 CFR 9004.6 for the travel and related ground service costs of media shall be qualified campaign expenses. Any reimbursement for travel and related services costs received by a candidate's authorized committee shall be subject to the provisions of 11 CFR 9004.6.

(5) Legal and accounting services which are provided solely to ensure compliance with 2 U.S.C. 431 *et seq.* or 26 U.S.C. 9001, *et seq.* shall be qualified campaign expenses which may be paid from payments received from the Fund. If federal funds are used to pay for such services, the payments will count against the candidate's expenditure limitation. Payments for such services may also be made from an account established in accordance with 11 CFR 9003.3 or may be provided to the committee in accordance with 11 CFR 100.7(b)(14) and 100.8(b)(15). If payments for such services are made from an account established in accordance with 11 CFR 9003.3, the payments do not count against the candidate's expenditure limitation. If payments for such services are made by a minor or new party candidate from an account containing private contributions, the payments do not count against that candidate's expenditure limitation. The amount paid by the committee shall be reported in accordance with 11 CFR part 9006. Amounts paid by the regular employer of the person providing such services pursuant to 11 CFR 100.7(b)(14) and 100.8(b)(15) shall be reported by the recipient committee in accordance with 11 CFR 104.3(h).

(c) Expenditures incurred either before the beginning of the expenditure report period or after the last day of a candidate's eligibility will be considered qualified campaign expenses if they meet the provisions of 11 CFR 9004.4(a). Expenditures described under 11 CFR 9004.4(b) will not be considered qualified campaign expenses.

§ 9002.12 Expenditure report period.

Expenditure report period means, with respect to any Presidential election, the period of time described in either paragraph (a) or (b) of this section, as appropriate. (a) In the case of a major party, the expenditure report period begins on September 1 before the election or on the date on which the major party's presidential nominee is chosen, whichever is earlier; and the period ends 30 days after the Presidential election.

(b) In the case of a minor or new party, the period will be the same as that of the major party with the shortest expenditure report period for that Presidential election as determined under paragraph (a) of this section.

§ 9002.13 Contribution.

Contribution has the same meaning given the term under 2 U.S.C. 431(8), 441b and 441c, and under 11 CFR 100.7, and 11 CFR Parts 114 and 115.

§ 9002.14 Secretary.

Secretary means the Secretary of the Treasury.

§ 9002.15 Political party.

Political party means an association, committee, or organization which nominates or selects an individual for election to any Federal office, including the office of President or Vice President of the United States, whose name appears on the general election ballot as the candidate of such association, committee, or organization.

PART 9003—ELIGIBILITY FOR PAYMENTS

Authority: 26 U.S.C. 9003 and 9009(b).

§ 9003.1 Candidate and committee agreements.

(a) *General.* (1) To become eligible to receive payments under 11 CFR part 9005, the Presidential and Vice Presidential candidates of a political party shall agree in a letter signed by the candidates to the Commission that they and their authorized committee(s) shall comply with the conditions set forth in 11 CFR 9003.1(b).

(2) Major party candidates shall sign and submit such letter to the Commission within 14 days after receiving the party's nomination for election. Minor and new party candidates shall sign and submit such letter within 14 days after such candidates have qualified to appear on the general election ballot in 10 or more states pursuant to 11 CFR 9002.2(a)(2). The Commission, on written request by a minor or new party candidate, at any time prior to the date of the general election, may extend the deadline for filing such letter except that the deadline shall be a date prior to the date of the general election.

(b) *Conditions.* The candidates shall:

(1) Agree that they have the burden of proving that disbursements made by them or any authorized committee(s) or agent(s) thereof are qualified campaign expenses as defined in 11 CFR 9002.11.

(2) Agree that they and their authorized committee(s) shall comply with the documentation requirements set forth at 11 CFR 9003.5.

(3) Agree that they and their authorized committee(s) shall provide an explanation, in addition to complying with the documentation requirements, of the connection between any disbursements made by the candidates or the authorized committee(s) of the candidates and the campaign if requested by the Commission.

(4) Agree that they and their authorized committee(s) will keep and furnish to the Commission all documentation relating to receipts and disbursements including any books, records (including bank records for all accounts), all documentation required by this subchapter including those required to be maintained under 11 CFR 9003.5, and other information that the Commission may request. If the candidate or the candidate's authorized committee maintains or uses computerized information containing any of the categories of data listed in 11 CFR 9003.6(a), the committee will

provide computerized magnetic media, such as magnetic tapes or magnetic diskettes, containing the computerized information at the times specified in 11 CFR 9007.1(b)(1) that meet the requirements of 11 CFR 9003.6(b). Upon request, documentation explaining the computer system's software capabilities shall be provided and such personnel as are necessary to explain the operation of the computer system's software and the computerized information prepared or maintained by the committee shall also be made available.

(5) Agree that they and their authorized committee(s) shall obtain and furnish to the Commission upon request all documentation relating to funds received and disbursements made on the candidate's behalf by other political committees and organizations associated with the candidate.

(6) Agree that they and their authorized committee(s) shall permit an audit and examination pursuant to 11 CFR part 9007 of all receipts and disbursements including those made by the candidate, all authorized committees and any agent or person authorized to make expenditures on behalf of the candidate or committee(s). The candidate and authorized committee(s) shall facilitate the audit by making available in one central location, office space, records and such personnel as are necessary to conduct the audit and examination, and shall pay any amounts required to be repaid under 11 CFR part 9007.

(7) Submit the name and mailing address of the person who is entitled to receive payments from the Fund on behalf of the candidates; the name and address of the depository designated by the candidates as required by 11 CFR part 103 and 11 CFR 9005.2; and the name under which each account is held at the depository at which the payments from the Fund are to be deposited.

(8) Agree that they and their authorized committee(s) shall comply with the applicable requirements of 2 U.S.C. 431 *et seq.*, 26 U.S.C. 9001 *et seq.*, and the Commission's regulations at 11 CFR parts 100–116, and 9001–9012.

(9) Agree that they and their authorized committee(s) shall pay any civil penalties included in a conciliation agreement entered into under 2 U.S.C. 437g against the candidates, any authorized committees of the candidates or any agent thereof.

§ 9003.2 Candidate certifications.

(a) *Major party candidates.* To be eligible to receive payments under 11 CFR part 9005, each Presidential and Vice Presidential candidate of a major party shall, under penalty of perjury, certify to the Commission:

(1) That the candidate and his or her authorized committee(s) have not incurred and will not incur qualified campaign expenses in excess of the aggregate payments to which they will be entitled under 11 CFR part 9004.

(2) That no contributions have been or will be accepted by the candidate or his or her authorized committee(s); except as contributions specifically solicited for, and deposited to, the candidate's legal and accounting compliance fund established under 11 CFR 9003.3(a); or except to the extent necessary to make up any deficiency in payments received from the Fund due to the application of 11 CFR 9005.2(b).

(b) *Minor and new party candidates.* To be eligible to receive any payments under 11 CFR part 9005, each Presidential and Vice Presidential candidate of a minor or new party shall, under penalty of perjury, certify to the Commission:

(1) That the candidate and his or her authorized committee(s) have not incurred and will not incur qualified campaign expenses in excess of the aggregate payments to which the eligible candidates of a major party are entitled under 11 CFR 9004.1.

(2) That no contributions to defray qualified campaign expenses have been or will be accepted by the candidate or his or her authorized committee(s) except to the extent that the qualified campaign expenses incurred exceed the aggregate payments received by such candidate from the Fund under 11 CFR 9004.2.

(c) *All candidates.* To be eligible to receive any payment under 11 CFR 9004.2, the Presidential candidate of each major, minor or new party shall certify to the Commission, under penalty of perjury, that such candidate will not knowingly make expenditures from his or her personal funds, or the personal funds of his or her immediate family, in connection with his or her campaign for the office of President in excess of $50,000 in the aggregate.

(1) For purposes of this section, the term *immediate family* means a candidate's spouse, and any child, parent, grandparent, brother, half-brother, sister, or half-sister of the candidate, and the spouses of such persons.

(2) Expenditures from personal funds made under this paragraph shall not apply against the expenditure limitations.

(3) For purposes of this section, the terms *personal funds* and *personal funds of his or her immediate family* mean:

(i) Any assets which, under applicable state law, at the time he or she became a candidate, the candidate had legal right of access to or control over, and with respect to which the candidate had either:

(A) Legal and rightful title, or

(B) An equitable interest.

(ii) Salary and other earned income from bona fide employment; dividends and proceeds from the sale of the candidate's stocks or other investments; bequests to the candidate; income from trusts established before candidacy; income from trusts established by bequest after candidacy of which the candidate is a beneficiary; gifts of a personal nature which had been customarily received prior to candidacy; proceeds from lotteries and similar legal games of chance.

(iii) A candidate may use a portion of assets jointly owned with his or her spouse as personal funds. The portion of the jointly owned assets that shall be considered as personal funds of the candidate shall be that portion which is the candidate's share under the instrument(s) of conveyance or ownership. If no specific share is indicated by any instrument of conveyance or ownership, the value of one-half of the property used shall be considered as personal funds of the candidate.

(4) For purposes of this section, expenditures from personal funds made by a candidate of a political party for the office of Vice President shall be considered to be expenditures made by the candidate of such party for the office of President.

(5) Contributions made by members of a candidate's family from funds which do not meet the definition of personal funds under 11 CFR 9003.2(c)(3) shall not count against such candidate's $50,000 expenditure limitation under 11 CFR 9003.2(c).

(6) Personal funds expended pursuant to this section shall be first deposited in an account established in accordance with 11 CFR 9003.3 (b) or (c).

(7) The provisions of this section shall not operate to limit the candidate's liability for, nor the candidate's ability to pay, any repayments required under 11 CFR part 9007. If the candidate or his or her committee knowingly incurs expenditures in excess of the limitations of 11 CFR 110.8(a), the Commission may seek civil penalties under 11 CFR part 111 in addition to any repayment determinations made on the basis of such excessive expenditures.

(8) Expenditures made using a credit card for which the candidate is jointly or solely liable will count against the limits

of this section to the extent that the full amount due, including any finance charge, is not paid by the committee within 60 days after the closing date of the billing statement on which the charges first appear. For purposes of this section, the "closing date" shall be the date indicated on the billing statement which serves as the cutoff date for determining which charges are included on that billing statement.

(d) *Form.* Major party candidates shall submit the certifications required under 11 CFR 9003.2 in a letter which shall be signed and submitted within 14 days after receiving the party's nomination for election. Minor and new party candidates shall sign and submit such letter within 14 days after such candidates have qualified to appear on the general election ballot in 10 or more States pursuant to 11 CFR 9002.2(a)(2). The Commission, upon written request by a minor or new party candidate made at any time prior to the date of the general election, may extend the deadline for filing such letter, except that the deadline shall be a date prior to the day of the general election.

§ 9003.3 Allowable contributions.

(a) *Legal and accounting compliance fund—major party candidates*—(1) *Sources.* (i) A major party candidate may accept contributions to a legal and accounting compliance fund if such contributions are received and disbursed in accordance with this section. A legal and accounting compliance fund may be established by such candidate prior to being nominated or selected as the candidate of a political party for the office of President or Vice President of the United States.

(A) All solicitations for contributions to this fund shall clearly state that such contributions are being solicited for this fund.

(B) Contributions to this fund shall be subject to the limitations and prohibitions of 11 CFR parts 110, 114, and 115.

(ii) Funds received during the matching payment period that are remaining in a candidate's primary election account, which funds are in excess of any amount needed to pay remaining primary expenses or any amount required to be reimbursed to the Presidential Primary Matching Payment Account under 11 CFR 9038.2, may be transferred to the legal and accounting compliance fund without regard to the contribution limitations of 11 CFR part 110 and used for any purpose permitted under this section. The excess funds so transferred may include contributions made before the beginning of the expenditure report period, which contributions do not exceed the contributor's limit for the primary election. Such contributions need not be redesignated by the contributors for the legal and accounting compliance fund.

(iii) Contributions that are made after the beginning of the expenditure report period but which are designated for the primary election, and contributions that exceed the contributor's limit for the primary election, may be redesignated for the legal and accounting compliance fund and transferred to or deposited in such fund if the candidate obtains the contributor's redesignation in accordance with 11 CFR 110.1. Contributions that do not exceed the contributor's limit for the primary election may be redesignated and deposited in the legal and accounting compliance fund only if—

(A) The contributions represent funds in excess of any amount needed to pay remaining primary expenses;

(B) The redesignations are received within 60 days of the Treasurer's receipt of the contributions;

(C) The requirements of 11 CFR 110.1 (b)(5) and (l) regarding redesignations are satisfied; and

(D) The contributions have not been submitted for matching.

All contributions so redesignated and deposited shall be subject to the contribution limitations applicable for the general election, pursuant to 11 CFR 110.1(b)(2)(i).

(2) *Uses.* (i) Contributions to the legal and accounting compliance fund shall be used only for the following purposes:

(A) To defray the cost of legal and accounting services provided solely to ensure compliance with 2 U.S.C. 431 *et seq.* and 26 U.S.C. 9001 *et seq.* in accordance with 11 CFR 9003.3(a)(2)(ii);

(B) To defray in accordance with 11 CFR 9003.3(a)(2)(ii)(A), that portion of expenditures for payroll, overhead, and computer services related to ensuring compliance with 2 U.S.C. 431 *et seq.* and 26 U.S.C. 9001 *et seq.*;

(C) To defray any civil or criminal penalties imposed pursuant to 2 U.S.C. 437g or 26 U.S.C. 9012;

(D) To make repayments under 11 CFR 9007.2;

(E) To defray the cost of soliciting contributions to the legal and accounting compliance fund;

(F) To defray the cost of producing, delivering and explaining the computerized information and materials provided pursuant to 11 CFR 9003.6 and explaining the operation of the computer system's software;

(G) To make a loan to an account established pursuant to 11 CFR 9003.4 to defray qualified campaign expenses incurred prior to the expenditure report period or prior to receipt of federal funds, provided that the amounts so loaned are restored to the legal and accounting compliance fund; and

(H) To defray unreimbursed costs incurred in providing transportation and services for the Secret Service and national security staff pursuant to 11 CFR 9004.6.

(ii)(A) Expenditures for payroll (including payroll taxes), overhead and computer services, a portion of which are related to ensuring compliance with title 2 and chapter 95 of title 26, shall be initially paid from the candidate's federal fund account under 11 CFR 9005.2 and may be later reimbursed by the compliance fund. For purposes of 11 CFR 9003.3(a)(2)(i)(B), a candidate may use contributions to the compliance fund to reimburse his or her federal fund account an amount equal to 10% of the payroll and overhead expenditures of his or her national campaign headquarters and state offices. Overhead expenditures include, but are not limited to rent, utilities, office equipment, furniture, supplies and all telephone charges except for telephone charges related to a special use such as voter registration and get out the vote efforts. In addition, a candidate may use contributions to the compliance fund to reimburse his or her federal fund account an amount equal to 70% of the costs (other than payroll) associated with computer services. Such costs include but are not limited to rental and maintenance of computer equipment, data entry services not performed by committee personnel, and related supplies. If the candidate wishes to claim a larger compliance exemption for payroll or overhead expenditures, the candidate shall establish allocation percentages for each individual who spends all or a portion of his or her time to perform duties which are considered necessary to ensure compliance with title 2 or chapter 95 of title 26. The candidate shall keep detailed records to support the derivation of each percentage. Such records shall indicate which duties are considered compliance and the percentage of time each person spends on such activity. If the candidate wishes to claim a larger compliance exemption for costs associated with computer services, the candidate shall establish allocation percentages for each computer function that is considered necessary, in whole or in part, to ensure compliance with 2 U.S.C. 431 *et seq.*, and 26 U.S.C. 9001 *et seq.* The allocation shall be based on a reasonable estimate of the costs associated with each computer function, such as the costs for data entry services performed by persons other than committee personnel and processing time. The candidate shall keep detailed records to support such calculations. The records shall indicate which computer functions are considered compliance-related and shall reflect which costs are associated with each computer function. The Commission's Financial Control and Compliance Manual for General Election Candidates Receiving Public Funding contains some accepted alternative allocation methods for determining the amount of salaries and overhead expenditures that may be considered exempt compliance costs.

(B) Reimbursement from the compliance fund may be made to the separate account maintained for federal funds under 11 CFR 9005.2 for legal and accounting compliance services disbursements that are initially paid from the separate federal funds account. Such reimbursement must be made prior to any final repayment determination by the Commission pursuant to 11 CFR 9007.2. Any amounts so reimbursed to the federal fund account may not subsequently be transferred back to the legal and accounting compliance fund.

(iii) Amounts paid from this account for the purposes permitted by 11 CFR 9003.3(a)(2)(i) (A) through (E) shall not be subject to the expenditure limits of 2 U.S.C. 441a(b) and 11 CFR 110.8. (See also 11 CFR 100.8(b)(15).) When the proceeds of loans made in accordance with 11 CFR 9003.2(a)(2)(i)(F) are expended on qualified campaign expenses, such expenditures shall count against the candidate's expenditure limit.

(iv) Contributions to or funds deposited in the legal and accounting compliance fund may not be used to retire debts remaining from the Presidential primaries, except that, if after payment of all expenses relating to the general election, there are excess campaign funds, such funds may be used for any purpose permitted under 2 U.S.C. 439a and 11 CFR part 113, including payment of primary election debts.

(3) *Deposit and disclosure.* (i) Amounts received pursuant to 11 CFR 9003.3(a)(1) shall be deposited and maintained in an account separate from that described in 11 CFR 9005.2 and shall not be commingled with any money paid to the candidate by the Secretary pursuant to 11 CFR 9005.2.

(ii) The receipts to and disbursements from this account shall be reported in a separate report in accordance with 11 CFR 9006.1(b)(2). All contributions made to this account shall be recorded in accordance with 11 CFR 102.9. Disbursements made from this account shall be documented in the same manner provided in 11 CFR 9003.5.

(b) *Contributions to defray qualified campaign expenses—major party candidates.* (1) A major party candidate or his or her authorized committee(s) may solicit contributions to defray qualified campaign expenses to the extent necessary to make up any deficiency in payments received from the Fund due to the application of 11 CFR 9005.2(b).

(2) Such contributions may be deposited in a separate account or may be deposited with federal funds received under 11 CFR 9005.2. Disbursements from this account shall be made only to defray qualified campaign expenses and to defray the cost of soliciting contributions to such account. All disbursements from this account shall be documented in accordance with 11 CFR 9003.5 and shall be reported in accordance with 11 CFR 9006.1.

(3) A candidate may make transfers to this account from his or her legal and accounting compliance fund.

(4) The contributions received under this section shall be subject to the limitations and prohibitions of 11 CFR parts 110, 114 and 115 and shall be aggregated with all contributions made by the same persons to the candidate's legal and accounting compliance fund under 11 CFR 9003.3(a) for the purposes of such limitations.

(5) Any costs incurred for soliciting contributions to this account shall not be considered expenditures to the extent that the aggregate of such costs does not exceed 20 percent of the expenditure limitation under 11 CFR 9003.2(a)(1). These costs shall, however, be reported as disbursements in accordance with 11 CFR part 104 and 11 CFR 9006.1. For purposes of this section, a candidate may exclude from the expenditure limitation an amount equal to 10% of the payroll (including payroll taxes) and overhead expenditures of his or her national campaign headquarters and state offices as exempt fundraising costs.

(6) Any costs incurred for legal and accounting services which are provided solely to ensure compliance with 2 U.S.C. 431 *et seq.* and 26 U.S.C. 9001 *et seq.* shall not count against the candidate's expenditure limitation. Such costs include the cost of producing, delivering and explaining the computerized information and materials provided pursuant to 11 CFR 9003.6 and explaining the operation of the computer system's software. For purposes of this section, a candidate may exclude from the expenditure limitation an amount equal to 10% of the payroll (including payroll taxes) and overhead expenditures of his or her national campaign headquarters and state offices. In addition, a candidate may exclude from the expenditure limitation an amount equal to 70% of the costs (other than payroll) associated with computer services.

(i) For purposes of 11 CFR 9003.3(b)(6), overhead costs include, but are not limited to, rent, utilities, office equipment, furniture, supplies and all telephone charges except for telephone charges related to a special use such as voter registration and get out the vote efforts.

(ii) For purposes of 11 CFR 9003.3(b)(6) costs associated with computer services include, but are not limited to, rental and maintenance of computer equipment, data entry services not performed by committee personnel, and related supplies.

(7) If the candidate wishes to claim a larger compliance or fundraising exemption under 11 CFR 9003.3(b) (5) or (6) for payroll and overhead expenditures, the candidate shall establish allocation percentages for each individual who spends all or a portion of his or her time to perform duties which are considered compliance or fundraising. The candidate shall keep detailed records to support the derivation of each percentage. Such records shall indicate which duties are considered compliance or fundraising and the percentage of time each person spends on such activity.

(8) If the candidate wishes to claim a larger compliance exemption under 11 CFR 9003.3(b)(6) for costs associated with computer services, the candidate shall establish allocation percentages for each computer function that is considered necessary, in whole or in part, to ensure compliance with 2 U.S.C. 431 *et seq.* and 26 U.S.C. 9001 *et seq.* The allocation shall be based on a reasonable estimate of the costs associated with each computer function, such as the costs for data entry services performed by other than committee personnel and processing time. The candidate shall keep detailed records to support such calculations. The records shall indicate which computer functions are considered compliance-related and shall reflect which costs are associated with each computer function.

(9) The Commission's Financial Control and Compliance Manual for General Election Candidates Receiving Public Funding contains some accepted alternative allocation methods for determining the amount of salaries and overhead expenditures that may be

considered exempt compliance costs or exempt fundraising costs.

(c) *Contributions to defray qualified campaign expenses—minor and new party candidates.* (1) A minor or new party candidate may solicit contributions to defray qualified campaign expenses which exceed the amount received by such candidate from the Fund, subject to the limits of 11 CFR 9003.2(b).

(2) The contributions received under this section shall be subject to the limitations and prohibitions of 11 CFR parts 110, 114 and 115.

(3) Such contributions may be deposited in a separate account or may be deposited with federal funds received under 11 CFR 9005.2. Disbursements from this account shall be made only for the following purposes:

(i) To defray qualified campaign expenses;

(ii) To make repayments under 11 CFR 9007.2;

(iii) To defray the cost of soliciting contributions to such account;

(iv) To defray the cost of legal and accounting services provided solely to ensure compliance with 2 U.S.C. 431 *et seq.* and 26 U.S.C. 9001 *et seq*;

(v) To defray the cost of producing, delivering and explaining the computerized information and materials provided pursuant to 11 CFR 9003.6 and explaining the operation of the computer system's software.

(4) All disbursements from this account shall be documented in accordance with 11 CFR 9003.5 and shall be reported in accordance with 11 CFR part 104 and 9006.1.

(5) Any costs incurred for soliciting contributions to this account shall not be considered expenditures to the extent that the aggregate of such costs does not exceed 20 percent of the expenditure limitation under 11 CFR 9003.2(a)(1). These costs shall, however, be reported as disbursements in accordance with 11 CFR part 104 and 9006.1. For purposes of this section, a candidate may exclude from the expenditure limitation an amount equal to 10% of the payroll (including payroll taxes) and overhead expenditures of his or her national campaign headquarters and state offices as exempt fundraising costs.

(6) Any costs incurred for legal and accounting services which are provided solely to ensure compliance with 2 U.S.C. 431 *et seq.* and 26 U.S.C. 9001 *et seq.* shall not count against the candidate's expenditure limitation. For purposes of this section, a candidate may exclude from the expenditure limitation an amount equal to 10% of the payroll (including payroll taxes) and overhead expenditures of his or her national campaign headquarters and state offices. In addition, a candidate may exclude from the expenditure limitation an amount equal to 70% of the costs (other than payroll) associated with computer services.

(i) For purposes of 11 CFR 9003.3(c)(6), overhead costs include, but are not limited to, rent, utilities, office equipment, furniture, supplies and all telephone charges except for telephone charges related to a special use such as voter registration and get out the vote efforts.

(ii) For purposes of 11 CFR 9003.3(c)(6) costs associated with computer services include but are not limited to, rental and maintenance of computer equipment, data entry services not performed by committee personnel, and related supplies.

(7) If the candidate wishes to claim a larger compliance or fundraising exemption under 11 CFR 9003.3(c)(6) for payroll and overhead expenditures, the candidate shall establish allocation percentages for each individual who spends all or a portion of his or her time to perform duties which are considered compliance or fundraising. The candidate shall keep detailed records to support the derivation of each percentage. Such records shall indicate which duties are considered compliance or fundraising and the percentage of time each person spends on such activity.

(8) If the candidate wishes to claim a larger compliance exemption under 11 CFR 9003.3(c)(6) for costs associated with computer services, the candidate shall establish allocation percentages for each computer function that is considered necessary, in whole or in part, to ensure compliance with 2 U.S.C. 431 *et seq.* and 26 U.S.C. 9001 *et seq.* The allocation shall be based on a reasonable estimate of the costs associated with each computer function, such as the costs for data entry services performed by other than committee personnel and processing time. The candidate shall keep detailed records to support such calculations. The records shall indicate which computer functions are considered compliance-related and shall reflect which costs are associated with each computer function.

(9) The candidate shall keep and maintain a separate record of disbursements made to defray exempt legal and accounting costs under 11 CFR 9003.3(c) (6) and (7) and shall report such disbursements in accordance with 11 CFR part 104 and 11 CFR 9006.1.

(10) The Commission's Financial Control and Compliance Manual for General Election Candidates Receiving Public Funding contains some accepted alternative allocation methods for determining the amount of salaries and overhead expenditures that may be considered exempt compliance costs or exempt fundraising costs.

§ 9003.4 Expenses incurred prior to the beginning of the expenditure report period or prior to receipt of Federal funds.

(a) *Permissible expenditures.* (1) A candidate may incur expenditures before the beginning of the expenditure report period, as defined at 11 CFR 9002.12, if such expenditures are for property, services or facilities which are to be used in connection with his or her general election campaign and which are for use during the expenditure report period. Such expenditures will be considered qualified campaign expenses. Examples of such expenditures include but are not limited to: Expenditures for establishing financial accounting systems, expenditures for organizational planning and expenditures for polling.

(2) A candidate may incur qualified campaign expenses prior to receiving payments under 11 CFR part 9005.

(b) *Sources.* (1) A candidate may obtain a loan which meets the requirements of 11 CFR 100.7(b)(11) for loans in the ordinary course of business to defray permissible expenditures described in 11 CFR 9003.4(a). A candidate receiving payments equal to the expenditure limitation in 11 CFR 110.8 shall make full repayment of principal and interest on such loans from payments received by the candidate under 11 CFR part 9005 within 15 days of receiving such payments.

(2) A major party candidate may borrow from his or her legal and accounting compliance fund for the purposes of defraying permissible expenditures described in 11 CFR 9003.4(a). All amounts borrowed from the legal and accounting compliance fund must be restored to such fund after the beginning of the expenditure report period either from federal funds received under 11 CFR part 9005 or private contributions received under 11 CFR 9003.3(b). For candidates receiving federal funds, restoration shall be made within 15 days after receipt of such funds.

(3) A minor or new party candidate may defray such expenditures from contributions received in accordance with 11 CFR 9003.3(c).

(4)(i) A candidate who has received federal funding under 11 CFR part 9031 *et seq.*, may borrow from his or her primary election committee(s) an amount not to exceed the residual balance projected to remain in the candidate's primary account(s) on the basis of the formula set forth at 11 CFR 9038.3(c). A major party candidate receiving payments equal to the expenditure limitation shall reimburse amounts borrowed from his or her primary committee(s) from payments received by the candidate under 11 CFR part 9005 within 15 days of such receipt.

(ii) A candidate who has not received federal funding during the primary campaign may borrow at any time from his or her primary account(s) to defray such expenditures, provided that a major party candidate receiving payments equal to the expenditure limitation shall reimburse all amounts borrowed from his or her primary committee(s) from payments received by the candidate under 11 CFR part 9005 within 15 days of such receipt.

(5) A candidate may use personal funds in accordance with 11 CFR 9003.2(c), up to his or her $50,000 limit, to defray such expenditures.

(c) *Deposit and disclosure.* Amounts received or borrowed by a candidate under 11 CFR 9003.4(b) to defray expenditures permitted under 11 CFR 9003.4(a) shall be deposited in a separate account to be used only for such expenditures. All receipts and disbursements from such account shall be reported pursuant to 11 CFR 9006.1(a) and documented in accordance with 11 CFR 9003.5

§ 9003.5 Documentation of disbursements.

(a) *Burden of proof.* Each candidate shall have the burden of proving that disbursements made by the candidate or his or her authorized committee(s) or persons authorized to make expenditures on behalf of the candidate or authorized committee(s) are qualified campaign expenses as defined in 11 CFR 9002.11. The candidate and his or her authorized committee(s) shall obtain and furnish to the Commission at its request any evidence regarding qualified campaign expenses made by the candidate, his or her authorized committees and agents or persons authorized to make expenditures on behalf of the candidate or committee(s) as provided in 11 CFR 9003.5(b).

(b) *Documentation required.* (1) For disbursements in excess of $200 to a payee, the candidate shall present either:

(i) A receipted bill from the payee that states the purpose of the disbursement; or

(ii) If such a receipt is not available, a canceled check negotiated by the payee, and

(A) One of the following documents generated by the payee: A bill, invoice, or voucher that states the purpose of the disbursement; or

(B) Where the documents specified in 11 CFR 9003.5(b)(1)(ii)(A) are not available, a voucher or contemporaneous memorandum from the candidate or the committee that states the purpose of the disbursement; or

(iii) If neither a receipted bill as specified in 11 CFR 9003.5(b)(1)(i) nor the supporting documentation specified in 11 CFR 9003.5(b)(1)(ii) is available, a canceled check negotiated by the payee that states the purpose of the disbursement.

(iv) Where the supporting documentation required in 11 CFR 9003.5(b)(1) (i), (ii) or (iii) is not available, the candidate or committee may present a canceled check and collateral evidence to document the qualified campaign expense. Such collateral evidence may include but is not limited to:

(A) Evidence demonstrating that the expenditure is part of an identifiable program or project which is otherwise sufficiently documented such as a disbursement which is one of a number of documented disbursements relating to a campaign mailing or to the operation of a campaign office:

(B) Evidence that the disbursement is covered by a pre-established written campaign committee policy, such as a daily travel expense policy.

(2) For all other disbursements the candidate shall present:

(i) A record disclosing the full name and mailing address of the payee, the amount, date and purpose of the disbursement, if made from a petty cash fund; or

(ii) A canceled check negotiated by the payee that states the full name and mailing address of the payee, and the amount, date and purpose of the disbursement.

(3) For purposes of this section:

(i) *Payee* means the person who provides the goods or services to the candidate or committee in return for the disbursement; except that an individual will be considered a payee under this section if he or she receives $500 or less advanced for travel and/or subsistence and if the individual is the recipient of the goods or services purchased.

(ii) *Purpose* means the full name and mailing address of the payee, the date and amount of the disbursement, and a brief description of the goods or services purchased.

(c) *Retention of records.* The candidate shall retain records with respect to each disbursement and receipt, including bank records, vouchers, worksheets, receipts, bills and accounts, journals, ledgers, fundraising solicitation material, accounting systems documentation, and any related materials documenting campaign receipts and disbursements, for a period of three years pursuant to 11 CFR 102.9(c), and shall present these records to the Commission on request.

(d) *List of capital and other assets*—(1) *Capital assets.* The candidate or committee shall maintain a list of all capital assets whose purchase price exceeded $2000 when acquired by the candidate's authorized committee(s). The list shall include a brief description of each capital asset, the purchase price, the date it was acquired, the method of disposition and the amount received in disposition. For purposes of this section, *capital asset* shall be defined in accordance with 11 CFR 9004.9(d)(1).

(2) *Other assets.* The candidate or committee shall maintain a list of other assets acquired for use in fundraising or as collateral for campaign loans, if the aggregate value of such assets exceeds $5000. The list shall include a brief description of each such asset, the fair market value of each asset, the method of disposition and the amount received in disposition. The fair market value of other assets shall be determined in accordance with 11 CFR 9004.9(d)(2).

§ 9003.6 Production of computer information.

(a) *Categories of computerized information to be provided.* If the candidate or the candidate's authorized committee maintains or uses computerized information containing any of the categories of data listed in paragraphs (a)(1) through (a)(9) of this section, the committee shall provide computerized magnetic media, such as magnetic tapes or magnetic diskettes, containing the computerized information at the times specified in 11 CFR 9007.1(b)(1):

(1) Information required by law to be maintained regarding the committee's receipts or disbursements;

(2) Receipts by and disbursements from a legal and accounting compliance fund under 11 CFR 9003.3(a), including the allocation of payroll and overhead expenditures;

(3) Receipts and disbursements under 11 CFR 9003.3 (b) or (c) to defray the costs of soliciting contributions or to defray the costs of legal and accounting services, including the allocation of payroll and overhead expenditures;

(4) Records relating to the costs of producing broadcast communications and purchasing airtime;

(5) Records used to prepare statements of net outstanding qualified campaign expenses;

(6) Records used to reconcile bank statements;

(7) Disbursements made and reimbursements received for the cost of transportation, ground services and facilities made available to media personnel, including records relating to how costs charged to media personnel were determined;

(8) Records relating to the acquisition, use and disposition of capital assets or other assets; and

(9) Any other information that may be used during the Commission's audit to review the committee's receipts, disbursements, loans, debts, obligations, bank reconciliations or statements of net outstanding qualified campaign expenses.

(b) *Organization of computerized information and technical specifications.* The computerized magnetic media shall be prepared and delivered at the committee's expense and shall conform to the technical specifications, including file requirements, described in the Federal Election Commission's Computerized Magnetic Media Requirements for title 26 Candidates/Committees Receiving Federal Funding. The data contained in the computerized magnetic media provided to the Commission shall be organized in the order specified by the Computerized Magnetic Media Requirements.

(c) *Additional materials and assistance.* Upon request, the committee shall produce documentation explaining the computer system's software capabilities, such as user guides, technical manuals, formats, layouts and other materials for processing and analyzing the information requested. Upon request, the committee shall also make available such personnel as are necessary to explain the operation of the computer system's software and the computerized information prepared or maintained by the committee.

PART 9004—ENTITLEMENT OF ELIGIBLE CANDIDATES TO PAYMENTS; USE OF PAYMENTS

Authority: 26 U.S.C. 9004 and 9009(b).

§ 9004.1 Major parties.

The eligible candidates of each major party in a Presidential election shall be entitled to equal payments under 11 CFR part 9005 in an amount which, in the aggregate, shall not exceed $20,000,000 as adjusted by the Consumer Price Index in the manner described in 11 CFR 110.9(c).

§ 9004.2 Pre-election payments for minor and new party candidates.

(a) *Candidate of a minor party in the preceding election.* An eligible candidate of a minor party is entitled to pre-election payments:

(1) If he or she received at least 5% of the total popular vote as the candidate of a minor party in the preceding election whether or not he or she is the same minor party's candidate in this election.

(2) In an amount which is equal, in the aggregate, to a proportionate share of the amount to which major party candidates are entitled under 11 CFR 9004.1.

The aggregate amount received by a minor party candidate shall bear the same ratio to the amount received by the major party candidates as the number of popular votes received by the minor party Presidential candidate in the preceding Presidential election bears to the average number of popular votes received by all major party candidates in that election.

(b) *Candidate of a minor party in the current election.* The eligible candidate of a minor party whose candidate for the office of President in the preceding election received at least 5% but less than 25% of the total popular vote is eligible to receive pre-election payments. The amount which a minor party candidate is entitled to receive under this section shall be computed pursuant to 11 CFR 9004.2(a) based on the number of popular votes received by the minor party's candidate in the preceding Presidential election; however, the amount to which the minor party candidate is entitled under this section shall be reduced by the amount to which the minor party's Presidential candidate in this election is entitled under 11 CFR 9004.2(a), if any.

(c) *New party candidate.* A candidate of a new party who was a candidate for the office of President in at least 10 States in the preceding election may be eligible to receive pre-election payments if he or she received at least 5% but less than 25% of the total popular vote in the preceding election. The amount which a new party candidate is entitled to receive under this section shall be computed pursuant to 11 CFR 9004.2(a) based on the number of popular votes received by the new party candidate in the preceding election. If a new party candidate is entitled to payments under this section, the amount of the entitlement shall be reduced by the amount to which the candidate is entitled under 11 CFR 9004.2(a), if any.

§ 9004.3 Post-election payments.

(a) *Minor and new party candidates.* Eligible candidates of a minor party or of a new party who, as candidates, receive 5 percent or more of the total number of popular votes cast for the office of President in the election shall be entitled to payments under 11 CFR part 9005 equal, in the aggregate, to a proportionate share of the amount allowed for major party candidates under 11 CFR 9004.1. The amount to which a minor or new party candidate is entitled shall bear the same ratio to the amount received by the major party candidates as the number of popular votes received by the minor or new party candidate in the Presidential election bears to the average number of popular votes received by the major party candidates for President in that election.

(b) *Amount of entitlement.* The aggregate payments to which an eligible candidate shall be entitled shall not exceed an amount equal to the lower of:

(1) The amount of qualified campaign expenses incurred by such eligible candidate and his or her authorized committee(s), reduced by the amount of contributions which are received to defray qualified campaign expenses by such eligible candidate and such committee(s); or

(2) The aggregate payments to which the eligible candidates of a major party are entitled under 11 CFR 9004.1, reduced by the amount of contributions received by such eligible candidates and their authorized committees to defray qualified campaign expenses in the case of a deficiency in the Fund.

(c) *Amount of entitlement limited by pre-election payment.* If an eligible candidate is entitled to payment under 11 CFR 9004.2, the amount allowable to that candidate under this section shall also be limited to the amount, if any, by which the entitlement under 11 CFR 9004.3(a) exceeds the amount of the entitlement under 11 CFR 9004.2.

§ 9004.4 Use of payments.

(a) *Qualified campaign expenses.* An eligible candidate shall use payments received under 11 CFR part 9005 only for the following purposes:

(1) A candidate may use such payments to defray qualified campaign expenses;

(2) A candidate may use such payments to repay loans that meet the requirements of 11 CFR 100.7(a)(1) or 100.7(b)(11) or to otherwise restore funds (other than contributions received pursuant to 11 CFR 9003.3(b) and expended to defray qualified campaign expenses) used to defray qualified campaign expenses;

(3) A candidate may use such payments to restore funds expended in accordance with 11 CFR 9003.4 for qualified campaign expenses incurred by the candidate prior to the beginning of the expenditure report period.

(4) *Winding down costs.* The following costs shall be considered qualified campaign expenses:

(i) Costs associated with the termination of the candidate's general election campaign such as complying with the post-election requirements of the Act and other necessary administrative costs associated with winding down the campaign, including office space rental, staff salaries and office supplies; or

(ii) Costs incurred by the candidate prior to the end of the expenditure report period for which written arrangement or commitment was made on or before the close of the expenditure report period.

(b) *Non-qualified campaign expenses*—(1) *General.* The following are examples of disbursements that are not qualified campaign expenses.

(2) *Excessive expenditures.* An expenditure which is in excess of any of the limitations under 11 CFR 9003.2 shall not be considered a qualified campaign expense. The Commission will calculate the amount of expenditures attributable to these limitations using the full amounts originally charged for goods and services rendered to the committee and not the amounts for which such obligations were later settled and paid, unless the committee can demonstrate that the lower amount paid reflects a reasonable settlement of a bona fide dispute with the creditor.

(3) *Expenditures incurred after the close of the expenditure report period.* Any expenditures incurred after the close of the expenditure report period, as defined in 11 CFR 9002.12, are not qualified campaign expenses except to the extent permitted under 11 CFR 9004.4(a)(4).

(4) *Civil or criminal penalties.* Civil or criminal penalties paid pursuant to the Federal Election Campaign Act are not qualified campaign expenses and cannot be defrayed from payments received under 11 CFR part 9005. Penalties may be paid from contributions in the candidate's legal and accounting compliance fund, in accordance with 11 CFR 9003.3(a)(2)(i)(C). Additional amounts may be received and expended to pay such penalties, if necessary. These funds shall not be considered contributions or expenditures but all amounts so received shall be subject to the prohibitions of the Act. Amounts received and expended under this section shall be reported in accordance with 11 CFR part 104.

(5) *Solicitation expenses.* Any expenses incurred by a major party candidate to solicit contributions to a legal and accounting compliance fund established pursuant to 11 CFR 9003.3(a) are not qualified campaign expenses and cannot be defrayed from payments received under 11 CFR part 9005.

(6) *Payments to candidate.* Payments made to the candidate by his or her committee, other than to reimburse funds advanced by the candidate for qualified campaign expenses, are not qualified campaign expenses.

(7) *Payments to other authorized committees.* Payments, including transfers, contributions and loans, to other committees authorized by the same candidate for a different election are not qualified campaign expenses.

(c) *Repayments.* Repayments may be made only from the following sources: Personal funds of the candidate (without regard to the limitations of 11 CFR 9003.2(c)), contributions and federal funds in the committee's account(s), and any additional funds raised subject to the limitations and prohibitions of the Federal Election Campaign Act of 1971, as amended.

§ 9004.5 Investment of public funds.

Investment of public funds or any other use of public funds to generate income is permissible, provided that an amount equal to all net income derived from such investments, less Federal, State and local taxes paid on such income, shall be repaid to the Secretary. Any net loss resulting from the investment of public funds will be considered a non-qualified campaign expense and an amount equal to the amount of such net loss shall be repaid to the United States Treasury as provided under 11 CFR 9007.2(b)(2)(i).

§ 9004.6 Reimbursements for transportation and services made available to media personnel.

(a) If an authorized committee incurs expenditures for transportation, ground services and facilities (including air travel, ground transportation, housing, meals, telephone service, typewriters) made available to media personnel, Secret Service personnel or national security staff, such expenditures will be considered qualified campaign expenses and, except for costs relating to Secret Service personnel or national security staff, subject to the overall expenditure limitations of 11 CFR 9003.2 (a)(1) and (b)(1).

(b) If reimbursement for such expenditures is received by a committee, the amount of such reimbursement for each media representative shall not exceed either: The media representative's pro rata share of the actual cost of the transportation and services made available; or a reasonable estimate of the media representative's pro rata share of the actual cost of the transportation and services made available. A media representative's pro rata share shall be calculated by dividing the total cost of the transportation and services by the total number of individuals to whom such transportation and services are made available. For purposes of this calculation, the total number of individuals shall include committee staff, media personnel, Secret Service personnel, national security staff and any other individuals to whom such transportation and services are made available. The total amount of reimbursements received from a media representative under this section shall not exceed the actual pro rata cost of the transportation and services made available to that media representative by more than 10%.

(c) The total amount paid by an authorized committee for the cost of transportation or for ground services and facilities shall be reported as an expenditure in accordance with 11 CFR 104.3(b)(2)(i). Any reimbursement received by such committee for transportation or ground services and facilities shall be reported in accordance with 11 CFR 104.3(a)(3)(ix).

(d)(1) The committee may deduct from the amount of expenditures subject to the overall expenditure limitation of 11 CFR 9003.2 (a)(1) and (b)(1) the amount of reimbursements received in payment for the actual cost of transportation and services described in paragraph (a) of this section. This deduction shall not exceed the amount the committee expended for the actual cost of transportation and services provided. The committee may also deduct from the overall expenditure limitation an additional amount of reimbursements received equal to 3% of the actual cost of transportation and services provided under this section as the administrative cost to the committee of providing such services and seeking reimbursement for them. If the committee has incurred higher administrative costs in providing these services, the committee must document the total cost incurred for such services in order to deduct a higher amount of reimbursements received from the overall expenditure limitation. Amounts reimbursed that exceed the amount actually paid by the committee for transportation and services provided under paragraph (a) of this section plus the amount of administrative costs permitted by this section up to the maximum amount that may be received under paragraph (b) of this section shall be repaid to the Treasury. Amounts paid by the committee for transportation, services and administrative costs for which no reimbursement is received will be considered qualified campaign expenses subject to the overall expenditure limitation in accordance with paragraph (a).

(2) For the purposes of this section, "administrative costs" shall include all costs incurred by the committee for making travel arrangements and for seeking reimbursements, whether performed by committee staff or independent contractors.

§ 9004.7 Allocation of travel expenditures.

(a) Notwithstanding the provisions of 11 CFR part 106, expenditures for travel relating to a Presidential or Vice Presidential candidate's campaign by any individual, including a candidate, shall, pursuant to the provisions of 11 CFR 9004.7(b), be qualified campaign expenses and be reported by the candidate's authorized committee(s) as expenditures.

(b)(1) For a trip which is entirely campaign-related, the total cost of the trip shall be a qualified campaign expense and a reportable expenditure.

(2) For a trip which includes campaign-related and non-campaign related stops, that portion of the cost of the trip allocable to campaign activity shall be a qualified campaign expense and a reportable expenditure. Such portion shall be determined by calculating what the trip would have cost from the point of origin of the trip to the first campaign-related stop and from the stop through each subsequent campaign-related stop to the point of origin. If any campaign activity, other than incidental contacts, is conducted at a stop, that stop shall be considered campaign-related.

(3) For each trip, an itinerary shall be prepared and such itinerary shall be made available for Commission inspection.

(4) For trips by government conveyance or by charter, a list of all passengers on such trip, along with a designation of which passengers are and which are not campaign-related, shall be made available for Commission inspection.

(5) If any individual, including a candidate, uses government conveyance or accommodations paid for by a government entity for campaign-related travel, the candidate's authorized committee shall pay the appropriate government entity an amount equal to:

(i) The first class commercial air fare plus the cost of other services, in the case of travel to a city served by a regularly scheduled commercial service; or

(ii) The commercial charter rate plus the cost of other services, in the case of travel to a city not served by a regularly scheduled commercial service.

(6) Travel expenses of a candidate's spouse and family when accompanying the candidate on campaign-related travel may be treated as qualified campaign expenses and reportable expenditures. If the spouse or family members conduct campaign-related activities, their travel expenses shall be qualified campaign expenses and reportable expenditures.

(7) If any individual, including a candidate, incurs expenses for campaign-related travel, other than by use of government conveyance or accommodations, an amount equal to that portion of the actual cost of the conveyance or accommodations which is allocable to all passengers, including the candidate, traveling for campaign purposes shall be a qualified campaign expense and shall be reported by the committee as an expenditure.

(i) If the trip is by charter, the actual cost for each passenger shall be determined by dividing the total operating cost for the charter by the total number of passengers transported. The amount which is a qualified campaign expense and a reportable expenditure shall be calculated in accordance with the formula set forth at 11 CFR 9004.7(b)(2) on the basis of the actual cost per passenger multiplied by the number of passengers traveling for campaign purposes.

(ii) If the trip is by non-charter commercial transportation, the actual cost shall be calculated in accordance with the formula set forth at 11 CFR 9004.7(b)(2) on the basis of the commercial fare. Such actual cost shall be a qualified campaign expense and a reportable expenditure.

§ 9004.8 Withdrawal by candidate.

(a) Any individual who is not actively conducting campaigns in more than one State for the office of President or Vice President shall cease to be a candidate under 11 CFR 9002.2.

(b) An individual who ceases to be a candidate under this section shall:

(1) No longer be eligible to receive any payments under 11 CFR 9005.2 except to defray qualified campaign expenses as provided in 11 CFR 9004.4.

(2) Submit a statement, within 30 calendar days after he or she ceases to be a candidate, setting forth the information required under 11 CFR 9004.9(c).

§ 9004.9 Net outstanding qualified campaign expenses.

(a) *Candidates receiving post-election funding.* A candidate who is eligible to receive post-election payments under 11 CFR 9004.3 shall file, no later than 20 calendar days after the date of the election, a preliminary statement of that candidate's net outstanding qualified campaign expenses. The candidate's net outstanding qualified campaign expenses under this section equal the difference between 11 CFR 9004.9(a) (1) and (2).

(1) The total of:

(i) All outstanding obligations for qualified campaign expenses as of the date of the election; plus

(ii) An estimate of the amount of qualified campaign expenses that will be incurred by the end of the expenditure report period; plus

(iii) An estimate of necessary winding down costs as defined under 11 CFR 9004.4(a)(4); less

(2) The total of:

(i) Cash on hand as of the close of business on the day of the election, including: All contributions dated on or before that date; currency; balances on deposit in banks, savings and loan institutions, and other depository institutions; traveler's checks; certificates of deposit; treasury bills; and any other committee investments valued at fair market value;

(ii) The fair market value of capital assets and other assets on hand; and

(iii) Amounts owed to the candidate's authorized committee(s) in the form of credits, refunds of deposits, returns, receivables, or rebates of qualified campaign expenses; or a commercially reasonable amount based on the collectibility of those credits, returns, receivables or rebates.

(3) The amount submitted as the total of outstanding campaign obligations under paragraph (a)(1) of this section shall not include any accounts payable for non-qualified campaign expenses nor any amounts determined or anticipated to be required as a repayment under 11 CFR part 9007 or any amounts paid to secure a surety bond under 11 CFR 9007.5(c).

(b) *All candidates.* Each candidate, except for individuals who have withdrawn pursuant to 11 CFR 9004.8, shall submit a statement of net outstanding qualified campaign expenses no later than 30 calendar days after the end of the expenditure report period. The statement shall contain the information required by 11 CFR 9004.9(a) (1) and (2), except that the amount of outstanding obligations under 11 CFR 9004.9(a)(1)(i) and the amount of cash on hand, assets and receivables under 11 CFR 9004.9(a)(2) shall be complete as of the last day of the expenditure report period.

(c) *Candidates who withdraw.* An individual who ceases to be a candidate pursuant to 11 CFR 9004.8 shall file a statement of net outstanding qualified campaign expenses no later than 30 calendar days after he or she ceases to be a candidate. The statement shall contain the information required under 11 CFR 9004.9(a) (1) and (2), except that the amount of outstanding obligations under 11 CFR 9004.9(a)(1)(i) and the amount of cash on hand, assets and receivables under 11 CFR 9004.9(a)(2) shall be complete as of the day on which the individual ceased to be a candidate.

(d) (1) *Capital assets.* For purposes of this section, the term *capital asset* means any property used in the operation of the campaign whose purchase price exceeded $2000 when acquired by the committee. Property that must be valued as capital assets under this section includes, but is not limited to, office equipment, furniture, vehicles and fixtures acquired for use in the operation of the candidate's campaign, but does not include property defined as "other assets" under 11 CFR 9004.9(d)(2). A list of all capital assets shall be maintained by the committee in accordance with 11 CFR 9003.5(d)(1). The fair market value of capital assets may be considered to be the total original cost of such items when acquired less 40%, to account for depreciation, except that items acquired after the date of ineligibility must be valued at their fair market value on the date acquired. If the candidate wishes to claim a higher depreciation percentage for an item, he or she must list that capital asset on the statement separately and demonstrate, through documentation, the fair market value of each such asset.

(2) *Other assets.* The term *other assets* means any property acquired by the committee for use in raising funds or as collateral for campaign loans. "Other assets" must be included on the candidate's statement of net outstanding qualified campaign expenses if the aggregate value of such assets exceeds $5000. The value of "other assets" shall be determined by the fair market value of each item on the last day of the expenditure report period or the day on which the individual ceased to be a candidate, whichever is earlier, unless the item is acquired after these dates, in which case the item shall be valued on the date it is acquired. A list of other assets shall be maintained by the committee in accordance with 11 CFR 9003.5(d)(2).

(e) *Collectibility of accounts receivable.* If the committee determines that an account receivable of $500 or more, including any credit, refund, return or rebate, is not collectible in whole or in part, the committee shall demonstrate through documentation that the determination was commercially reasonable. The documentation shall include records showing the original amount of the account receivable, copies of correspondence and memoranda of communications with the debtor showing attempts to collect the amount due, and an explanation of how the lesser amount or full write-off was determined.

(f) *Review of candidate statement*—(1) *General.* The Commission will review the statement filed by each candidate under this section. The Commission may request further information with respect to statements filed pursuant to 11 CFR 9004.9(b) during the audit of that candidate's authorized committee(s) under 11 CFR part 9007.

(2) *Candidate eligible for post-election funding.* (i) If, in reviewing the preliminary statement of a candidate eligible to receive post-election funding, the Commission receives information indicating that substantial assets of that candidate's authorized committee(s) have been undervalued or not included in the statement or that the amount of outstanding qualified campaign expenses has been otherwise overstated in relation to committee assets, the Commission may decide to temporarily postpone its certification of funds to that candidate pending a final determination of whether the candidate is entitled to all or a portion of the funds for which he or she is eligible based on the percentage of votes the candidate received in the general election.

(ii) *Initial determination.* In making a determination under 11 CFR 9004.9(f)(2)(i), the Commission will notify the candidate within 10 business days after its receipt of the statement of its initial determination that the candidate is not entitled to receive the full amount for which the candidate may be eligible. The notice will give the legal and factual reasons for the initial determination and advise the candidate of the evidence on which the Commission's initial determination is based. The candidate will be given the opportunity to revise the statement or to submit, within 10 business days, written legal or factual materials to demonstrate that the candidate has net outstanding qualified campaign expenses that entitle the candidate to post-election funds. Such materials may be submitted by counsel if the candidate so desires.

(iii) *Final determination.* The Commission will consider any written legal or factual materials submitted by the candidate before making its final determination. A final determination that the candidate is entitled to receive only a portion or no post-election funding will be accompanied by a written statement of reasons for the Commission's action. This statement will explain the legal and factual reasons underlying the Commission's determination and will summarize the results of any investigation on which the determination is based.

(iv) If the candidate demonstrates that the amount of outstanding qualified campaign expenses still exceeds committee assets, the Commission will certify the payment of post-election funds to which the candidate is entitled.

(v) *Petitions for rehearing.* The candidate may file a petition for rehearing of a final determination under this section in accordance with 11 CFR 9007.5(a).

§ 9004.10 Sale of assets acquired for fundraising purposes.

(a) *General.* A minor or new party candidate may sell assets donated to the candidate's authorized committee(s) or otherwise acquired for fundraising purposes subject to the limitations and prohibitions of 11 CFR 9003.2, title 2, United States Code, and 11 CFR parts 110 and 114. This section will only apply to major party candidates to the extent that they sell assets acquired either for fundraising purposes in connection with his or her legal and accounting compliance fund or when it is necessary to make up any deficiency in payments received from the Fund due to the application of 11 CFR 9005.2(b).

(b) *Sale after end of expenditure report period.* A minor or new party candidate, or a major party candidate in the event of a deficiency in the payments received from the Fund due to the application of 11 CFR 9005.2(b), whose outstanding debts exceed the cash on hand after the end of the expenditure report period as determined under 11 CFR 9002.12, may dispose of assets acquired for fundraising purposes in a sale to a wholesaler or other intermediary who will in turn sell such assets to the public provided that the sale to the wholesaler or intermediary is an arms-length transaction. Sales made under this subsection will not be subject to the limitations and prohibitions of title 2, United States Code and 11 CFR parts 110 and 114.

PART 9005—CERTIFICATION BY COMMISSION

Authority: 26 U.S.C. 9005, 9006 and 9009(b).

§ 9005.1 Certification of payments for candidates.

(a) *Certification of payments for major party candidates.* Not later than 10 days after the Commission determines that the Presidential and Vice Presidential candidates of a major party have met all applicable conditions for eligibility tb receive payments under 11 CFR 9003.1 and 9003.2, the Commission shall certify to the Secretary that payment in full of the amounts to which such candidates are entitled under 11 CFR part 9004 should be made pursuant to 11 CFR 9005.2.

(b) *Certification of pre-election payments for minor and new party candidates.* (1) Not later than 10 days after a minor or new party candidate has met all applicable conditions for eligibility to receive payments under 11 CFR 9003.1, 9003.2 and 9004.2, the Commission will make an initial determination of the amount, if any, to which the candidate is entitled. The Commission will base its determination on the percentage of votes received in the official vote count certified in each State. In notifying the candidate, the Commission will give the legal and factual reasons for its determination and advise the candidate of the evidence on which the determination is based.

(2) The candidate may submit, within 15 days after the Commission's initial determination, written legal or factual materials to demonstrate that a redetermination is appropriate. Such materials may be submitted by counsel if the candidate so desires.

(3) The Commission will consider any written legal or factual materials timely submitted by the candidate in making its final determination. A final determination of certification by the Commission will be accompanied by a written statement of reasons for the Commission's action. This statement will explain the reasons underlying the Commission's determination and will summarize the results of any investigation on which the determination is based.

(c) *Certification of minor and new party candidates for post-election payments.* (1) Not later than 30 days after the general election, the Commission will determine whether a minor or new party candidate is eligible for post-election payments.

(2) The Commission's determination of eligibility will be based on the following factors:

(i) The candidate has received at least 5% or more of the total popular vote based on unofficial vote results in each State;

(ii) The candidate has filed a preliminary statement of his or her net outstanding qualified campaign expenses pursuant to 11 CFR 9004.9(a); and

(iii) The candidate has met all applicable conditions for eligibility under 11 CFR 9003.1 and 9003.2.

(3) The Commission will notify the candidate of its initial determination of the amount, if any, to which the candidate is entitled, give the legal and factual reasons for its determination and advise the candidate of the evidence on which the determination is based. The Commission will also notify the candidate that it will deduct a percentage of the amount to which the candidate is entitled based on the unofficial vote results when the Commission certifies an amount for payment to the Secretary. This deduction will be based on the average percentage differential between the unofficial and official vote results for all candidates who received public funds in the preceding Presidential general election.

(4) The candidate may submit within 15 days after the Commission's initial determination written legal or factual materials to demonstrate that a redetermination is appropriate. Such materials may be submitted by counsel if the candidate so desires.

(5) The Commission will consider any written legal or factual materials timely submitted by the candidate in making its final determination. A final determination of certification by the Commission will be accompanied by a written statement of reasons for the Commission's action. This statement will explain the reasons underlying the Commission's determination and will summarize the results of any investigation on which the determination is based.

(d) All certifications made by the Commission pursuant to this section shall be final and conclusive, except to the extent that they are subject to examination and audit by the Commission under 11 CFR part 9007 and judicial review under 26 U.S.C. 9011.

§ 9005.2 Payments to eligible candidates from the Fund.

(a) Upon receipt of a certification from the Commission under 11 CFR 9005.1 for payment to the eligible Presidential and Vice Presidential candidates of a political party, the Secretary shall pay to such candidates out of the Fund the amount certified by the Commission. Amounts paid to a candidate shall be under the control of that candidate.

(b)(1) If at the time of a certification from the Commission under 11 CFR 9005.1, the Secretary determines that the monies in the Fund are not, or may not be, sufficient to satisfy the full entitlements of the eligible candidates of all political parties, he or she shall withhold an amount which is determined to be necessary to assure that the eligible candidates of each political party will receive their pro rata share.

(2) Amounts withheld under 11 CFR 9005.2(b)(1) shall be paid when the Secretary determines that there are sufficient monies in the Fund to pay such amounts, or pro rata portions thereof, to all eligible candidates from whom amounts have been withheld.

(c) Payments received from the Fund by a major party candidate shall be deposited in a separate account maintained by his or her authorized committee, unless there is a deficiency in the Fund as provided under 11 CFR 9005.2(b)(1). In the case of a deficiency, the candidate may establish a separate account for payments from the Fund or may deposit such payments with contributions received pursuant to 11 CFR 9003.3(b). The account(s) shall be maintained at a State bank, federally chartered depository institution or other depository institution, the deposits or accounts of which are insured by the Federal Deposit Insurance Corporation.

(d) No funds other than the payments received from the Treasury, reimbursements, or income generated through use of public funds in accordance with 11 CFR 9004.5, shall be deposited in the account described in 11 CFR 9005.2(c). "Reimbursements" shall include, but are not limited to, refunds of deposits, vendor refunds, reimbursements for travel expenses under 11 CFR 9004.6 and 9004.7 and reimbursements for legal and accounting costs under 11 CFR 9003.3(a)(2)(ii)(B).

PART 9006—REPORTS AND RECORDKEEPING

Authority: 2 U.S.C. 434 and 26 U.S.C. 9009(b).

§ 9006.1 Separate reports.

(a) The authorized committee(s) of a candidate shall report all expenditures to further the candidate's general election campaign in reports separate from reports of any other expenditures made by such committee(s) with respect to other elections. Such reports shall be filed pursuant to the requirements of 11 CFR part 104.

(b) The authorized committee(s) of a candidate shall file separate reports as follows:

(1) One report shall be filed which lists all receipts and disbursements of:

(i) Contributions and loans received by a major party candidate pursuant to 11 CFR part 9003 to make up deficiencies in Fund payments due to the application of 11 CFR part 9005;

(ii) Contributions and loans received pursuant to 11 CFR 9003.2(b)(2) by a minor, or new party for use in the general election;

(iii) Receipts for expenses incurred before the beginning of the expenditure report period pursuant to 11 CFR 9003.4;

(iv) Personal funds expended in accordance with 11 CFR 9003.2(c); and

(v) Payments received from the Fund.

(2) A second report shall be filed which lists all receipts of and disbursements from, contributions received for the candidate's legal and accounting compliance fund in accordance with 11 CFR 9003.3(a).

§ 9006.2 Filing dates.

The reports required to be filed under 11 CFR 9006.1 shall be filed during an election year on a monthly or quarterly basis as prescribed at 11 CFR 104.5(b)(1). During a non-election year, the candidate's principal campaign committee may elect to file reports either on a monthly or quarterly basis in accordance with 11 CFR 104.5(b)(2).

PART 9007—EXAMINATIONS AND AUDITS; REPAYMENTS

Authority: 26 U.S.C. 9007 and 9009(b).

§ 9007.1 Audits.

(a) *General.* (1) After each Presidential election, the Commission will conduct a thorough examination and audit of the receipts, disbursements, debts and obligations of each candidate, his or her authorized committee(s), and agents of such candidates or committees. Such examination and audit will include, but will not be limited to, expenditures pursuant to 11 CFR 9003.4 prior to the beginning of the expenditure report period, contributions to and expenditures made from the legal and accounting compliance fund established under 11 CFR 9003.3(a), contributions received to supplement any payments received from the Fund, and qualified campaign expenses.

(2) In addition, the Commission may conduct other examinations and audits from time to time as it deems necessary to carry out the provisions of this subchapter.

(3) Information obtained pursuant to any audit and examination conducted under 11 CFR 9007.1(a) (1) and (2) may be used by the Commission as the basis, or partial basis, for its repayment determinations under 11 CFR 9007.2.

(b) *Conduct of fieldwork.* (1) If the candidate or the candidate's authorized committee does not maintain or use any computerized information containing the data listed in 11 CFR 9003.6, the Commission will give the candidate's authorized committee at least two weeks, notice of the Commission's intention to commence fieldwork on the audit and examination. The fieldwork shall be conducted at a site provided by the committee. If the candidate or the candidate's authorized committee maintains or uses computerized information containing any of the data listed in 11 CFR 9003.6, the Commission generally will request such information prior to commencement of audit fieldwork. Such request will be made in writing. The committee shall produce the computerized information no later than 15 calendar days after service of such request. Upon receipt of the computerized information requested and compliance with the technical specifications of 11 CFR 9003.6(b), the Commission will give the candidate's authorized committee at least two weeks, notice of the Commission's intention to commence fieldwork on the audit and examination. The fieldwork shall be conducted at a site provided by the committee. During or after audit fieldwork, the Commission may request additional or updated computerized information which expands the coverage dates of computerized information previously provided, and which may be used for purposes including, but not limited to, updating a statement of net outstanding qualified campaign expenses. During or after audit fieldwork, the Commission may also request additional computerized information which was created by or becomes available to the committee that is of assistance in the Commission's audit. The committee shall produce the additional or updated computerized information no later than 15 calendar days after service of the Commission's request.

(i) *Office space and records.* On the date scheduled for the commencement of fieldwork, the candidate or his or her authorized committee(s) shall provide Commission staff with office space and committee records in accordance with the candidate and committee agreement under 11 CFR 9003.1(b)(6).

(ii) *Availability of committee personnel.* On the date scheduled for the commencement of fieldwork, the candidate or his or her authorized committee(s) shall have committee personnel present at the site of the fieldwork. Such personnel shall be familiar with the committee's records and operation and shall be available to Commission staff to answer questions and to aid in locating records.

(iii) *Failure to provide staff, records or office space.* If the candidate or his or her authorized committee(s) fail to provide adequate office space, personnel or committee records, the Commission may seek judicial intervention under 2 U.S.C. 437d or 26 U.S.C. 9010(c) to enforce the candidate and committee agreement made under 11 CFR 9003.1(b). Before seeking judicial intervention, the Commission will notify the candidate of his or her failure to comply with the agreement and will recommend corrective action to bring the candidate into compliance. Upon receipt of the Commission's notification, the candidate will have ten (10) calendar days in which to take the corrective action indicated or to otherwise demonstrate to the Commission in writing that he or she is complying with the candidate and committee agreements.

(iv) If, in the course of the audit process, a dispute arises over the documentation sought or other requirements of the candidate agreement, the candidate may seek review by the Commission of the issues raised. To seek review, the candidate shall submit a written statement within 10 days after the disputed Commission staff request is made, describing the dispute and indicating the candidate's proposed alternative(s).

(v) If the candidate or his or her authorized committee fails to produce particular records, materials, evidence or other information requested by the Commission, the Commission may issue an order pursuant to 2 U.S.C. 437d(a)(1) or a subpoena or subpoena duces tecum pursuant to 2 U.S.C. 437d(a)(3). The procedures set forth in 11 CFR 111.11 through 111.15, as appropriate, shall apply to the production of such records, materials, evidence or other information as specified in the order, subpoena or subpoena duces tecum.

(2) Fieldwork will include the following steps designed to keep the candidate and committee informed as to the progress of the audit and to expedite the process:

(i) *Entrance conference.* At the outset of the fieldwork, Commission staff will hold an entrance conference, at which the candidate's representatives will be advised of the purpose of the audit and the general procedures to be followed. Future requirements of the candidate and his or her authorized committee, such as possible repayments to the United States Treasury, will also be discussed. Committee representatives shall provide information and records necessary to conduct the audit, and Commission staff will be available to answer committee questions.

(ii) *Review of records.* During the fieldwork, Commission staff will review committee records and may conduct interviews of committee personnel. Commission staff will be available to explain aspects of the audit and examination as it progresses. Additional meetings between Commission staff and committee personnel may be held from time to time during the fieldwork to discuss possible audit findings and to resolve issues arising during the course of the audit.

(iii) *Exit conference.* At the conclusion of the fieldwork, Commission staff will hold an exit conference to discuss with committee representatives the staff's preliminary findings and recommendations which the Commission staff anticipates that it may present to the Commission for approval. Commission staff will advise committee representatives at this conference of the projected timetable regarding the issuance of an audit report, the committee's opportunity to respond thereto, and the Commission's initial and final repayment determinations under 11 CFR 9007.2.

(3) Commission staff may conduct additional fieldwork after the completion of the fieldwork conducted pursuant to 11 CFR 9007.1(b) (1) and (2). Factors that may necessitate such follow-up fieldwork include, but are not limited to, the following:

(i) Committee response to audit findings;

(ii) Financial activity of the committee subsequent to the fieldwork conducted pursuant to 11 CFR 9007.1(b)(1);

(iii) Committee responses to Commission repayment determinations made under 11 CFR 9007.2.

(4) The Commission will notify the candidate and his or her authorized committee if follow-up fieldwork is necessary. The provisions of 11 CFR 9007.1(b) (1) and (2) will apply to any additional fieldwork conducted.

(c) *Preparation of interim audit report.* (1) After the completion of the fieldwork conducted pursuant to 11 CFR 9007.1(b)(1), the Commission will issue an interim audit report to the candidate and his or her authorized committee. The interim audit report may contain Commission findings and recommendations regarding one or more of the following areas:

(i) An evaluation of procedures and systems employed by the candidate and committee to comply with applicable provisions of the Federal Election Campaign Act, Presidential Election Campaign Fund Act and Commission regulations;

(ii) Accuracy of statements and reports filed with the Commission by the candidate and committee;

(iii) Compliance of the candidate and committee with applicable statutory and regulatory provisions in those instances where the Commission has not instituted any enforcement action on the matter(s) under the provisions of 2 U.S.C. 437g and 11 CFR part 111; and

(iv) Preliminary calculations regarding future repayments to the United States Treasury.

(2) The candidate and his or her authorized committee will have an opportunity to submit in writing within 30 calendar days of service of the interim report, legal and factual materials disputing or commenting on the contents of the interim report. Such materials may be submitted by counsel if the candidate so desires.

(3) The Commission will consider any written legal and factual materials submitted by the candidate or his or her authorized committee in accordance with 11 CFR 9007.1(c)(2) before approving and issuing an audit report to be released to the public. The contents of the publicly released audit report may differ from that of the interim report since the Commission will consider timely submissions of legal and factual materials by the candidate or committee in response to the interim report.

(d) *Preparation of publicly released audit report.* An audit report prepared subsequent to an interim report will be publicly released pursuant to 11 CFR 9007.1(e). This report will contain Commission findings and recommendations addressed in the interim audit report but may contain adjustments based on the candidate's response to the interim report. In addition, this report will contain an initial repayment determination made by the Commission pursuant to 11 CFR 9007.2(c)(1) in lieu of the preliminary calculations set forth in the interim report.

(e) *Public release of audit report.* (1) After the candidate and committee have had an opportunity to respond to a written interim report of the Commission, the Commission will make public the audit report prepared subsequent to the interim report, as provided in 11 CFR 9007.1(d).

(2) If the Commission determines, on the basis of information obtained under the audit and examination process, that certain matters warrant enforcement under 2 U.S.C. 437g and 11 CFR part 111, those matters will not be contained in the publicly released report. In such cases, the audit report will indicate that certain other matters have been referred to the Commission's Office of General Counsel.

(3) The Commission will provide the candidate and the committee with copies of the agenda document containing those portions of the final audit report to be considered in open session 24 hours prior to releasing the agenda document to the public. The Commission will also provide the candidate and committee with copies of the final audit report 24 hours before releasing the report to the public.

(4) Addenda to the audit report may be issued from time to time as circumstances warrant and as additional information becomes available. Such addenda may be based in part on follow-up fieldwork conducted under 11 CFR 9007.1(b)(3) and will be placed on the public record.

§ 9007.2 Repayments.

(a) *General.* (1) A candidate who has received payments from the Fund under

11 CFR part 9005 shall pay the United States Treasury any amounts which the Commission determines to be repayable under this section. In making repayment determinations under this section, the Commission may utilize information obtained from audits and examinations conducted pursuant to 11 CFR 9007.1 or otherwise obtained by the Commission in carrying out its responsibilities under this subchapter.

(2) The Commission will notify the candidate of any repayment determinations made under this section as soon as possible, but not later than 3 years after the close of the expenditure report period. The Commission's issuance of an interim audit report to the candidate under 11 CFR 9007.1(c) will constitute notification for purposes of the 3-year period.

(3) Once the candidate receives notice of the Commission's final repayment determination under this section, the candidate should give preference to the repayment over all other outstanding obligations of his or her committee, except for any federal taxes owed by the committee.

(b) *Bases for repayment.* The Commission may determine that an eligible candidate of a political party who has received payments from the Fund must repay the United States Treasury under any of the circumstances described below.

(1) *Payments in excess of candidate's entitlement.* If the Commission determines that any portion of the payments made to the candidate was in excess of the aggregate payments to which such candidate was entitled, it will so notify the candidate, and such candidate shall pay to the United States Treasury an amount equal to such portion.

(2) *Use of funds for non-qualified campaign expenses.* (i) If the Commission determines that any amount of any payment to an eligible candidate from the Fund was used for purposes other than those described in paragraphs (b)(2)(i) (A) through (C) of this section, it will notify the candidate of the amount so used, and such candidate shall pay to the United States Treasury an amount equal to such amount.

(A) To defray qualified campaign expenses;

(B) To repay loans, the proceeds of which were used to defray qualified campaign expenses; and

(C) To restore funds (other than contributions which were received and expended by minor or new party candidates to defray qualified campaign expenses) which were used to defray qualified campaign expenses.

(ii) Examples of Commission repayment determinations under 11 CFR 9007.2(b)(2) include, but are not limited to the following:

(A) Determinations that a candidate, a candidate's authorized committee(s) or agent(s) have incurred expenses in excess of the aggregate payments to which an eligible major party candidate is entitled;

(B) Determinations that amounts spent by a candidate, a candidate's authorized committee(s) or agent(s) from the Fund were not documented in accordance with 11 CFR 9003.5;

(C) Determinations that any portion of the payments made to a candidate from the Fund was expended in violation of State or Federal law; and

(D) Determinations that any portion of the payments made to a candidate from the Fund was used to defray expenses resulting from a violation of State or Federal law, such as the payment of fines or penalties.

(iii) In the case of a candidate who has received contributions pursuant to 11 CFR 9003.3 (b) or (c), the amount of any repayment sought under this section shall bear the same ratio to the total amount determined to have been used for non-qualified campaign expenses as the amount of payments certified to the candidate from the Fund bears to the total deposits, as of December 31 of the Presidential election year. For purposes of this section, total deposits means all deposits to all candidate accounts minus transfers between accounts, refunds, rebates, reimbursements, checks returned for insufficient funds, proceeds of loans and other similar amounts.

(3) *Surplus.* If the Commission determines that a portion of payments from the Fund remains unspent after all qualified campaign expenses have been paid, it shall so notify the candidate, and such candidate shall pay the United States Treasury that portion of surplus funds.

(4) *Income on investment of payments from the Fund.* If the Commission determines that a candidate received any income as a result of 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.

(5) *Unlawful acceptance of contributions by an eligible candidate of a major party.* 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.

(c) *Repayment determination procedures.* The Commission repayment determination will be made in accordance with the procedures set forth at 11 CFR 9007.2 (c)(1) through (c)(4).

(1) *Initial determination.* The Commission will provide the candidate with a written notice of its initial repayment determination(s). This notice will be included in the Commission's publicly-released audit report pursuant to 11 CFR 9007.1(d) and will set forth the legal and factual reasons for such determination(s). Such notice will also advise the candidate of the evidence upon which any such determination is based. If the candidate does not dispute an initial repayment determination of the Commission within 30 calendar days after service of the notice, such initial determination will be considered a final determination of the Commission.

(2) *Submission of written materials.* If the candidate disputes the Commission's initial repayment determination(s), he or she shall have an opportunity to submit in writing, within 30 calendar days after service of the Commission's notice, legal and factual materials to demonstrate that no repayment, or a lesser repayment, is required. The Commission will consider any written legal and factual materials submitted by the candidate within this 30 day period in making its final repayment determination(s). Such materials may be submitted by counsel if the candidate so desires.

(3) *Oral presentation.* A candidate who has submitted written materials under 11 CFR 9007.2(c)(2) may request that the Commission provide such candidate with an opportunity to address the Commission in open session. If the Commission decides by an affirmative vote of four (4) of its members to grant the candidate's request, it will inform the candidate of the date and time set for the oral presentation. At the date and time set by the Commission, the candidate or candidate's designated representative will be allotted an amount of time in which to make an oral presentation to the Commission based upon the legal and factual materials submitted under 11 CFR 9007.2(c)(2). The candidate or

representative will also have the opportunity to answer any questions from individual members of the Commission.

(4) *Final determination.* In making its final repayment determination(s), the Commission will consider any submission made under 11 CFR 9007.2(c)(2) and any oral presentation made under 11 CFR 9007.2(c)(3). A final determination that a candidate must repay a certain amount will be accompanied by a written statement of reasons for the Commission's actions. This statement will explain the reasons underlying the Commission's determination and will summarize the results of any investigation upon which the determination is based.

(d) *Repayment period.* (1) Within 90 calendar days of service of the notice of the Commission's initial repayment determination(s), the candidate shall repay to the United States Treasury amounts which the Commission has determined to be repayable. Upon application by the candidate, the Commission may grant an extension of up to 90 calendar days in which to make repayment.

(2) If the candidate submits written materials under 11 CFR 9007.2(c)(2) disputing the Commission's initial repayment determination(s), the time for repayment will be suspended until the Commission makes its final repayment determination(s). Within 30 calendar days after service of the notice of the Commission's final repayment determination(s), the candidate shall repay to the United States Treasury amounts which the Commission has determined to be repayable. Upon application by the candidate, the Commission may grant an extension of up to 90 calendar days in which to make repayment.

(e) *Computation of time.* The time periods established by this section shall be computed in accordance with 11 CFR 111.2.

(f) *Additional repayments.* Nothing in this section will prevent the Commission from making additional repayment determinations on one or more of the bases set forth at 11 CFR 9007.2(b) after it has made a final determination on any such basis. The Commission may make additional repayment determinations where there exist facts not used as the basis for a previous final determination. Any such additional repayment determination will be made in accordance with the provisions of this section.

(g) *Newly-discovered assets.* If, after any initial or final repayment determination made under this section, a candidate or his or her authorized committee(s) receives or becomes aware of assets not previously included in any statement of net outstanding qualified campaign expenses submitted pursuant to 11 CFR 9004.9, the candidate or his or her authorized committee(s) shall promptly notify the Commission of such newly-discovered assets. Newly-discovered assets may include refunds, rebates, late-arriving receivables, and actual receipts for capital assets in excess of the value specified in any previously-submitted statement of net outstanding qualified campaign expenses. Newly-discovered assets may serve as a basis for additional repayment determinations under 11 CFR 9007.2(f).

(h) *Limit on repayment.* No repayment shall be required from the eligible candidates of a political party under 11 CFR 9007.2 to the extent that such repayment, when added to other repayments required from such candidates under 11 CFR 9007.2, exceeds the amount of payments received by such candidates under 11 CFR 9005.2.

(i) *Petitions for rehearing; stays pending appeal.* The candidate may file a petition for rehearing of a final repayment determination in accordance with 11 CFR 9007.5(a). The candidate may request a stay of a final repayment determination in accordance with 11 CFR 9007.5(c) pending the candidate's appeal of that repayment determination.

§ 9007.3 Extensions of time.

(a) It is the policy of the Commission that extensions of time under 11 CFR part 9007 will not be routinely granted.

(b) Whenever a candidate has a right or is required to take action within a period of time prescribed by 11 CFR part 9007 or by notice given thereunder, the candidate may apply in writing to the Commission for an extension of time in which to exercise such right or take such action. The candidate shall demonstrate in the application for extension that good cause exists for his or her request.

(c) An application for extension of time shall be made at least 7 calendar days prior to the expiration of the time period for which the extension is sought. The Commission may, upon a showing of good cause, grant an extension of time to a candidate who has applied for such extension in a timely manner. The length of time of any extension granted hereunder shall be decided by the Commission and may be less than the amount of time sought by the candidate in his or her application.

(d) If a candidate fails to seek an extension of time, exercise a right or take a required action prior to the expiration of a time period prescribed by 11 CFR part 9007, the Commission may, on the candidate's showing of excusable neglect:

(1) Permit such candidate to exercise his or her right(s), or take such required action(s) after the expiration of the prescribed time period; and

(2) Take into consideration any information obtained in connection with the exercise of any such right or taking of any such action before making decisions or determinations under 11 CFR part 9007.

§ 9007.4 Additional audits.

In accordance with 11 CFR 104.16(c), the Commission, pursuant to 11 CFR 111.10, may upon affirmative vote of four members conduct an audit and field investigation of any committee in any case in which the Commission finds reason to believe that a violation of a statute or regulation over which the Commission has jurisdiction has occurred or is about to occur.

§ 9007.5 Petitions for rehearing; stays of repayment determinations.

(a) *Petitions for rehearing.* (1) Following the Commission's final repayment determination or a final determination that a candidate is not entitled to all or a portion of post election funding under 11 CFR 9004.9(f), the candidate may file a petition for rehearing setting forth the relief desired and the legal and factual basis in support. To be considered by the Commission, petitions for rehearing must:

(i) Be filed within 20 calendar days following service of the Commission's final determination;

(ii) Raise new questions of law or fact that would materially alter the Commission's final determination; and

(iii) Set forth clear and convincing grounds why such questions were not and could not have been presented during the earlier determination process.

(2) If a candidate files a timely petition under this section challenging a Commission final repayment determination, the time for repayment will be suspended until the Commission serves notice on the candidate of its determination on the petition. The time periods for making repayment under 11 CFR 9007.2(d)(2) shall apply to any amounts determined to be repayable following the Commission's consideration of a petition for rehearing under this section.

(b) *Effect of failure to raise issues.* The candidate's failure to raise an argument in a timely fashion during the initial determination process or in a petition for rehearing under this section, as appropriate, shall be deemed a waiver of the candidate's right to present such arguments in any future stage of proceedings including any petition for review filed under 26 U.S.C. 9011(a). An issue is not timely raised in a petition for rehearing if it could have been raised earlier in response to the Commission's initial determination.

(c) *Stay of repayment determination pending appeal.* (1)(i) The candidate may apply to the Commission for a stay of all or a portion of the amount determined to be repayable under this section or under 11 CFR 9007.2 pending the candidate's appeal of that repayment determination pursuant to 26 U.S.C. 9011(a). The repayment amount requested to be stayed shall not exceed the amount at issue on appeal.

(ii) A request for a stay shall be made in writing and shall be filed within 30 calendar days after service of the Commission's decision on a petition for rehearing under paragraph (a) of this section or, if no petition for rehearing is filed, within 30 calendar days after service of the Commission's final repayment determination under 11 CFR 9007.2(c)(4).

(2) The Commission's approval of a stay request will be conditioned upon the candidate's presentation of evidence in the stay request that he or she:

(i) Has placed the entire amount at issue in a separate interest-bearing account pending the outcome of the appeal and that withdrawals from the account may only be made with the joint signatures of the candidate or his or her agent and a Commission representative; or

(ii) Has posted a surety bond guaranteeing payment of the entire amount at issue plus interest; or

(iii) Has met the following criteria:

(A) He or she will suffer irreparable injury in the absence of a stay; and, if so, that

(B) He or she has made a strong showing of the likelihood of success on the merits of the judicial action.

(C) Such relief is consistent with the public interest; and

(D) No other party interested in the proceedings would be substantially harmed by the stay.

(3) In determining whether the candidate has made a strong showing of the likelihood of success on the merits under paragraph (c)(2)(iii)(B) of this section, the Commission may consider whether the issue on appeal presents a novel or admittedly difficult legal question and whether the equities of the case suggest that the status quo should be maintained.

(4) All stays shall require the payment of interest on the amount at issue. The amount of interest due shall be calculated from the date 30 days after service of the Commission's final repayment determination under 11 CFR 9007.2(c)(4) and shall be the greater of:

(i) An amount calculated in accordance with 28 U.S.C. 1961 (a) and (b); or

(ii) The amount actually earned on the funds set aside under this section.

§ 9007.6 Stale-dated committee checks.

If the committee has checks outstanding to creditors or contributors that have not been cashed, the committee shall notify the Commission. The committee shall inform the Commission of its efforts to locate the payees, if such efforts have been necessary, and its efforts to encourage the payees to cash the outstanding checks. The committee shall also submit a check for the total amount of such outstanding checks, payable to the United States Treasury.

14. 11 CFR part 9012 is revised to read as follows:

PART 9012—UNAUTHORIZED EXPENDITURES AND CONTRIBUTIONS

Sec.

Authority: 26 U.S.C. 9012. 12.

§ 9012.1 Excessive expenses.

(a) It shall be unlawful for an eligible candidate of a political party for President and Vice President in a Presidential election or the candidate's authorized committee(s) knowingly and willfully to incur qualified campaign expenses in excess of the aggregate payments to which the eligible candidates of a major party are entitled under 11 CFR part 9004 with respect to such election.

(b) It shall be unlawful for the national committee of a major or minor party knowingly and willfully to incur expenses with respect to a presidential nominating convention in excess of the expenditure limitation applicable with respect to such committee under 11 CFR part 9008, unless the incurring of such expenses is authorized by the Commission under 11 CFR 9008.7(a)(3).

§ 9012.2 Unauthorized acceptance of contributions.

(a) It shall be unlawful for an eligible candidate of a major party in a Presidential election or any of his or her authorized committees knowingly and willfully to accept any contribution to defray qualified campaign expenses, except to the extent necessary to make up any deficiency in payments received from the Fund due to the application of 11 CFR 9005.2(b), or to defray expenses which would be qualified campaign expenses but for 11 CFR 9002.11(a)(3).

(b) It shall be unlawful for an eligible candidate of a political party (other than a major party) in a Presidential election or any of his or her authorized committees knowingly and willfully to accept and expend or retain contributions to defray qualified campaign expenses in an amount which exceeds the qualified campaign expenses incurred in that election by that eligible candidate or his or her authorized committee(s).

§ 9012.3 Unlawful use of payments received from the Fund.

(a) It shall be unlawful for any person who receives any payment under 11 CFR part 9005, or to whom any portion of any payment so received is transferred, knowingly and willfully to use, or authorize the use of, such payment or any portion thereof for any purpose other than—

(1) To defray the qualified campaign expenses with respect to which such payment was made; or

(2) To repay loans the proceeds of which were used, or otherwise to restore funds (other than contributions to defray qualified campaign expenses which were received and expended) which were used, to defray such qualified campaign expenses.

(b) It shall be unlawful for the national committee of a major or minor party which receives any payment under 11 CFR part 9008 to use, or authorize the use of, such payment for any purpose other than a purpose authorized by 11 CFR 9008.6.

§ 9012.4 Unlawful misrepresentations and falsification of statements, records or other evidence to the Commission; refusal to furnish books and records.

It shall be unlawful for any person knowingly and willfully—

(a) To furnish any false, fictitious, or fraudulent evidence, books or information to the Commission under 11 CFR parts 9001-9008, or to include in any evidence, books or information so furnished any misrepresentation of a material fact, or to falsify or conceal any evidence, books or information relevant to a certification by the Commission or any examination and audit by the Commission under 11 CFR parts 9001 *et seq.*; or

(b) To fail to furnish to the Commission any records, books or information requested by the Commission for purposes of 11 CFR parts 9001 *et seq.*

§ 9012.5 Kickbacks and illegal payments.

(a) It shall be unlawful for any person knowingly and willfully to give or accept any kickback or any illegal payment in connection with any qualified campaign expenses of any eligible candidate or his or her authorized committee(s).

(b) It shall be unlawful for the national committee of a major or minor party knowingly and willfully to give or accept any kickback or any illegal payment in connection with any expense incurred by such committee with respect to a Presidential nominating convention.

15. 11 CFR parts 9031 through 9039 is revised to read as follows:

PART 9031—SCOPE

Sec.
9031.1 Scope.

Authority: 26 U.S.C. 9031 and 9039(b).

§ 9031.1 Scope.

This subchapter governs entitlement to and use of funds certified from the Presidential Primary Matching Payment Account under 26 U.S.C. 9031 *et seq.* The definitions, restrictions, liabilities and obligations imposed by this subchapter are in addition to those imposed by sections 431–455 of title 2, United States Code, and regulations prescribed thereunder (11 CFR part 100 through 116). Unless expressly stated to the contrary, this subchapter does not alter the effect of any definitions, restrictions, obligations and liabilities imposed by sections 431–455 of title 2, United States Code, or regulations prescribed thereunder (11 CFR parts 100 through 116).

PART 9032—DEFINITIONS

Sec.
9032.1 Authorized committee.
9032.2 Candidate.
9032.3 Commission.
9032.4 Contribution.
9032.5 Matching payment account.
9032.6 Matching payment period.
9032.7 Primary election.
9032.8 Political committee.
9032.9 Qualified campaign expenses.
9032.10 Secretary.
9032.11 State.

Authority: 26 U.S.C. 9032 and 9039(b).

§ 9032.1 Authorized committee.

(a) Notwithstanding the definition at 11 CFR 100.5, *authorized committee* means with respect to candidates (as defined at 11 CFR 9032.2) seeking the nomination of a political party for the office of President, any political committee that is authorized by a candidate to solicit or receive contributions or to incur expenditures on behalf of the candidate. The term *authorized committee* includes the candidate's principal campaign committee designated in accordance with 11 CFR 102.12, any political committee authorized in writing by the candidate in accordance with 11 CFR 102.13, and any political committee not disavowed by the candidate in writing pursuant to 11 CFR 100.3(a)(3).

(b) Any withdrawal of an authorization shall be in writing and shall be addressed and filed in the same manner provided for at 11 CFR 102.12 or 102.13.

(c) For the purposes of this subchapter, references to the "candidate" and his or her responsibilities under this subchapter shall also be deemed to refer to the candidate's authorized committee(s).

(d) An expenditure by an authorized committee on behalf of the candidate who authorized the committee cannot qualify as an independent expenditure.

(e) A delegate committee, as defined in 11 CFR 100.5(e)(5), is not an authorized committee of a candidate unless it also meets the requirements of 11 CFR 9032.1(a). Expenditures by delegate committees on behalf of a candidate may count against that candidate's expenditure limitation under the circumstances set forth in 11 CFR 110.14.

§ 9032.2 Candidate.

Candidate means an individual who seeks nomination for election to the office of President of the United States. An individual is considered to seek nomination for election if he or she—

(a) Takes the action necessary under the law of a State to qualify for a caucus, convention, primary election or run-off election;

(b) Receives contributions or incurs qualified campaign expenses;

(c) Gives consent to any other person to receive contributions or to incur qualified campaign expenses on his or her behalf; or

(d) Receives written notification from the Commission that any other person is receiving contributions or making expenditures on the individual's behalf and fails to disavow that activity by letter to the Commission within 30 calendar days after receipt of notification.

§ 9032.3 Commission.

Commission means the Federal Election Commission, 999 E Street NW., Washington, DC 20463.

§ 9032.4 Contribution.

For purposes of this subchapter, *contribution* has the same meaning given the term under 2 U.S.C. 431(8)(A) and 11 CFR 100.7, except as provided at 11 CFR 9034.4(b)(4).

§ 9032.5 Matching payment account.

Matching payment account means the Presidential Primary Matching Payment Account established by the Secretary of the Treasury under 26 U.S.C. 9037(a).

§ 9032.6 Matching payment period.

Matching payment period means the period beginning January 1 of the calendar year in which a Presidential general election is held and may not exceed one of the following dates:

(a) For a candidate seeking the nomination of a party which nominates its Presidential candidate at a national convention, the date on which the party nominates its candidate.

(b) For a candidate seeking the nomination of a party which does not make its nomination at a national convention, the earlier of—

(1) The date the party nominates its Presidential candidate, or

(2) The last day of the last national convention held by a major party in the calendar year.

§ 9032.7 Primary election.

(a) *Primary election* means an election held by a State or a political party, including a run-off election, or a nominating convention or a caucus—

(1) For the selection of delegates to a national nominating convention of a political party;

(2) For the expression of a preference for the nomination of Presidential candidates;

(3) For the purposes stated in both paragraphs (a) (1) and (2) of this section; or

(4) To nominate a Presidential candidate.

(b) If separate primary elections are held in a State by the State and a political party, the primary election for the purposes of this subchapter will be the election held by the political party.

§ 9032.8 Political committee.

Political committee means any committee, club, association, organization or other group of persons (whether or not incorporated) which accepts contributions or incurs qualified campaign expenses for the purpose of influencing, or attempting to influence, the nomination of any individual for election to the office of President of the United States.

§ 9032.9 Qualified campaign expense.

(a) *Qualified campaign expense* means a purchase, payment, distribution, loan, advance, deposit, or gift of money or anything of value—

(1) Incurred by or on behalf of a candidate or his or her authorized committees from the date the individual becomes a candidate through the last day of the candidate's eligibility as determined under 11 CFR 9033.5;

(2) Made in connection with his or her campaign for nomination; and

(3) Neither the incurrence nor payment of which constitutes a violation of any law of the United States or of any law of any State in which the expense is incurred or paid, or of any regulation prescribed under such law of the United States or of any State, except that any State law which has been preempted by the Federal Election Campaign Act of 1971, as amended, will not be considered a State law for purposes of this subchapter.

(b) An expenditure is made on behalf of a candidate, including a Vice Presidential candidate, if it is made by—

(1) An authorized committee or any other agent of the candidate for purposes of making an expenditure;

(2) Any person authorized or requested by the candidate, an authorized committee of the candidate, or an agent of the candidate to make the expenditure; or

(3) A committee which has been requested by the candidate, by an authorized committee of the candidate, or by an agent of the candidate to make the expenditure, even though such committee is not authorized in writing.

(c) Expenditures incurred either before the date an individual becomes a candidate or after the last day of a candidate's eligibility will be considered qualified campaign expenses if they meet the provisions of 11 CFR 9034.4(a). Expenditures described under 11 CFR 9034.4(b) will not be considered qualified campaign expenses.

§ 9032.10 Secretary.

For purposes of this subchapter, *Secretary* means the Secretary of the Treasury.

§ 9032.11 State.

State means each State of the United States, Puerto Rico, the Canal Zone, the Virgin Islands, the District of Columbia, and Guam.

PART 9033—ELIGIBILITY FOR PAYMENTS

Authority: 26 U.S.C. 9033 and 9039(b)

§ 9033.1 Candidate and committee agreements.

(a) *General.* (1) A candidate seeking to become eligible to receive Presidential primary matching fund payments shall agree in a letter signed by the candidate to the Commission that the candidate and the candidate's authorized committee(s) will comply with the conditions set forth in 11 CFR 9033.1(b). The candidate may submit the letter containing the agreements required by this section at any time after January 1 of the year immediately preceding the Presidential election year.

(2) The Commission will not consider a candidate's threshold submission until the candidate has submitted a candidate agreement that meets the requirements of this section.

(b) *Conditions.* The candidate shall agree that:

(1) The candidate has the burden of proving that disbursements by the candidate or any authorized committee(s) or agents thereof are qualified campaign expenses as defined at 11 CFR 9032.9.

(2) The candidate and the candidate's authorized committee(s) will comply with the documentation requirements set forth in 11 CFR 9033.11.

(3) The candidate and the candidate's authorized committee(s) will provide an explanation, in addition to complying with the documentation requirements, of the connection between any disbursements made by the candidate or authorized committee(s) of the candidate and the campaign if requested by the Commission.

(4) The candidate and the candidate's authorized committee(s) will keep and furnish to the Commission all documentation for matching fund submissions, any books, records (including bank records for all accounts), and supporting documentation and other information that the Commission may request.

(5) The candidate and the candidate's authorized committee(s) will keep and furnish to the Commission all documentation relating to disbursements and receipts including any books, records (including bank records for all accounts), all documentation required by this section including those required to be maintained under 11 CFR 9033.11, and other information that the Commission may request. If the candidate or the candidate's authorized committee maintains or uses computerized information containing any of the categories of data listed in 11 CFR 9033.12(a), the committee will provide computerized magnetic media such as magnetic tapes or magnetic diskettes, containing the computerized information at the times specified in 11 CFR 9038.1(b)(1) that meet the requirements of 11 CFR 9033.12(b). Upon request, documentation explaining the computer system's software capabilities shall be provided, and such personnel as are necessary to explain the operation of the computer system's software and the computerized information prepared or maintained by the committee shall also be made available.

(6) The candidate and the candidate's authorized committee(s) will obtain and furnish to the Commission upon request all documentation relating to funds received and disbursements made on the candidate's behalf by other political committees and organizations associated with the candidate.

(7) The candidate and the candidate's authorized committee(s) will permit an audit and examination pursuant to 11 CFR part 9038 of all receipts and disbursements including those made by the candidate, all authorized committee(s) and any agent or person authorized to make expenditures on behalf of the candidate or committee(s). The candidate and authorized committee(s) shall facilitate the audit by making available in one central location, office space, records and such personnel as are necessary to conduct the audit and examination, and shall pay any amounts required to be repaid under 11 CFR parts 9038 and 9039.

(8) The candidate and the candidate's authorized committee(s) will submit the name and mailing address of the person who is entitled to receive matching fund payments on behalf of the candidate and the name and address of the campaign depository designated by the candidate as required by 11 CFR part 103 and 11 CFR 9037.3. Changes in the

information required by this paragraph shall not be effective until submitted to the Commission in a letter signed by the candidate or the Committee treasurer.

(9) The candidate and the candidate's authorized committee(s) will prepare matching fund submissions in accordance with the Federal Election Commission's Guideline for Presentation in Good Order.

(10) The candidate and the candidate's authorized committee(s) will comply with the applicable requirements of 2 U.S.C. 431 *et seq.*; 26 U.S.C. 9031 *et seq.* and the Commission's regulations at 11 CFR parts 100–116, and 9031–9039.

(11) The candidate and the candidate's authorized committee(s) will pay any civil penalties included in a conciliation agreement imposed under 2 U.S.C. 437g against the candidate, any authorized committee of the candidate or any agent thereof.

§ 9033.2 Candidate and committee certifications; threshold submission.

(a) *General.* (1) A candidate seeking to become eligible to receive Presidential primary matching fund payments shall make the certifications set forth in 11 CFR 9033.2(b) to the Commission in a written statement signed by the candidate. The candidate may submit the letter containing the required certifications at any time after January 1 of the year immediately preceding the Presidential election year.

(2) The Commission will not consider a candidate's threshold submission until the candidate has submitted candidate certifications that meet the requirements of this section.

(b) *Certifications.* (1) The candidate shall certify that he or she is seeking nomination by a political party to the Office of President in more than one State. For purposes of this section, in order for a candidate to be deemed to be seeking nomination by a political party to the office of President, the party whose nomination the candidate seeks must have a procedure for holding a primary election, as defined in 11 CFR 9032.7, for nomination to that office. For purposes of this section, the term "political party" means an association, committee or organization which nominates an individual for election to the office of President. The fact that an association, committee or organization qualifies as a political party under this section does not affect the party's status as a national political party for purposes of 2 U.S.C. 441a(a)(1)(B) and 441a(a)(2)(B).

(2) The candidate and the candidate's authorized committee(s) shall certify that they have not incurred and will not incur expenditures in connection with the candidate's campaign for nomination, which expenditures are in excess of the limitations under 11 CFR part 9035.

(3) The candidate and the candidate's authorized committee(s) shall certify:

(i) That they have received matchable contributions totaling more than $5,000 in each of at least 20 States; and

(ii) That the matchable contributions are from individuals who are residents of the State for which their contributions are submitted.

(iii) A maximum of $250 of each individual's aggregate contributions will be considered as matchable contributions for the purpose of meeting the thresholds of this section.

(iv) For purposes of this section, contributions of an individual who maintains residences in more than one State may only be counted toward the $5,000 threshold for the State from which the earliest contribution was made by that contributor.

(c) *Threshold submission.* To become eligible to receive matching payments, the candidate shall submit documentation of the contributions described in 11 CFR 9033.2(b)(3) to the Commission for review. The submission shall follow the format and requirements of 11 CFR 9036.1.

§ 9033.3 Expenditure limitation certification.

(a) If the Commission makes an initial determination that a candidate or the candidate's authorized committee(s) have knowingly and substantially exceeded the expenditure limitations at 11 CFR part 9035 prior to that candidate's application for certification, the Commission may make an initial determination that the candidate is ineligible to receive matching funds.

(b) The Commission will notify the candidate of its initial determination, in accordance with the procedures outlined in 11 CFR 9033.10(b). The candidate may submit, within 20 calendar days after service of the Commission's notice, written legal or factual materials, in accordance with 11 CFR 9033.10(b), demonstrating that he or she has not knowingly and substantially exceeded the expenditure limitations at 11 CFR part 9035.

(c) A final determination of the candidate's ineligibility will be made by the Commission in accordance with the procedures outlined in 11 CFR 9033.10(c).

(d) A candidate who receives a final determination of ineligibility under 11 CFR 9033.3(c) shall be ineligible to receive matching fund payments under 11 CFR 9034.1.

§ 9033.4 Matching payment eligibility threshold requirements.

(a) The Commission will examine the submission made under 11 CFR 9033.1 and 9033.2 and either—

(1) Make a determination that the candidate has satisfied the minimum contribution threshold requirements under 11 CFR 9033.2(c); or

(2) Make an initial determination that the candidate has failed to satisfy the matching payment threshold requirements. The Commission will notify the candidate of its initial determination in accordance with the procedures outlined in 11 CFR 9033.10(b). The candidate may, within 30 calendar days after service of the Commission's notice, satisfy the threshold requirements or submit in accordance with 11 CFR 9033.10(b) written legal or factual materials to demonstrate that he or she has satisfied those requirements. A final determination by the Commission that the candidate has failed to satisfy threshold requirements will be made in accordance with the procedures outlined in 11 CFR 9033.10(c).

(b) In evaluating the candidate's submission under 11 CFR 9033.1 and 9033.2, the Commission may consider other information in its possession, including but not limited to past actions of the candidate in an earlier publicly-financed campaign, that is relevant to a determination regarding the candidate's eligibility for matching funds.

(c) The Commission will make its examination and determination under this section as soon as practicable. During the Presidential election year, the Commission will generally complete its review and make its determination within 15 business days.

§ 9033.5 Determination of ineligibility date.

The candidate's date of ineligibility shall be whichever date by operation of 11 CFR 9033.5 (a), (b), or (c) occurs first. After the candidate's date of ineligibility, he or she may only receive matching payments to the extent that he or she has net outstanding campaign obligations as defined in 11 CFR 9034.5.

(a) *Inactive candidate.* The ineligibility date shall be the day on which an individual ceases to be a candidate because he or she is not actively conducting campaigns in more than one State in connection with seeking the Presidential nomination. This date shall be the earliest of—

(1) The date the candidate publicly announces that he or she will not be actively conducting campaigns in more than one State; or

(2) The date the candidate notifies the Commission by letter that he or she is not actively conducting campaigns in more than one State; or

(3) The date which the Commission determines under 11 CFR 9033.6 to be the date that the candidate is not actively seeking election in more than one State.

(b) *Insufficient votes.* The ineligibility date shall be the 30th day following the date of the second consecutive primary election in which such individual receives less than 10 percent of the number of popular votes cast for all candidates of the same party for the same office in that primary election, if the candidate permitted or authorized his or her name to appear on the ballot, unless the candidate certifies to the Commission at least 25 business days prior to the primary that he or she will not be an active candidate in the primary involved.

(1) The Commission may refuse to accept the candidate's certification if it determines under 11 CFR 9033.7 that the candidate is an active candidate in the primary involved.

(2) For purposes of this paragraph, if the candidate is running in two primary elections in different States on the same date, the highest percentage of votes the candidate receives in any one State will govern. Separate primary elections held in more than one State on the same date are not deemed to be consecutive primaries. If two primary elections are held on the same date in the same State (e.g., a primary to select delegates to a national nominating convention and a primary for the expression of preference for the nomination of candidates for election to the office of President), the highest percentage of votes a candidate receives in either election will govern. If two or more primaries are held in the same State on different dates, the earliest primary will govern.

(3) If the candidate certifies that he or she will not be an active candidate in a particular primary, and the Commission accepts the candidate's certification, the primary involved shall not be counted in determining the candidate's date of ineligibility under paragraph (b) of this section, regardless of the percentage of popular votes cast for the candidate in that primary.

(c) *End of matching payment period.* The ineligibility date shall be the last day of the matching payment period for the candidate as specified in 11 CFR 9032.6.

(d) *Reestablishment of eligibility.* If the Commission has determined that a candidate is ineligible under 11 CFR 9033.5 (a) or (b), the candidate may reestablish eligibility to receive matching funds under 11 CFR 9033.8.

§ 9033.6 Determination of inactive candidacy.

(a) *General.* The Commission may, on the basis of the factors listed in 11 CFR 9033.6(b) below, make a determination that a candidate is no longer actively seeking nomination for election in more than one State. Upon a final determination by the Commission that a candidate is inactive, that candidate will become ineligible as provided in 11 CFR 9033.5.

(b) *Factors considered.* In making its determination of inactive candidacy, the Commission may consider, but is not limited to considering, the following factors:

(1) The frequency and type of public appearances, speeches, and advertisements;

(2) Campaign activity with respect to soliciting contributions or making expenditures for campaign purposes;

(3) Continued employment of campaign personnel or the use of volunteers;

(4) The release of committed delegates;

(5) The candidate urges his or her delegates to support another candidate while not actually releasing committed delegates;

(6) The candidate urges supporters to support another candidate.

(c) *Initial determination.* The Commission will notify the candidate of its initial determination in accordance with the procedures outlined in 11 CFR 9033.10(b) and will advise the candidate of the date on which active campaigning in more than one State ceased. The candidate may, within 15 business days after service of the Commission's notice, submit in accordance with 11 CFR 9033.10(b) written legal or factual materials to demonstrate that he or she is actively campaigning in more than one State.

(d) *Final determination.* A final determination of inactive candidacy will be made by the Commission in accordance with the procedures outlined in 11 CFR 9033.10(c).

§ 9033.7 Determination of active candidacy.

(a) Where a candidate certifies to the Commission under 11 CFR 9033.5(b) that he or she will not be an active candidate in an upcoming primary, the Commission may, nevertheless, on the basis of factors listed in 11 CFR 9033.6(b), make an initial determination that the candidate is an active candidate in the primary involved.

(b) The Commission will notify the candidate of its initial determination within 10 business days of receiving the candidate's certification under 11 CFR 9033.5(b) or, if the timing of the activity does not permit notice during the 10 day period, as soon as practicable following campaign activity by the candidate in the primary state. The Commission's initial determination will be made in accordance with the procedures outlined in 11 CFR 9033.10(b). Within 10 business days after service of the Commission's notice the candidate may submit, in accordance with 11 CFR 9033.10(b), written legal or factual materials to demonstrate that he or she is not an active candidate in the primary involved.

(c) A final determination by the Commission that the candidate is active will be made in accordance with the procedures outlined in 11 CFR 9033.10(c).

§ 9033.8 Reestablishment of eligibility.

(a) *Candidates found to be inactive.* A candidate who has become ineligible under 11 CFR 9033.5(a) on the basis that he or she is not actively campaigning in more than one State may reestablish eligibility for matching payments by submitting to the Commission evidence of active campaigning in more than one State. In determining whether the candidate has reestablished eligibility, the Commission will consider, but is not limited to considering, the factors listed in 11 CFR 9033.6(b). The day the Commission determines to be the day the candidate becomes active again will be the date on which eligibility is reestablished.

(b) *Candidates receiving insufficient votes.* A candidate determined to be ineligible under 11 CFR 9033.5(b) by failing to obtain the required percentage of votes in two consecutive primaries may have his or her eligibility reestablished if the candidate receives at least 20 percent of the total number of votes cast for candidates of the same party for the same office in a primary election held subsequent to the date of the election which rendered the candidate ineligible.

(c) The Commission will make its determination under 11 CFR 9033.8 (a) or (b) without requiring the individual to reestablish eligibility under 11 CFR 9033.1 and 2. A candidate whose eligibility is reestablished under this section may submit, for matching payment, contributions received during ineligibility. Any expenses incurred during the period of ineligibility that would have been considered qualified campaign expenses if the candidate had been eligible during that time may be defrayed with matching payments.

§ 9033.9 Failure to comply with disclosure requirements or expenditure limitations.

(a) If the Commission receives information indicating that a candidate or his or her authorized committee(s) has knowingly and substantially failed to comply with the disclosure requirements of 2 U.S.C. 434 and 11 CFR part 104, or that a candidate has knowingly and substantially exceeded the expenditure limitations at 11 CFR part 9035, the Commission may make an initial determination to suspend payments to that candidate.

(b) The Commission will notify the candidate of its initial determination in accordance with the procedures outlined in 11 CFR 9033.10(b). The candidate will be given an opportunity, within 20 calendar days after service of the Commission's notice, to comply with the above cited provisions or to submit in accordance with 11 CFR 9033.10(b) written legal or factual materials to demonstrate that he or she is not in violation of those provisions.

(c) Suspension of payments to a candidate will occur upon a final determination by the Commission to suspend payments. Such final determination will be made in accordance with the procedures outlined in 11 CFR 9033.10(c).

(d) (1) A candidate whose payments have been suspended for failure to comply with reporting requirements may become entitled to receive payments if he or she subsequently files the required reports and pays or agrees to pay any civil or criminal penalties resulting from failure to comply.

(2) A candidate whose payments are suspended for exceeding the expenditure limitations shall not be entitled to receive further matching payments under 11 CFR 9034.1.

§ 9033.10 Procedures for initial and final determinations.

(a) *General.* The Commission will follow the procedures set forth in this section when making an initial or final determination based on any of the following reasons.

(1) The candidate has knowingly and substantially exceeded the expenditure limitations of 11 CFR part 9035 prior to the candidate's application for certification, as provided in 11 CFR 9033.3;

(2) The candidate has failed to satisfy the matching payment threshold requirements, as provided in 11 CFR 9033.4;

(3) The candidate is no longer actively seeking nomination in more than one state, as provided in 11 CFR 9033.6;

(4) The candidate is an active candidate in an upcoming primary despite the candidate's assertion to the contrary, as provided in 11 CFR 9033.7;

(5) The Commission receives information indicating that the candidate has knowingly and substantially failed to comply with the disclosure requirements or exceeded the expenditure limits, as provided in 11 CFR 9033.9; or

(6) The Commission receives information indicating that substantial assets of the candidate's authorized committee have been undervalued or not included in the candidate's statement of net outstanding campaign obligations or that the amount of outstanding campaign obligations has been otherwise overstated in relation to committee assets, as provided in 11 CFR 9034.5(g).

(b) *Initial determination.* If the Commission makes an initial determination that a candidate may not receive matching funds for one or more of the reasons indicated in 11 CFR 9033.10(a), the Commission will notify the candidate of its initial determination. The notification will give the legal and factual reasons for the determination and advise the candidate of the evidence on which the Commission's initial determination is based. The candidate will be given an opportunity to comply with the requirements at issue or to submit, within the time provided by the relevant section as referred to in 11 CFR 9033.10(a), written legal or factual materials to demonstrate that the candidate has satisfied those requirements. Such materials may be submitted by counsel if the candidate so desires.

(c) *Final determination.* The Commission will consider any written legal or factual materials timely submitted by the candidate before making its final determination. A final determination that the candidate has failed to satisfy the requirements at issue will be accompanied by a written statement of reasons for the Commission's action. This statement will explain the legal and factual reasons underlying the Commission's determination and will summarize the results of any investigation upon which the determination is based.

(d) *Effect on other determinations.* If the Commission makes an initial determination under this section, but decides to take no further action at that time, the Commission may use the legal and factual bases on which the initial determination was based in any future repayment determination under 11 CFR part 9038 or 9039. A determination by the Commission under this section may be independent of any Commission decision to institute an enforcement proceeding under 2 U.S.C. 437g.

(e) *Petitions for rehearing.* Following a final determination under this section, the candidate may file a petition for rehearing in accordance with 11 CFR 9038.5(a).

§ 9033.11 Documentation of disbursements.

(a) *Burden of proof.* Each candidate shall have the burden of proving that disbursements made by the candidate or his or her authorized committee(s) or persons authorized to make expenditures on behalf of the candidate or committee(s) are qualified campaign expenses as defined in 11 CFR 9032.9. The candidate and his or her authorized committee(s) shall obtain and furnish to the Commission on request any evidence regarding qualified campaign expenses made by the candidate, his or her authorized committees and agents or persons authorized to make expenditures on behalf of the candidate or committee(s) as provided in 11 CFR 9033.11(b).

(b) *Documentation required.* (1) For disbursements in excess of $200 to a payee, the candidate shall present either:

(i) A receipted bill from the payee that states the purpose of the disbursement, or

(ii) If such a receipt is not available, a canceled check negotiated by the payee, and

(A) One of the following documents generated by the payee: A bill, invoice, or voucher that states the purpose of the disbursement; or

(B) Where the documents specified in 11 CFR 9033.11(b)(1)(ii)(A) are not available, a voucher or contemporaneous memorandum from the candidate or the committee that states the purpose of the disbursement; or

(iii) If neither a receipted bill as specified in 11 CFR 9033.11(b)(1)(i) nor the supporting documentation specified in 11 CFR 9033.11(b)(1)(ii) is available, a canceled check negotiated by the payee that states the purpose of the disbursement.

(iv) Where the supporting documentation required in 11 CFR 9033.11(b)(1) (i), (ii) or (iii) is not available, the candidate or committee may present a canceled check and collateral evidence to document the qualified campaign expense. Such collateral evidence may include but is not limited to:

(A) Evidence demonstrating that the expenditure is part of an identifiable program or project which is otherwise sufficiently documented such as a disbursement which is one of a number of documented disbursements relating to a campaign mailing or to the operation of a campaign office;

(B) Evidence that the disbursement is covered by a preestablished written campaign committee policy, such as a daily travel expense policy.

(2) For all other disbursements the candidate shall present:

(i) A record disclosing the identification of the payee, the amount, date and purpose of the disbursement, if made from a petty cash fund; or

(ii) A canceled check negotiated by the payee that states the identification of the payee, and the amount, date and purpose of the disbursement.

(3) For purposes of this section,

(i) *Payee* means the person who provides the goods or services to the candidate or committee in return for the disbursement; except that an individual will be considered a payee under this section if he or she receives $500 or less advanced for travel and or/subsistence and if he or she is the recipient of the goods or services purchased.

(ii) *Purpose* means the identification of the payee, the date and amount of the disbursement, and a description of the goods or services purchased.

(c) *Retention of records.* The candidate shall retain records, with respect to each disbursement and receipt, including bank records, vouchers, worksheets, receipts, bills and accounts, journals, ledgers, fundraising solicitation material, accounting systems documentation, matching fund submissions, and any related materials documenting campaign receipts and disbursements, for a period of three years pursuant to 11 CFR 102.9(c), and shall present these records to the Commission on request.

(d) *List of capital and other assets*—(1) *Capital assets.* The candidate or committee shall maintain a list of all capital assets whose purchase price exceeded $2000 when acquired by the candidate's authorized committee(s). The list shall include a brief description of each capital asset, the purchase price, the date it was acquired, the method of disposition and the amount received in disposition. For purposes of this section, *capital asset* shall be defined in accordance with 11 CFR 9034.5(c)(1).

(2) *Other assets.* The candidate or committee shall maintain a list of other assets acquired for use in fundraising or as collateral for campaign loans, if the aggregate value of such assets exceeds $5000. The list shall include a brief description of each such asset, the fair market value of each asset, the method of disposition and the amount received in disposition. The fair market value of other assets shall be determined in accordance with 11 CFR 9034.5(c)(2).

§ 9033.12 Production of computerized information.

(a) *Categories of computerized information to be provided.* If the candidate or the candidate's authorized committee maintains or uses computerized information containing any of the categories of data listed in paragraphs (a)(1) through (a)(9) of this section, the committee shall provide computerized magnetic media, such as magnetic tapes or magnetic diskettes, containing the computerized information at the times specified in 11 CFR 9038.1(b)(1):

(1) Information required by law to be maintained regarding the committee's receipts or disbursements;

(2) Records of allocations of expenditures to particular state expenditure limits and to the overall expenditure limit;

(3) Disbursements for exempt fundraising and exempt compliance costs, including the allocation of salaries and overhead expenditures;

(4) Records of allocations of expenditures for the purchase of broadcast media;

(5) Records used to prepare statements of net outstanding campaign obligations;

(6) Records used to reconcile bank statements;

(7) Disbursements made and reimbursements received for the cost of transportation, ground services and facilities made available to media personnel, including records relating to how costs charged to media personnel were determined;

(8) Records relating to the acquisition, use and disposition of capital assets or other assets; and

(9) Any other information that may be used during the Commission's audit to review the committee's receipts, disbursements, loans, debts, obligations, bank reconciliations or statements of net outstanding campaign obligations.

(b) *Organization of computerized information and technical specifications.* The computerized magnetic media shall be prepared and delivered at the committee's expense and shall conform to the technical specifications, including file requirements, described in the Federal Election Commission's Computerized Magnetic Media Requirements for title 26 Candidates/Committees Receiving Federal Funding. The data contained in the computerized magnetic media provided to the Commission shall be organized in the order specified by the Computerized Magnetic Media Requirements.

(c) *Additional materials and assistance.* Upon request, the committee shall provide documentation explaining the computer system's software capabilities, such as user guides, technical manuals, formats, layouts and other materials for processing and analyzing the information requested. Upon request, the committee shall also make available such personnel as are necessary to explain the operation of the computer system's software and the computerized information prepared or maintained by the committee.

PART 9034—ENTITLEMENTS

Sec.

Authority: 26 U.S.C. 9034 and 9039(b).

§ 9034.1 Candidate entitlements.

(a) A candidate who has been notified by the Commission under 11 CFR 9036.1 that he or she has successfully satisfied eligibility and certification requirements is entitled to receive payments under 26 U.S.C. 9037 and 11 CFR part 9037 in an amount equal to the amount of each matchable campaign contribution received by the candidate, except that a candidate who has become ineligible under 11 CFR 9033.5 may not receive further matching payments regardless of the date of deposit of the underlying contributions if he or she has no net outstanding campaign obligations as defined in 11 CFR 9034.5.

(b) If on the date of ineligibility a candidate has net outstanding campaign obligations as defined under 11 CFR 9034.5, that candidate may continue to receive matching payments for matchable contributions received and deposited on or before December 31 of the Presidential election year provided that on the date of payment there are remaining net outstanding campaign obligations, i.e., the sum of the contributions received on or after the date of ineligibility plus matching funds received on or after the date of ineligibility is less than the candidate's net outstanding campaign obligations. This entitlement will be equal to the lesser of:

(1) The amount of contributions submitted for matching; or

(2) The remaining net outstanding campaign obligations.

(c) A candidate whose eligibility has been reestablished under 11 CFR 9033.8 or who after suspension of payments has met the conditions set forth at 11 CFR 9033.9(d) is entitled to receive payments for matchable contributions for which payments were not received during the ineligibility or suspension period.

(d) The total amount of payments to a candidate under this section shall not exceed 50% of the total expenditure limitation applicable under 11 CFR part 9035.

§ 9034.2 Matchable contributions.

(a) Contributions meeting the following requirements will be considered matchable campaign contributions.

(1) The contribution shall be a gift of money made: By an individual; by a written instrument and for the purpose of influencing the result of a primary election.

(2) Only a maximum of $250 of the aggregate amount contributed by an individual may be matched.

(3) Before a contribution may be submitted for matching, it must actually be received by the candidate or any of the candidate's authorized committees and deposited in a designated campaign depository maintained by the candidate's authorized committee.

(4) The written instrument used in making the contribution must be dated, physically received and deposited by the candidate or authorized committee on or after January 1 of the year immediately preceding the calendar year of the Presidential election, but no later than December 31 following the matching payment period as defined under 11 CFR 9032.6. Donations received by an individual who is testing the waters pursuant to 11 CFR 100.7(b)(1) and 100.8(b)(1) may be matched when the individual becomes a candidate if such donations meet the requirements of this section.

(b) For purposes of this section, the term *written instrument* means a check written on a personal, escrow or trust account representing or containing the contributor's personal funds; a money order; or any similar negotiable instrument.

(c) The written instrument shall be: Payable on demand; and to the order of, or specifically endorsed without qualification to, the Presidential candidate, or his or her authorized committee. The written instrument shall contain: The full name and signature of the contributor(s); the amount and date of the contribution; and the mailing address of the contributor(s).

(1) In cases of a check drawn on a joint checking account, the contributor is considered to be the owner whose signature appears on the check.

(i) To be attributed equally to other joint tenants of the account, the check or other accompanying written document shall contain the signature(s) of the joint tenant(s). If a contribution on a joint account is to be attributed other than equally to the joint tenants, the check or other written documentation shall also indicate the amount to be attributed to each joint tenant.

(ii) In the case of a check for a contribution attributed to more than one person, where it is not apparent from the face of the check that each contributor is a joint tenant of the account, a written statement shall accompany the check stating that the contribution was made from each individual's personal funds in the amount so attributed and shall be signed by each contributor.

(iii) In the case of a contribution reattributed to a joint tenant of the account, the reattribution shall comply with the requirements of 11 CFR 110.1(k) and the documentation described in 11 CFR 110.1 (1), (3), (5) and (6) shall accompany the reattributed contribution.

(2) Contributions in the form of checks drawn on an escrow or trust account are matchable contributions, provided that:

(i) The contributor has equitable ownership of the account; and

(ii) The check is accompanied by a statement, signed by each contributor to whom all or a portion of the contribution is being attributed, together with the check number, amount and date of contribution. This statement shall specify that the contributor has equitable ownership of the account and the account represents the personal funds of the contributor.

(3) Contributions in the form of checks written on partnership accounts or accounts of unincorporated associations or businesses are matchable contributions, so long as:

(i) The check is accompanied by a statement, signed by each contributor to whom all or a portion of the contribution is being attributed, together with the check number, amount and date of contribution. This statement shall specify that the contribution is made with the contributor's personal funds and that the account on which the contribution is drawn is not maintained or controlled by an incorporated entity; and

(ii) The aggregate amount of the contributions drawn on a partnership or unincorporated association or business does not exceed $1,000 to any one Presidential candidate seeking nomination.

(4) Contributions in the form of money orders, cashier's checks, or other similar negotiable instruments are matchable contributions, provided that:

(i) At the time it is initially submitted for matching, such instrument is signed by each contributor and is accompanied by a statement which specifies that the contribution was made in the form of a money order, cashier's check, traveler's check, or other similar negotiable instrument, with the contributor's personal funds;

(ii) Such statement identifies the date and amount of the contribution made by money order, cashier's check, traveler's check, or other similar negotiable instrument, the check or serial number, and the name of the issuer of the negotiable instrument; and

(iii) Such statement is signed by each contributor.

(5) Contributions in the form of the purchase price paid for the admission to any activity that primarily confers private benefits in the form of entertainment to the contributor (i.e., concerts, motion pictures) are matchable. The promotional material and tickets for the event shall clearly indicate that the ticket purchase price represents a contribution to the Presidential candidate.

(6) Contributions in the form of a purchase price paid for admission to an activity that is essentially political are matchable. An "essentially political" activity is one the principal purpose of which is political speech or discussion, such as the traditional political dinner or reception.

(7) Contributions received from a joint fundraising activity conducted in accordance with 11 CFR 9034.8 are matchable, provided that such contributions are accompanied by a copy of the joint fundraising agreement when they are submitted for matching.

§ 9034.3 Non-matchable contributions.

A contribution to a candidate other than one which meets the requirements of 11 CFR 9034.2 is not matchable. Contributions which are not matchable include, for example:

(a) In-kind contributions of real or personal property;

(b) A subscription, loan, advance, or deposit of money, or anything of value;

(c) A contract, promise, or agreement, whether or not legally enforceable, such as a pledge card or credit card transaction, to make a contribution for any such purposes (but a gift of money by written instrument is not rendered unmatchable solely because the contribution was preceded by a promise or pledge);

(d) Funds from a corporation, labor organization, government contractor, political committee as defined in 11 CFR 100.5 or any group of persons other than those under 11 CFR 9034.2(c)(3);

(e) Contributions which are made or accepted in violation of 2 U.S.C. 441a, 441b, 441c, 441e, 441f, or 441g;

(f) Contributions in the form of a check drawn on the account of a committee, corporation, union or government contractor even though the funds represent personal funds earmarked by a contributing individual to a Presidential candidate;

(g) Contributions in the form of the purchase price paid for an item with significant intrinsic and enduring value, such as a watch;

(h) Contributions in the form of the purchase price paid for or other otherwise induced by a chance to participate in a raffle, lottery, or a similar drawing for valuable prizes;

(i) Contributions which are made by persons without the necessary donative intent to make a gift or made for any purpose other than to influence the result of a primary election;

(j) Contributions of currency of the United States or currency of any foreign country; and

(k) Contributions redesignated for a different election or redesignated for a legal and accounting compliance fund pursuant to 11 CFR 9003.3.

§ 9034.4 Use of contributions and matching payments.

(a) *Qualified campaign expenses*—(1) *General.* Except as provided in 11 CFR 9034.4(b)(3), all contributions received by an individual from the date he or she becomes a candidate and all matching payments received by the candidate shall be used only to defray qualified campaign expenses or to repay loans or otherwise restore funds (other than contributions which were received and expended to defray qualified campaign expenses), which were used to defray qualified campaign expenses.

(2) *Testing the waters.* Even though incurred prior to the date an individual becomes a candidate, payments made for the purpose of determining whether an individual should become a candidate, such as those incurred in conducting a poll, shall be considered qualified campaign expenses if the individual subsequently becomes a candidate and shall count against that candidate's limits under 2 U.S.C. 441a(b). See 11 CFR 100.8(b)(1).

(3) *Winding down costs and continuing to campaign.* (i) Costs associated with the termination of political activity, such as the costs of complying with the post election requirements of the Act and other necessary administrative costs associated with winding down the campaign, including office space rental, staff salaries and office supplies, shall be considered qualified campaign expenses. A candidate may receive and use matching funds for these purposes either after he or she has notified the Commission in writing of his or her withdrawal from the campaign for nomination or after the date of the party's nominating convention, if he or she has not withdrawn before the convention.

(ii) If the candidate continues to campaign after becoming ineligible due to the operation of 11 CFR 9033.5(b), the candidate may only receive matching funds based on net outstanding campaign obligations as of the candidate's date of ineligibility. The statement of net outstanding campaign obligations shall only include costs incurred before the candidate's date of ineligibility for goods and services to be received before the date of ineligibility and for which written arrangement or commitment was made on or before the candidate's date of ineligibility, and shall not include winding down costs until the date on which the candidate qualifies to receive winding down costs under paragraph (a)(3)(i) of this section. Contributions received after the candidate's date of ineligibility may be used to continue to campaign, and may be submitted for matching fund payments. The candidate shall be entitled to receive the same proportion of matching funds to defray net outstanding campaign obligations as the candidate received before his or her date of ineligibility. Payments from the matching payment account that are received after the candidate's date of ineligibility may be used to defray the candidate's net outstanding campaign obligations, but shall not be used to defray any costs associated with continuing to campaign unless the candidate reestablishes eligibility under 11 CFR 9033.8.

(4) *Taxes.* Federal income taxes paid by the committee on non-exempt function income, such as interest, dividends and sale of property, shall be considered qualified campaign expenses. These expenses shall not, however, count against the state or overall expenditure limits of 11 CFR 9035.1(a).

(b) *Non-qualified campaign expenses*—(1) *General.* The following are examples of disbursements that are not qualified campaign expenses.

(2) *Excessive expenditures.* An expenditure which is in excess of any of the limitations under 11 CFR Part 9035 shall not be considered a qualified campaign expense. The Commission will calculate the amount of expenditures attributable to the limitations in accordance with 11 CFR 9035.1(a)(2).

(3) *Post-ineligibility expenditures.* Any expenses incurred after a candidate's date of ineligibility, as determined under 11 CFR 9033.5, are not qualified campaign expenses except to the extent permitted under 11 CFR 9034.4(a)(3). Any expenses incurred before the candidate's date of ineligibility for goods and services to be received after the candidate's date of ineligibility are not qualified campaign expenses.

(4) *Civil or criminal penalties.* Civil or criminal penalties paid pursuant to the Federal Election Campaign Act are not qualified campaign expenses and cannot be defrayed from contributions or matching payments. Any amounts received or expended to pay such penalties shall not be considered contributions or expenditures but all amounts so received shall be subject to the prohibitions of the Act. Amounts received and expended under this section shall be reported in accordance with 11 CFR part 104.

(5) *Payments to candidate.* Payments made to the candidate by his or her committee, other than to reimburse funds advanced by the candidate for qualified campaign expenses, are not qualified campaign expenses.

(6) *Payments to other authorized committees.* Payments, including transfers and loans, to other committees authorized by the same candidate for a different election are not qualified campaign expenses.

(7) *Allocable expenses.* Payments for expenses subject to state allocation under 11 CFR 106.2 are not qualified campaign expenses if the records retained are not sufficient to permit allocation to any state, such as the failure to keep records of the date on which the expense is incurred.

(c) *Repayments.* Repayments may be made only from the following sources: personal funds of the candidate (without regard to the limitations of 11 CFR 9035.2(a)), contributions and matching payments in the committee's account(s), and any additional funds raised subject to the limitations and prohibitions of the Federal Election Campaign Act of 1971, as amended.

(d) *Transfers to other campaigns*—(1) *Other Federal offices.* If a candidate has received matching funds and is simultaneously seeking nomination or election to another Federal office, no transfer of funds between his or her principal campaign committees or authorized committees may be made. See 2 U.S.C. 441a(a)(5)(C) and 11 CFR 110.3(c)(5) and 110.8(d). A candidate will be considered to be simultaneously seeking nomination or election to another Federal office if he or she is seeking nomination or election to such Federal office under 11 CFR 110.3(c)(5).

(2) *General election.* If a candidate has received matching funds, all transfers from the candidate's primary election account to a legal and accounting compliance fund established for the general election must be made in accordance with 11 CFR 9003.3(a)(1) (ii) and (iii).

§ 9034.5 Net outstanding campaign obligations.

(a) Within 15 calendar days after the candidate's date of ineligibility, as determined under 11 CFR 9033.5, the candidate shall submit a statement of net outstanding campaign obligations. The candidate's net outstanding campaign obligations under this section equal the difference between paragraphs (a) (1) and (2) of this section:

(1) The total of all outstanding obligations for qualified campaign expenses as of the candidate's date of ineligibility as determined under 11 CFR 9033.5, plus estimated necessary winding down costs as defined under 11 CFR 9034.4(a)(3), less

(2) The total of:

(i) Cash on hand as of the close of business on the last day of eligibility (including all contributions dated on or before that date whether or not submitted for matching; currency; balances on deposit in banks; savings and loan institutions; and other depository institutions; traveler's checks; certificates of deposit; treasury bills; and any other committee investments valued at fair market value);

(ii) The fair market value of capital assets and other assets on hand; and

(iii) Amounts owed to the committee in the form of credits, refunds of deposits, returns, receivables, or rebates of qualified campaign expenses; or a commercially reasonable amount based on the collectibility of those credits, returns, receivables or rebates.

(b) The amount submitted as the total of outstanding campaign obligations under paragraph (a)(1) of this section shall not include any accounts payable for non-qualified campaign expenses nor any amounts determined or anticipated to be required as a repayment under 11 CFR part 9038 or any amounts paid to secure a surety bond under 11 CFR 9038.5(c).

(c) (1) *Capital assets.* For purposes of this section, the term *capital asset* means any property used in the operation of the campaign whose purchase price exceeded $2000 when acquired by the committee. Property that must be valued as capital assets under this section includes, but is not limited to, office equipment, furniture, vehicles and fixtures acquired for use in the operation of the candidate's campaign, but does not include property defined as "other assets" under 11 CFR 9034.5(c)(2). A list of all capital assets shall be maintained by the Committee in accordance with 11 CFR 9033.11(d). The fair market value of capital assets may be considered to be the total original cost of such items when acquired less 40%, to account for depreciation, except that items acquired after the date of ineligibility must be valued at their fair market value on the date acquired. If the candidate wishes to claim a higher depreciation percentage for an item, he or she must list that capital asset on the statement separately and demonstrate, through documentation, the fair market value of each such asset.

(2) *Other assets.* The term *other assets* means any property acquired by the committee for use in raising funds or as collateral for campaign loans. "Other assets" must be included on the candidate's statement of net outstanding campaign obligations if the aggregate value of such assets exceeds $5000. The value of "other assets" shall be determined by the fair market value of each item on the candidate's date of ineligibility or on the date the item is acquired if acquired after the date of ineligibility. A list of other assets shall be maintained by the committee in accordance with 11 CFR 9033.11(d)(2).

(d) *Collectibility of accounts receivable.* If the committee determines that an account receivable of $500 or more, including any credit, refund, return or rebate, is not collectible in whole or in part, the committee shall demonstrate through documentation that the determination was commercially reasonable. The documentation shall include records showing the original amount of the account receivable, copies of correspondence and memoranda of communications with the debtor showing attempts to collect the amount due, and an explanation of how the lesser amount or full writeoff was determined.

(e) Contributions received from joint fundraising activities conducted under 11 CFR 9034.8 may be used to pay a candidate's outstanding campaign obligations.

(1) Such contributions shall be deemed monies available to pay outstanding campaign obligations as of the date these funds are received by the fundraising representative committee and shall be included in the candidate's statement of net outstanding campaign obligations.

(2) The amount of money deemed available to pay a candidate's net outstanding campaign obligations will equal either—

(i) An amount calculated on the basis of the predetermined allocation formula, as adjusted for 2 U.S.C. 441a limitations; or

(ii) If a candidate receives an amount greater than that calculated under 11 CFR 9034.5(e)(2)(i), the amount actually received.

(f) The candidate shall submit a revised statement of net outstanding campaign obligations with each submission for matching funds payments filed after the candidate's date of ineligibility. The revised statement shall reflect the financial status of the committee as of the close of business on the last business day preceding the date of submission for matching funds. The revised statement shall also contain a brief explanation of each change in the committee's assets and obligations from the previous statement.

(g) (1) If the Commission receives information indicating that substantial assets of the candidate's authorized committee(s) have been undervalued or not included in the statement or that the amount of outstanding campaign obligations has been otherwise overstated in relation to committee assets, the Commission may decide to temporarily suspend further matching payments pending a final determination whether the candidate is entitled to receive all or a portion of the matching funds requested.

(2) In making a determination under 11 CFR 9034.5(g)(1), the Commission will follow the procedures for initial and final determinations under 11 CFR 9033.10 (b) and (c). The Commission will notify the candidate of its initial determination within 15 business days after receipt of the candidate's statement of net outstanding campaign obligations. Within 15 business days after service of the Commission's notice,

the candidate may submit written legal or factual materials to demonstrate that he or she has met outstanding campaign obligations that entitle the campaign to further matching payments.

(3) If the candidate demonstrates that the amount of outstanding campaign obligations still exceeds committee assets, he or she may continue to receive matching payments.

(4) Following a final determination under this section, the candidate may file a petition for rehearing in accordance with 11 CFR 9038.5(a).

§ 9034.6 Reimbursements for transportation and services made available to media personnel.

(a) If an authorized committee incurs expenditures for transportation, ground services and facilities (including air travel, ground transportation, housing, meals, telephone service, and typewriters) made available to media personnel, Secret Service personnel or national security staff, such expenditures will be considered qualified campaign expenses and, except for costs relating to Secret Service personnel or national security staff, subject to the overall expenditure limitations of 11 CFR 9035.1(a).

(b) If reimbursement for such expenditures is received by a committee, the amount of such reimbursement for each media representative shall not exceed either: The media representative's pro rata share of the actual cost of the transportation and services made available; or a reasonable estimate of the media representative's pro rata share of the actual cost of the transportation and services made available. A media representative's pro rata share shall be calculated by dividing the total cost of the transportation and services by the total number of individuals to whom such transportation and services are made available. For purposes of this calculation, the total number of individuals shall include committee staff, media personnel, Secret Service personnel, national security staff and any other individuals to whom such transportation and services are made available. The total amount of reimbursements received from a media representative under this section shall not exceed the actual pro rata cost of the transportation and services made available to that media representative by more than 10%.

(c) The total amount paid by an authorized committee for the cost of transportation or for ground services and facilities shall be reported as an expenditure in accordance with 11 CFR 104.3(b)(2)(i). Any reimbursement received by such committee for transportation or ground services and facilities shall be reported in accordance with 11 CFR 104.3(a)(3)(ix).

(d)(1) The committee may deduct from the amount of expenditures subject to the overall expenditure limitation of 11 CFR 9035.1(a) the amount of reimbursements received in payment for the actual cost of transportation and services described in paragraph (a) of this section. This deduction shall not exceed the amount the committee expended for the actual cost of transportation and services provided. The committee may also deduct from the overall expenditure limitation an additional amount of reimbursements received equal to 3% of the actual cost of transportation and services provided under this section as the administrative cost to the committee of providing such services and seeking reimbursement for them. If the committee has incurred higher administrative costs in providing these services, the committee must document the total cost incurred for such services in order to deduct a higher amount of reimbursements received from the overall expenditure limitation. Amounts reimbursed that exceed the amount actually paid by the committee for transportation and services provided under paragraph (a) of this section plus the amount of administrative costs permitted by this section up to the maximum amount that may be received under paragraph (b) shall be repaid to the Treasury. Amounts paid by the committee for transportation, services and administrative costs for which no reimbursement is received will be considered qualified campaign expenses subject to the overall expenditure limitation in accordance with paragraph (a) of this section.

(2) For the purposes of this section, "administrative costs" shall include all costs incurred by the committee for making travel arrangements and for seeking reimbursements, whether performed by committee staff or independent contractors.

§ 9034.7 Allocation of travel expenditures.

(a) Notwithstanding the provisions of 11 CFR part 106, expenditures for travel relating to the campaign of a candidate seeking nomination for election to the office of President by any individual, including a candidate, shall, pursuant to the provisions of 11 CFR 9034.7(b), be qualified campaign expenses and be reported by the candidate's authorized committee(s) as expenditures.

(b)(1) For a trip which is entirely campaign-related, the total cost of the trip shall be a qualified campaign expense and a reportable expenditure.

(2) For a trip which includes campaign-related and non-campaign related stops, that portion of the cost of the trip allocable to campaign activity shall be a qualified campaign expense and a reportable expenditure. Such portion shall be determined by calculating what the trip would have cost from the point of origin of the trip to the first campaign-related stop and from that stop through each subsequent campaign-related stop, back to the point of origin. If any campaign activity, other than incidental contacts, is conducted at a stop, that stop shall be considered campaign-related.

(3) For each trip, an itinerary shall be prepared and such itinerary shall be made available for Commission inspection.

(4) For trips by government conveyance or by charter, a list of all passengers on such trip, along with a designation of which passengers are and which are not campaign-related, shall be made available for Commission inspection.

(5) If any individual, including a candidate, uses government conveyance or accommodations paid for by a government entity for campaign-related travel, the candidate's authorized committee shall pay the appropriate government entity an amount equal to:

(i) The first class commercial air fare plus the cost of other services, in the case of travel to a city served by a regularly scheduled commercial service; or

(ii) The commercial charter rate plus the cost of other services, in the case of travel to a city not served by a regularly scheduled commercial service.

(6) Travel expenses of a candidate's spouse and family when accompanying the candidate on campaign-related travel may be treated as qualified campaign expenses and reportable expenditures. If the spouse or family members conduct campaign-related activities, their travel expenses will be treated as qualified campaign expenses and reportable expenditures.

(7) If any individual, including a candidate, incurs expenses for campaign-related travel, other than by use of government conveyance or accommodations, an amount equal to that portion of the actual cost of the conveyance or accommodations which is allocable to all passengers, including the candidate, traveling for campaign purposes will be a qualified campaign expense and shall be reported by the committee as an expenditure.

(i) If the trip is by charter, the actual cost for each passenger shall be determined by dividing the total operating cost for the charter by the total number of passengers transported. The amount which is a qualified campaign expense and a reportable expenditure shall be calculated in accordance with the formula set forth at 11 CFR 9034.7(b)(2) on the basis of the actual cost per passenger multiplied by the number of passengers traveling for campaign purposes.

(ii) If the trip is by non-charter commercial transportation, the actual cost shall be calculated in accordance with the formula set forth at 11 CFR 9034.7(b)(2) on the basis of the commercial fare. Such actual cost shall be a qualified campaign expense and a reportable expenditure.

§ 9034.8 Joint fundraising.

(a) *General.*—(1) *Permissible participants.* Presidential primary candidates who receive matching funds under this subchapter may engage in joint fundraising with other candidates, political committees or unregistered committees or organizations.

(2) *Use of funds.* Contributions received as a result of a candidate's participation in a joint fundraising activity under this section may be—

(i) Submitted for matching purposes in accordance with the requirements of 11 CFR 9034.2 and the Federal Election Commission's Guideline for Presentation in Good Order;

(ii) Used to pay a candidate's net outstanding campaign obligations as provided in 11 CFR 9034.5;

(iii) Used to defray qualified campaign expenses;

(iv) Used to defray exempt legal and accounting costs; or

(v) If in excess of a candidate's net outstanding campaign obligations or expenditure limit, used in any manner consistent with 11 CFR 113.2, including repayment of funds under 11 CFR part 9038.

(b) *Fundraising representatives.*—(1) *Establishment or selection of fundraising representative.* The participants in a joint fundraising effort under this section shall either establish a separate committee or select a participating committee, to act as fundraising representative for all participants. The fundraising representative shall be a reporting political committee and an authorized committee of each candidate. If the participants estabish a separate committee to act as the fundraising representative, the separate committee shall not be a participant in any other joint fundraising effort, but the separate committee may conduct more than one joint fundraising effort for the participants.

(2) *Separate fundraising committee as fundraising representative.* A separate fundraising committee established by the participants to act as fundraising representative for all participants shall—

(i) Be established as a reporting political committee under 11 CFR 100.5;

(ii) Collect contributions;

(iii) Pay fundraising costs from gross proceeds and funds advanced by participants; and

(iv) Disburse net proceeds to each participant.

(3) *Participating committee as fundraising representative.* A participant selected to act as fundraising representative for all participants shall—

(i) Be a political committee as defined in 11 CFR 100.5;

(ii) Collect contributions; however, other participants may also collect contributions and then forward them to the fundraising representative as required by 11 CFR 102.8;

(iii) Pay fundraising costs from gross proceeds and funds advanced by participants; and

(iv) Disburse net proceeds to each participant.

(4) *Independent fundraising agent.* The participants or the fundraising representative may hire a commercial fundraising firm or other agent to assist in conducting the joint fundraising activity. In that case, however, the fundraising representative shall still be responsible for ensuring that the recordkeeping, reporting and documentation requirements set forth in this subchapter are met.

(c) *Joint fundraising procedures.* Any joint fundraising activity under this section shall be conducted in accordance with the following requirements:

(1) *Written agreement.* The participants in a joint fundraising activity shall enter into a written agreement, whether or not all participants are political committees under 11 CFR 100.5. The written agteement shall identify the fundraising representative and shall state a formula for the allocation of fundraising proceeds. The formula shall be stated as the amount or percentage of each contribution received to be allocated to each participant. The fundraising representative shall retain the written agreement for a period of three years and shall make it available to the Commission on request.

(2) *Funds advanced for fundraising costs.* (i) Except as provided in 11 CFR 9034.8(c)(2)(ii), the amount of funds advanced by each participant for fundraising costs shall be in proportion to the allocation formula agreed upon under 11 CFR 9034.8(c)(1).

(ii) A participant may advance more than its proportionate share of the fundraising costs; however, the amount advanced which is in excess of the participant's proportionate share shall not exceed the amount that participant could legally contribute to the remaining participants. See 11 CFR 102.12(c)(2), part 110, and 9034.4(b)(6).

(3) *Fundraising notice.* In addition to any notice required under 11 CFR 110.11, a joint fundraising notice shall be included with every solicitation for contributions.

(i) This notice shall include the following information:

(A) The names of all committees participating in the joint fundraising activity whether or not such committees are political committees under 11 CFR 100.5;

(B) The allocation formula to be used for distributing joint fundraising proceeds;

(C) A statement informing contributors that, notwithstanding the stated allocation formula, they may designate their contributions for a particular participant or participants; and

(D) A statement informing contributors that the allocation formula may change if a contributor makes a contribution which would exceed the amount that contributor may give to any participant.

(ii) If one or more participants engage in the joint fundraising activity solely to satisfy outstanding debts, the notice shall also contain a statement informing contributors that the allocation formula may change if a participant receives sufficient funds to pay its outstanding debts.

(4) *Separate depository account.* (i) The participants or the fundraising representative shall establish a separate depository account to be used solely for the receipt and disbursement of the joint fundraising proceeds. All contributions deposited into the separate depository account must be permissible under title 2, United States Code. Each political committee shall amend its Statement of Organization to reflect the account as an additional depository.

(ii) The fundraising representative shall deposit all joint fundraising proceeds in the separate depository account within ten days of receipt as required by 11 CFR 103.3. The fundraising representative may delay distribution of the fundraising proceeds to the participants until all contributions are received and all expenses are paid.

(iii) For contribution reporting and limitation purposes, the date of receipt of a contribution by a participating political committee is the date that the contribution is received by the fundraising representative. The fundraising representative shall report contributions in the reporting period in which they are received. Participating political committees shall report joint fundraising proceeds in accordance with 11 CFR 9034.8(c)(9) when such funds are received from the fundraising representative.

(5) *Recordkeeping requirements.* (i) The fundraising representative and participating committees shall screen all contributions received to insure that the prohibitions and limitations of 11 CFR parts 110 and 114 are observed. Participating political committees shall make their contributor records available to the fundraising representative to enable the fundraising representative to carry out its duty to screen contributions.

(ii) The fundraising representative shall collect and retain contributor information with regard to gross proceeds as required under 11 CFR 102.8 and shall also forward such information to participating political committees.

(iii) The fundraising representative shall retain the records required under 11 CFR 9033.11 regarding fundraising disbursements for a period of three years. Commercial fundraising firms or agents shall forward such information to the fundraising representative.

(6) *Contribution limitations.* Except to the extent that the contributor has previously contributed to any of the participants, a contributor may make a contribution to the joint fundraising effort which contribution represents the total amount that the contributor could contribute to all of the participants under the applicable limits of 11 CFR 110.1 and 110.2.

(7) *Allocation of gross proceeds.* (i) The fundraising representative shall allocate proceeds according to the formula stated in the fundraising agreement. Each contribution received shall be allocated among the participants in accordance with the allocation formula, unless the circumstances described in paragraphs (c)(7) (ii), (iii) or (iv) of this section apply. Funds may not be distributed or reallocated so as to maximize the matchability of the contributions.

(ii) If distribution according to the allocation formula extinguishes the debts of one or more participants or if distribution under the formula results in a violation of the contribution limits of 11 CFR 110.1(b), the fundraising representative may reallocate the surplus funds. The fundraising representative shall not reallocate funds so as to allow candidates seeking to extinguish outstanding debts to rely on the receipt of matching funds to pay the remainder of their debts; rather, all funds to which a participant is entitled under the allocation formula shall be deemed funds available to pay the candidate's outstanding campaign obligations as provided in 11 CFR 9034.5(c).

(iii) Reallocation shall be based upon the remaining participant's proportionate shares under the allocation formula. If reallocation results in a violation of a contributor's limit under 11 CFR 110.1, the fundraising representative shall return to the contributor the amount of the contribution that exceeds the limit.

(iv) Earmarked contributions which exceed the contributor's limit to the designated participant under 11 CFR part 110 may not be reallocated by the fundraising representative without the prior written permission of the contributor. A written instrument made payable to one of the participants shall be considered an earmarked contribution unless a written statement by the contributor indicates that it is intended for inclusion in the general proceeds of the fundraising activity.

(8) *Allocation of expenses and distribution of net proceeds.* (i) If participating committees are not affiliated as defined in 11 CFR 110.3 prior to the joint fundraising activity and are not committees of the same political party:

(A) After gross contributions are allocated among the participants under 11 CFR 9034.8(c)(7), the fundraising representative shall calculate each participant's share of expenses based on the percentage of the total receipts each participant had been allocated. To calculate each participant's net proceeds, the fundraising representative shall subtract the participant's share of expenses from the amount that participant has been allocated from gross proceeds.

(B) A participant may only pay expenses on behalf of another participant subject to the contribution limits of 11 CFR part 110. See also 11 CFR 9034.4(b)(6).

(C) The expenses from a series of fundraising events or activities shall be allocated among the participants on a per-event basis regardless of whether the participants change or remain the same throughout the series.

(ii) If participating committees are affiliated as defined in 11 CFR 110.3 prior to the joint fundraising activity or if participants are party committees of the same political party, expenses need not be allocated among those participants. Payment of such expenses by an unregistered committee or organization on behalf of an affiliated political committee may cause the unregistered organization to become a political committee.

(iii) Payment of expenses may be made from gross proceeds by the fundraising representative.

(9) *Reporting of receipts and disbursements.*— (i) *Reporting receipts.* (A) The fundraising representative shall report all funds received in the reporting period in which they are received. Each Schedule A filed by the fundraising representative under this section shall clearly indicate that the contributions reported on that schedule represent joint fundraising proceeds.

(B) After distribution of net proceeds, each participating political committee shall report its share of net proceeds received as a transfer-in from the fundraising representative. Each participating political committee shall also file a memo Schedule A itemizing its share of gross receipts as contributions from original contributors to the extent required under 11 CFR 104.3(a).

(ii) *Reporting disbursements.* The fundraising representative shall report all disbursements in the reporting period in which they are made. Each participant shall report in a memo Schedule B his or her total allocated share of these disbursements in the same reporting period in which net proceeds are distributed and reported and include the amount on page 4 of Form 3–P, under "Expenditures Subject to Limit."

§ 9034.9 Sale of assets acquired for fundraising purposes.

(a) *General.* A candidate may sell assets donated to the candidate's authorized committee(s) or otherwise acquired for fundraising purposes (See 11 CFR 9034.5(c)(2)), subject to the limitations and prohibitions of title 2, United States Code and 11 CFR parts 110 and 114.

(b) *Sale after end of matching payment period.* A candidate whose outstanding debts exceed his or her cash on hand after the end of the matching payment period as determined under 11 CFR 9032.6 may dispose of assets acquired for fundraising purposes in a sale to a wholesaler or other intermediary who will in turn sell such assets to the public, provided that the sale to the wholesaler or intermediary is an arms-length transaction. Sales made under this subsection will not be subject to the limitations and prohibitions of title 2, United States Code and 11 CFR parts 110 and 114.

PART 9035—EXPENDITURE LIMITATIONS

Authority: 26 U.S.C. 9035 and 9039(b).

§ 9035.1 Campaign expenditure limitation.

(a)(1) No candidate or his or her authorized committee(s) shall knowingly incur expenditures in connection with the candidate's campaign for nomination, which expenditures, in the aggregate, exceed $10,000,000 (as adjusted under 2 U.S.C. 441a(c)), except that the aggregate expenditures by a candidate in any one State shall not exceed the greater of: 16 cents (as adjusted under 2 U.S.C. 441a(c)) multiplied by the voting age population of the State (as certified under 2 U.S.C. 441a(e)); or $200,000 (as adjusted under 2 U.S.C. 441a(c)).

(2) The Commission will calculate the amount of expenditures attributable to the overall expenditure limit or to a particular state using the full amounts originally charged for goods and services rendered to the committee and not the amounts for which such obligations were settled and paid, unless the committee can demonstrate that the lower amount paid reflects a reasonable settlement of a bona fide dispute with the creditor.

(b) Each candidate receiving or expecting to receive matching funds under this subchapter shall also allocate his or her expenditures in accordance with the provisions of 11 CFR 106.2.

(c)(1) A candidate may exclude from the overall expenditure limitation of 11 CFR 9035.1 an amount equal to 10% of all salaries and overhead expenditures as an exempt legal and accounting compliance cost under 11 CFR 100.8(b)(15). For purposes of this section overhead expenditures include, but are not limited to rent, utilities, office equipment, furniture, supplies, and telephone base service charges as set forth at 11 CFR 106.2(b)(2)(iii)(A).

(i) If the candidate wishes to claim a larger compliance exemption for any person, the candidate shall establish allocation percentages for each individual who spends all or a portion of his or her time to perform duties which are considered compliance. The candidate shall keep detailed records to support the derivation of each percentage. Such records shall indicate which duties are considered compliance and the percentage of time each person spends on such activity. Alternatively, the Commission's Financial Control and Compliance Manual for Presidential Primary Candidates contains some other accepted allocation methods for calculating a compliance exemption.

(ii) Exempt compliance costs are those legal and accounting costs incurred solely to ensure compliance with 26 U.S.C. 9031 *et seq.*, 2 U.S.C. 431 *et seq.*, and 11 CFR ch. I, including the costs of preparing matching fund submissions and the costs of producing, delivering and explaining computerized information and materials provided pursuant to 11 CFR 9033.12 and explaining the operation of the computer system's software. The costs of preparing matching fund submissions shall be limited to those functions not required for general contribution processing and shall include the costs associated with: Generating the matching fund submission list and the matching fund computer tape or other form of magnetic media for each submission, edits of the contributor data base that are related to preparing a matching fund submission, making photocopies of contributor checks, and seeking additional documentation from contributors for matching purposes. The costs associated with general contribution processing shall include those normally performed for fundraising purposes, or for compliance with the recordkeeping and reporting requirements of 11 CFR part 100 *et seq.*, such as data entry, batching contributions for deposit, and preparation of FEC reports.

(2) A candidate may exclude from the overall expenditure limitation of 11 CFR 9035.1 the amount of exempt fundraising costs specified in 11 CFR 100.8(b)(21)(iii).

(d) The expenditure limitations of 11 CFR 9035.1 shall not apply to a candidate who does not receive matching funds at any time during the matching payment period.

§ 9035.2 Limitation on expenditures from personal or family funds.

(a)(1) No candidate who has accepted matching funds shall knowingly make expenditures from his or her personal funds, or funds of his or her immediate family, in connection with his or her campaign for nomination for election to the office of President which exceed $50,000, in the aggregate. This section shall not operate to prohibit any member of the candidate's immediate family from contributing his or her personal funds to the candidate, subject to the limitations of 11 CFR part 110. The provisions of this section also shall not limit the candidate's liability for, nor the candidate's ability to pay, any repayments required under 11 CFR part 9038. If the candidate or his or her committee knowingly incurs expenditures in excess of the limitations of 11 CFR 110.8(a), the Commission may seek civil penalties under 11 CFR part 111 in addition to any repayment determinations made on the basis of such excessive expenditures.

(2) Expenditures made using a credit card for which the candidate is jointly or solely liable will count against the limits of this section to the extent that the full amount due, including any finance charge, is not paid by the committee within 60 days after the closing date of the billing statement on which the charges first appear. For purposes of this section, the *closing date* shall be the date indicated on the billing statement which serves as the cutoff date for determining which charges are included on that billing statement.

(b) For purposes of this section, the term *immediate family* means a candidate, spouse, and any child, parent, grandparent, brother, half-brother, sister, or half-sister of the candidate, and the spouses of such persons.

(c) For purposes of this section, *personal funds* has the same meaning as specified in 11 CFR 110.10.

PART 9036—REVIEW OF SUBMISSION AND CERTIFICATION OF PAYMENTS BY COMMISSION

Authority: 26 U.S.C. 9036 and 9039(b).

§ 9036.1 Threshold submission.

(a) *Time for submission of threshold submission.* At any time after January 1 of the year immediately preceding the Presidential election year, the candidate may submit a threshold submission for matching fund payments in accordance with the format for such submissions set forth in 11 CFR 9036.1(b). The candidate may submit the threshold submission simultaneously with or subsequent to his or her submission of the candidate agreement and certifications required by 11 CFR 9033.1 and 9033.2.

(b) *Format for threshold submission.* (1) For each State in which the candidate certifies that he or she has met the requirements of the certifications in 11 CFR 9033.2(b), the candidate shall submit an alphabetical list of contributors showing:

(i) Each contributor's full name and residential address;

(ii) The occupation and name of employer for individuals whose aggregate contributions exceed $200 in the calendar year;

(iii) The date of deposit of each contribution into the designated campaign depository;

(iv) The full dollar amount of each contribution submitted for matching purposes;

(v) The matchable portion of each contribution submitted for matching purposes;

(vi) The aggregate amount of all matchable contributions from that contributor submitted for matching purposes;

(vii) A notation indicating which contributions were received as a result of joint fundraising activities.

(2) For each list of contributors generated directly or indirectly from computerized files or computerized records, the candidate shall submit computerized magnetic media, such as magnetic tapes or magnetic diskettes, containing the information required by 11 CFR 9036.1(b)(1) in accordance with 11 CFR 9033.12.

(3) The candidate shall submit a full-size photocopy of each check or written instrument and of supporting documentation in accordance with 11 CFR 9034.2 for each contribution that the candidate submits to establish eligibility for matching funds. For purposes of the threshold submission, the photocopies shall be segregated alphabetically by contributor within each State, and shall be accompanied by and referenced to copies of the relevant deposit slips.

(4) The candidate shall submit bank documentation, such as bank-validated deposit slips or unvalidated deposit slips accompanied by the relevant bank statements, which indicate that the contributions submitted were deposited into a designated campaign depository.

(5) For each State in which the candidate certifies that he or she has met the requirements to establish eligibility, the candidate shall submit a listing, alphabetically by contributor, of all checks returned by the bank to date as unpaid (e.g., stop payments, non-sufficient funds) regardless of whether the contribution was submitted for matching. This listing shall be accompanied by a full-size photocopy of each unpaid check, and copies of the associated debit memo and bank statement.

(6) For each State in which the candidate certifies that he or she has met the requirements to establish eligibility, the candidate shall submit a listing, in alphabetical order by contributor, of all contributions that were refunded to the contributor, regardless of whether the contributions were submitted for matching. For each refunded contribution, the listing shall state the contributor's full name and address, the deposit date and batch number, an indication of which matching fund submission the contribution was included in, if any, and the amount and date of the refund. The listing shall be accompanied by a full-sized photocopy of each refunded contributor check.

(7) The candidate shall submit all contributions in accordance with the Federal Election Commission's Guideline for Presentation in Good Order.

(8) Contributions that are not submitted in compliance with this section shall not count toward the threshold amount.

(c) *Threshold certification by Commission.* (1) After the Commission has determined under 11 CFR 9033.4 that the candidate has satisfied the eligibility and certification requirements of 11 CFR 9033.1 and 9033.2, the Commission will notify the candidate in writing that the candidate is eligible to receive primary matching fund payments as provided in 11 CFR part 9034.

(2) If the Commission makes a determination of a candidate's eligibility under 11 CFR 9036.1(a) in a Presidential election year, the Commission shall certify to the Secretary, within 10 calendar days after the Commission has made its determination, the amount to which the candidate is entitled.

(3) If the Commission makes a determination of a candidate's eligibility under 11 CFR 9036.1(a) in the year preceding the Presidential election year, the Commission will notify the candidate that he or she is eligible to receive matching fund payments; however, the Commission's determination will not result in a payment of funds to the candidate until after January 1 of the Presidential election year.

§ 9036.2 Additional submissions for matching fund payments.

(a) *Time for submission of additional submissions.* The candidate may submit additional submissions for payments to the Commission on dates to be determined and published by the Commission.

(b) *Format for additional submissions.* The candidate may obtain additional matching fund payments subsequent to the Commission's threshold certification and payment of primary matching funds to the candidate by filing an additional submission for payment. All additional submissions for payments filed by the candidate shall be made in accordance with the Federal Election Commission's Guideline for Presentation in Good Order.

(1) The first submission for matching funds following the candidate's threshold submission shall contain all the matchable contributions included in the threshold submission and any additional contributions to be submitted for matching in that submission. This submission shall contain all the information required for the threshold submission except that:

(i) The candidate is not required to resubmit the candidate agreement and certifications of 11 CFR 9033.1 and 9033.2;

(ii) The candidate is required to submit an alphabetical list of contributors, but not segregated by State as required in the threshold submission;

(iii) The candidate is required to submit a listing, alphabetical by contributor, of all checks returned unpaid, but not segregated by State as required in the threshold submission;

(iv) The candidate is required to submit a listing, in alphabetical order by contributor, of all contributions refunded to the contributor but not segregated by State as required in the threshold submission.

(v) The occupation and employer's name need not be disclosed on the contributor list for individuals whose aggregate contributions exceed $200 in the calendar year, but such information is subject to the recordkeeping and reporting requirements of 2 U.S.C. 432(c)(3), 434(b)(3)(A) and 11 CFR 102.9(a)(2), 104.3(a)(4)(i); and

(vi) The photocopies of each check or written instrument and of supporting documentation shall either be alphabetized and referenced to copies of the relevant deposit slip, but not segregated by State as required in the threshold submission; or such photocopies may be batched in deposits of 50 contributions or less and cross-referenced by deposit number and sequence number within each deposit on the contributor list.

(2) Following the first submission under 11 CFR 9036.2(b)(1), candidates may request additional matching funds on dates prescribed by the Commission by making a letter request in lieu of making a full submission as required under 11 CFR 9036.2(b)(1), however, letter requests may not be submitted

after the candidate's date of ineligibility. Letter requests shall state an amount of matchable contributions not previously submitted for matching and shall provide bank documentation, such as bank-validated deposit slips or unvalidated deposit slips accompanied by the relevant bank statement, demonstrating that the committee has received the funds for which matching payments are requested. The amount requested for matching may include contributions received up to the last business day preceding the date of the request. On the next submission date as designated for that committee after a letter request has been made, the committee shall submit the documentation required under 11 CFR 9036.2(b)(1) for all contributions included in the letter request, as well as any contributions submitted for matching in that full submission. A committee may not submit two consecutive letter requests, but the committee may choose to make a full regular submission on a date designated by the Commission as a letter request date for that committee.

(c) *Certification of additional payments by Commission.* (1)(i) When a candidate who is eligible under 11 CFR 9033.4 submits an additional submission for payment in the Presidential election year, the Commission may certify to the Secretary within 5 business days after the Commission's receipt of information submitted by the candidate under 11 CFR 9036.2(a), an amount based on the holdback procedure described in the Federal Election Commission's Guideline for Presentation in Good Order. If the candidate makes a letter request, the Commission may certify to the Secretary an amount which is less than that requested based upon the ratio of verified matchable contributions to total deposits for that committee in the committee's last regular submission.

(ii) The Commission will certify to the Secretary any additional amount to which the eligible candidate is entitled, if any, within 20 business days after the Commission's receipt of information submitted by the candidate under 11 CFR 9036.2(a), unless the projected dollar value of the nonmatchable contributions contained in the submission exceeds 10% of the amount requested. In the latter case, the Commission will certify any additional amount within 25 business days. See 11 CFR 9036.4 for Commission procedures for certification of additional payments.

(2) After a candidate's date of ineligibility, the Commission will certify to the Secretary, within 20 business days after receipt of a submission by the candidate under 11 CFR 9036.2(a), an amount to which the ineligible candidate is entitled in accordance with 11 CFR 9034.1(b), unless the projected dollar value of the nonmatchable contributions contained in the submission exceeds 10% of the amount requested. In the latter case, the Commission will certify any amount to which the ineligible candidate is entitled within 25 business days.

(d) *Additional submissions submitted in non-Presidential election year.* The candidate may submit additional contributions for review during the year preceding the presidential election year; however, the amount of each submission made during this period must exceed $50,000. Additional submissions filed by a candidate in a non-Presidential election year will not result in payment of matching funds to the candidate until after January 1 of the Presidential election year.

§ 9036.3 Submission of errors and insufficient documentation.

Contributions which are otherwise matchable may be rejected for matching purposes because of submission errors or insufficient supporting documentation. Contributions, other than those defined in 11 CFR 9034.3 or in the form of money orders, cashier's checks, or similar negotiable instruments, may become matchable if there is a proper resubmission in accordance with 11 CFR 9036.5 and 9036.6. Insufficient documentation or submission errors include but are not limited to:

(a) Discrepancies in the written instrument, such as:

(1) Instruments drawn on other than personal accounts of contributors and not signed by the contributing individual;

(2) Signature discrepancies; and

(3) Lack of the contributor's signature, the amount or date of the contribution, or the listing of the committee or candidate as payee.

(b) Discrepancies between listed contributions and the written instrument or supporting documentation, such as:

(1) The listed amount requested for matching exceeds the amount contained on the written instrument;

(2) A written instrument has not been submitted to support a listed contribution;

(3) The submitted written instrument cannot be associated either by accountholder identification or signature with the listed contributor; or

(4) A discrepancy between the listed contribution and the supporting bank documentation or the bank documentation is omitted.

(c) Discrepancies within or between contributor lists submitted, such as:

(1) The address of the contributor is omitted or incomplete or the contributor's name is alphabetized incorrectly, or more than one contributor is listed per item;

(2) A discrepancy in aggregation within or between submissions which results in a request that more than $250 be matched for that contributor, or a listing of a contributor more than once within the same submission; or

(3) A written instrument has been previously submitted and matched in full or is listed twice in the same submission.

(d) The omission of information, supporting statements, or documentation required by 11 CFR 9034.2.

§ 9036.4 Commission review of submissions.

(a) *Non-acceptance of submission for review of matchability.* The Commission will make an initial review of each submission made under 11 CFR part 9036 to determine if it substantially meets the format requirements of 11 CFR 9036.1(b) and 9036.2(b) and the Federal Election Commission's Guideline for Presentation in Good Order. If the Commission determines that a submission does not substantially meet these requirements, it will not review the matchability of the contributions contained therein. In such a case, the Commission will return the submission to the candidate and request that it be corrected in accordance with the format requirements. If the candidate makes a corrected submission within 3 business days after the Commission's return of the original, the Commission will review the corrected submission prior to the next regularly-scheduled submission date. Corrected submissions made after this three-day period will be reviewed subsequent to the next regularly-scheduled submission date.

(b) *Acceptance of submission for review of matchability.* If the Commission determines that a submission made under 11 CFR part 9036 satisfies the format requirements of 11 CFR 9036.1(b) and 9036.2(b) and the Federal Election Commission's Guideline for Presentation in Good Order, it will review the matchability of the contributions contained therein. The Commission, in conducting its review, may utilize statistical sampling techniques. Based on the results of its review, the Commission may calculate a matchable amount for the submission which is less than the amount requested by the candidate. If the Commission certifies for payment to the Secretary an amount that is less than the amount requested by the candidate in a particular submission, or reduces the amount of a subsequent certification to the Secretary by adjusting a previous certification made under 11 CFR 9036.2(c)(1), the Commission will notify the candidate in writing of the following:

(1) The amount of the difference between the amount requested and the amount to be certified by the Commission;

(2) The amount of each contribution and the corresponding contributor's name for each contribution that the Commission has rejected as non-matchable and the reason that it is not matchable; or if statistical sampling is used, the estimated amount of contributions by type and the reason for rejection;

(3) The amount of contributions that have been determined to be matchable and that the Commission will certify to the Secretary for payment; and

(4) A statement that the candidate may supply the Commission with additional documentation or other information in the resubmission of any rejected contribution under 11 CFR 9036.5 in order to show that a rejected contribution is matchable under 11 CFR 9034.2.

(c) *Adjustment of amount to be certified by Commission.* The candidate shall notify the Commission as soon as possible if the candidate or the candidate's authorized committee(s) has knowledge that a contribution submitted for matching does not qualify under 11 CFR 9034.2 as a matchable contribution, such as a check returned to the committee for insufficient funds or a contribution that has been refunded, so that the Commission may properly adjust the amount to be certified for payment.

(d) *Commission audit of submissions.* The Commission may determine, for the reasons stated in 11 CFR part 9039, that an audit and examination of contributions submitted for matching payment is warranted. The audit and examination shall be conducted in accordance with the procedures of 11 CFR part 9039.

§ 9036.5 Resubmissions.

(a) *Alternative resubmission methods.* Upon receipt of the Commission's notice of the results of the submission review pursuant to 11 CFR 9036.4(b), a candidate may choose to:

(1) Resubmit the entire submission; or

(2) Make a written request for the identification of the specific contributions that were rejected for matching, and resubmit those specific contributions.

(b) *Time for presentation of resubmissions.* If the candidate chooses to resubmit any contributions under 11 CFR 9036.5(a), the contributions shall be resubmitted on dates to be determined and published by the Commission. The candidate may not make any resubmissions later than the first Tuesday in September of the year following the Presidential election year.

(c) *Format for resubmissions.* All resubmissions filed by the candidate shall be made in accordance with the Federal Election Commission's Guideline for Presentation in Good Order. In making a presentation of resubmitted contributions, the candidate shall follow the format requirements as specified in 11 CFR 9036.2(b)(1), except that:

(1) The candidate need not provide photocopies of written instruments, supporting documentation and bank documentation unless it is necessary to supplement the original documentation.

(2) Each resubmitted contribution shall be referenced to the submission in which it was first presented.

(3) Each list of resubmitted contributions shall reflect the aggregate amount of contributions submitted for matching from each contributor as of the date of the original submission.

(4) Each list of resubmitted contributions shall reflect the aggregate amount of contributions submitted for matching from each contributor as of the date of the resubmission.

(5) Each list of resubmitted contributions shall only contain contributions previously submitted for matching and no new or additional contributions.

(6) Each resubmission shall be accompanied by a statement that the candidate has corrected his or her contributor records (including the data base for those candidates maintaining their contributor list on computer).

(d) *Certification of resubmitted contributions.* Contributions that the Commission determines to be matchable will be certified to the Secretary within 15 business days. If the candidate chooses to request the specific contributions rejected for matching pursuant to 11 CFR 9036.5(a)(2), the amount certified shall equal only the matchable amount of the particular contribution that meets the standards on resubmission, rather than the amount projected as being nonmatchable based on that contribution due to the sampling techniques used in reviewing the original submission.

(e) *Initial determinations.* If the candidate resubmits a contribution for matching and the Commission determines that the rejected contribution is still non-matchable, the Commission will notify the candidate in writing of its determination. The Commission will advise the candidate of the legal and factual reasons for its determination and of the evidence on which that determination is based. The candidate may submit written legal or factual materials to demonstrate that the contribution is matchable within 30 calendar days after service of the Commission's notice. Such materials may be submitted by counsel if the candidate so desires.

(f) *Final determinations.* The Commission will consider any written legal or factual materials timely submitted by the candidate in making its final determination. A final determination by the Commission that a contribution is not matchable will be accompanied by a written statement of reasons for the Commission's action. This statement will explain the reasons underlying the Commission's determination and will summarize the results of any investigation upon which the determination is based.

§ 9036.6 Continuation of certification.

Candidates who have received matching funds and who are eligible to continue to receive such funds may continue to submit additional submissions for payment to the Commission on dates specified in the Federal Election Commission's Guideline for Presentation in Good Order. The Commission will notify each candidate of the last date on which contributions may be submitted for the first time for matching in the year following the election. The last date for first-time submissions will be either the last Monday in February or the second Monday in March of the year following the election, depending on the submission schedule the Commission has designated for the candidate. No contribution will be matched if it is submitted after the last submission date designated for that candidate, regardless of the date the contribution was deposited.

PART 9037—PAYMENTS AND REPORTING

Sec.

Authority: 26 U.S.C. 9037 and 9039(b).

§ 9037.1 Payments of Presidential primary matching funds.

Upon receipt of a written certification from the Commission, but not before the beginning of the matching payment period, the Secretary will promptly transfer the amount certified from the matching payment account to the candidate.

§ 9037.2 Equitable distribution of funds.

In making such transfers to candidates of the same political party, the Secretary will seek to achieve an equitable distribution of funds available in the matching payment account, and the Secretary will take into account, in seeking to achieve an equitable distribution of funds available in the matching payment account, the sequence in which such certifications are received.

§ 9037.3 Deposits of Presidential primary matching funds.

Upon receipt of any matching funds, the candidate shall deposit the full amount received into a checking account maintained by the candidate's principal campaign committee in the depository designated by the candidate. The account(s) shall be maintained at a State bank, federally chartered depository institution or other depository institution, the deposits of which are insured by the Federal Deposit Insurance Corporation.

PART 9038—EXAMINATION AND AUDITS

Authority: 26 U.S.C. 9038 and 9039(b).

§ 9038.1 Audit.

(a) *General.* (1) The Commission will conduct an audit of the qualified campaign expenses of every candidate and his or her authorized committee(s) who received Presidential primary matching funds. The audit may be conducted at any time after the date of the candidate's ineligibility.

(2) In addition, the Commission may conduct other examinations and audits from time to time as it deems necessary to carry out the provisions of this subchapter.

(3) Information obtained pursuant to any audit and examination conducted under 11 CFR 9038.1(a) (1) and (2) may be used by the Commission as the basis, or partial basis, for its repayment determinations under 11 CFR 9038.2.

(b) *Conduct of fieldwork.* (1) If the candidate or the candidate's authorized committee does not maintain or use any computerized information containing the data listed in 11 CFR 9033.12, the Commission will give the candidate's authorized committee at least two weeks' notice of the Commission's intention to commence fieldwork on the audit and examination. The fieldwork shall be conducted at a site provided by the committee. If the candidate or the candidate's authorized committee maintains or uses computerized information containing any of the data listed in 11 CFR 9033.12, the Commission generally will request such information prior to commencement of audit fieldwork. Such request will be made in writing. The committee shall produce the computerized information no later than 15 calendar days after service of such request. Upon receipt of the computerized information requested and compliance with the technical specifications of 11 CFR 9033.12(b), the Commission will give the candidate's authorized committee at least two weeks' notice of the Commission's intention to commence fieldwork on the audit and examination. The fieldwork shall be conducted at a site provided by the committee. During or after audit fieldwork, the Commission may request additional or updated computerized information which expands the coverage dates of computerized information previously provided, and which may be used for purposes including, but not limited to, updating a statement of net outstanding campaign obligations, or updating the amount chargeable to a state expenditure limit. During or after audit fieldwork, the Commission may also request additional computerized information which was created by or becomes available to the committee and that is of assistance in the Commission's audit. The committee shall produce the additional or updated computerized information no later than 15 calendar days after service of the Commission's request.

(i) *Office space and records.* On the date scheduled for the commencement of fieldwork, the candidate or his or her authorized committee(s) shall provide Commission staff with office space and committee records in accordance with the candidate and committee agreement under 11 CFR 9033.1(b)(6).

(ii) *Availability of committee personnel.* On the date scheduled for the commencement of fieldwork, the candidate or his or her authorized committee(s) shall have committee personnel present at the site of the fieldwork. Such Personnel shall be familiar with the committee's records and operation and shall be available to Commission staff to answer questions and to aid in locating records.

(iii) *Failure to provide staff, records or office space.* If the candidate or his or her authorized committee(s) fail to provide adequate office space, personnel or committee records, the Commission may seek judicial intervention under 2 U.S.C. 437d or 26 U.S.C. 9040(c) to enforce the candidate and committee agreement made under 11 CFR 9033.1(b). Before seeking judicial intervention, the Commission will notify the candidate of his or her failure to comply with the agreement and will recommend corrective action to bring the candidate into compliance. Upon receipt of the Commission's notification, the candidate will have 10 calendar days in which to take the corrective action indicated or to otherwise demonstrate to the Commission in writing that he or she is complying with the candidate and committee agreement.

(iv) If, in the course of the audit process, a dispute arises over the documentation sought or other requirements of the candidate agreement, the candidate may seek review by the Commission of the issues raised. To seek review, the candidate shall submit a written statement, within 10 calendar days after the disputed Commission staff request is made, describing the dispute and indicating the candidate's proposed alternative(s).

(v) If the candidate or his or her authorized committee fails to produce particular records, materials, evidence or other information requested by the Commission, the Commission may issue an order pursuant to 2 U.S.C. 437d(a)(1) or a subpoena or subpoena duces tecum pursuant to 2 U.S.C. 437(d)(a)(3). The procedures set forth in 11 CFR 111.11 through 111.15, as appropriate, shall apply to the production of such records, materials, evidence or other information as specified in the order, subpoena or subpoena duces tecum.

(2) Fieldwork will include the following steps designed to keep the candidate and committee informed as to the progress of the audit and to expedite the process:

(i) *Entrance conference.* At the outset of the fieldwork, Commission staff will hold an entrance conference, at which the candidate's representatives will be advised of the purpose of the audit and the general procedures to be followed. Future requirements of the candidate and his or her authorized committee, such as possible repayments to the United States Treasury, will also be discussed. Committee representatives shall provide information and records necessary to conduct the audit, and Commission staff will be available to answer committee questions.

(ii) *Review of records.* During the fieldwork, Commission staff will review committee records and may conduct interviews of committee personnel. Commission staff will be available to explain aspects of the audit and examination as it progresses. Additional meetings between Commission staff and committee personnel may be held from time to time during the fieldwork to discuss possible audit findings and to resolve issues arising during the course of the audit.

(iii) *Exit conference.* At the conclusion of the fieldwork, Commission staff will hold an exit conference to discuss with committee representatives the staff's preliminary findings and recommendations which the Commission staff anticipates that it may present to the Commission for approval. Commission staff will advise committee representatives at this conference of the projected timetable regarding the issuance of an audit report, the committee's opportunity to respond thereto, and the Commission's initial and final repayment determinations under 11 CFR 9038.2.

(3) Commission staff may conduct additional fieldwork after the completion of the fieldwork conducted pursuant to 11 CFR 9038.1(b) (1) and (2). Factors that may necessitate such follow-up fieldwork include, but are not limited to, the following:

(i) Committee responses to audit findings;

(ii) Financial activity of the committee subsequent to the fieldwork conducted pursuant to 11 CFR 9038.1(b)(1);

(iii) Committee responses to Commission repayment determinations made under 11 CFR 9038.2.

(4) The Commission will notify the candidate and his or her authorized committee if follow-up fieldwork is necessary. The provisions of 11 CFR 9038.1(b) (1) and (2) shall apply to any additional fieldwork conducted.

(c) *Preparation of interim audit report.* (1) After the completion of the fieldwork conducted pursuant to 11 CFR 9038.1(b)(1), the Commission will issue an interim audit report to the candidate and his or her authorized committee. The interim audit report may contain Commission findings and recommendations regarding one or more of the following areas:

(i) An evaluation of procedures and systems employed by the candidate and committee to comply with applicable provisions of the Federal Election Campaign Act, Primary Matching Payment Account Act and Commission regulations;

(ii) Eligibility of the candidate to receive primary matching payments;

(iii) Accuracy of statements and reports filed with the Commission by the candidate and committee;

(iv) Compliance of the candidate and committee with applicable statutory and regulatory provisions except for those instances where the Commission has instituted an enforcement action on the matter(s) under the provisions of 2 U.S.C. 437g and 11 CFR part 111; and

(v) Preliminary calculations regarding future repayments to the United States Treasury.

(2) The candidate and his or her authorized committee will have an opportunity to submit, in writing, within 30 calendar days after service of the interim report legal and factual materials disputing or commenting on the contents of the interim report. Such materials may be submitted by counsel if the candidate so desires.

(3) The Commission will consider any written legal and factual materials submitted by the candidate or his or her authorized committee in accordance with 11 CFR 9038.1(c)(2) before approving and issuing an audit report to be released to the public. The contents of the publicly-released audit report may differ from that of the interim report since the Commission will consider timely submissions of legal and factual materials by the candidate or committee in response to the interim report.

(d) *Preparation of publicly-released audit report.* An audit report prepared subsequent to an interim report will be publicly released pursuant to 11 CFR 9038.1(e). This report will contain Commission findings and recommendations addressed in the interim audit report but may contain adjustments based on the candidate's response to the interim report. In addition, this report will contain an initial repayment determination made by the Commission pursuant to 11 CFR 9038.2(c)(1) in lieu of the preliminary calculations set forth in the interim report.

(e) *Public release of audit report.* (1) After the candidate and committee have had an opportunity to respond to a written interim report of the Commission, the Commission will make public the audit report prepared subsequent to the interim report, as provided in 11 CFR 9038.1(d).

(2) If the Commission determines, on the basis of information obtained under the audit and examination process, that certain matters warrant enforcement under 2 U.S.C. 437g and 11 CFR part 111, those matters will not be contained in the publicly-released report. In such cases, the audit report will indicate that certain other matters have been referred to the Commission's Office of General Counsel.

(3) The Commission will provide the candidate and the committee with copies of the agenda document containing those portions of the final audit report to be considered in open session 24 hours prior to releasing the agenda document to the public. The Commission will also provide the candidate and committee with copies of the final audit report 24 hours before releasing the report to the public.

(4) Addenda to the audit report may be issued from time to time as circumstances warrant and as additional information becomes available. Such addenda may be based, in part, on follow-up fieldwork conducted under 11 CFR 9038.1(b)(3), and will be placed on the public record.

§ 9038.2 Repayments.

(a) *General.* (1) A candidate who has received payments from the matching payment account shall pay the United States Treasury any amounts which the Commission determines to be repayable under this section. In making repayment determinations under this section, the Commission may utilize information obtained from audits and examinations conducted pursuant to 11 CFR 9038.1 and part 9039 or otherwise obtained by the Commission in carrying out its responsibilities under this subchapter.

(2) The Commission will notify the candidate of any repayment determinations made under this section as soon as possible, but not later than 3 years after the end of the matching payment period. The Commission's issuance of an interim audit report to the candidate under 11 CFR 9038.1(c) will constitute notification for purposes of the 3 year period.

(3) Once the candidate receives notice of the Commission's final repayment determination under this section, the candidate should give preference to the repayment over all other outstanding obligations of his or her committee, except for any federal taxes owed by the committee.

(b) *Bases for repayment*—(1) *Payments in excess of candidate's entitlement.* The Commission may determine that certain portions of the payments made to a candidate from the matching payment account were in excess of the aggregate amount of payments to which such candidate was entitled. Examples of such excessive payments include, but are not limited to, the following:

(i) Payments made to the candidate after the candidate's date of ineligibility where it is later determined that the candidate had no net outstanding campaign obligations as defined in 11 CFR 9034.5;

(ii) Payments or portions of payments made to the candidate which are later determined to have been excessive due to the operation of the Commission's expedited payment procedures as set forth in the Federal Election Commission's Guideline for Presentation in Good Order;

(iii) Payments or portions of payments made on the basis of matched contributions later determined to have been non-matchable;

(iv) Payments or portions of payments made to the candidate which are later determined to have been excessive due to the candidate's failure to include funds received by a fundraising representative committee under 11 CFR 9034.8 on the candidate's statement of net outstanding campaign obligations under 11 CFR 9034.5; and

(v) Payments or portions of payments made to the candidate on the basis of the debts reflected in the candidate's statement of net outstanding campaign obligations, which debts are later settled for an amount less than that stated in the statement of net outstanding campaign obligations.

(2) *Use of funds for non-qualified campaign expenses.* (i) The Commission may determine that amount(s) of any payments made to a candidate from the matching payment account were used for purposes other than those set forth in paragraphs (b)(2)(i) (A)–(C) of this section:

(A) Defrayal of qualified campaign expenses;

(B) Repayment of loans which were used to defray qualified campaign expenses; and

(C) Restoration of funds (other than contributions which were received and expended to defray qualified campaign expenses) which were used to defray qualified campaign expenses.

(ii) Examples of Commission repayment determinations under 11 CFR 9038.2(b)(2) include, but are not limited to, the following:

(A) Determinations that a candidate, a candidate's authorized committee(s) or agents have made expenditures in excess of the limitations set forth in 11 CFR part 9035;

(B) Determinations that funds described in 11 CFR 9038.2(b)(2)(i) were expended in violation of state or federal law;

(C) Determinations that funds described in 11 CFR 9038.2(b)(2)(i) were expended for expenses resulting from a violation of state or federal law, such as the payment of fines or penalties; and

(D) Determinations that funds described in 11 CFR 9038.2(b)(2)(i) were expended for costs associated with continuing to campaign after the candidate's date of ineligibility.

(iii) The amount of any repayment sought under this section shall bear the same ratio to the total amount determined to have been used for non-qualified campaign expenses as the amount of matching funds certified to the candidate bears to the total deposits, as of the candidate's date of ineligibility. Total deposits is defined in accordance with 11 CFR 9038.3(c)(2). For the purpose of seeking repayment for non-qualified campaign expenses from committees that have received matching fund payments after the candidate's date of ineligibility, the Commission will review committee expenditures to determine at what point committee accounts no longer contain matching funds. In doing this, the Commission will review committee expenditures from the date of the last matching fund payment to which the candidate was entitled, using the assumption that the last payment has been expended on a last-in, first-out basis.

(iv) Repayment determinations under 11 CFR 9038.2(b)(2) will include all non-qualified campaign expenses paid before the point when committee accounts no longer contain matching funds, including non-qualified campaign expenses listed on the candidate's statement of net outstanding campaign obligations that may result in a separate repayment determination under 11 CFR 9038.2(b)(1).

(v) If a candidate or a candidate's authorized committee(s) exceeds both the overall expenditure limitation and one or more State expenditure limitations, as set forth at 11 CFR 9035.1(a), the repayment determination under 11 CFR 9038.2(b)(2)(ii)(A) shall be based on only the larger of either the amount exceeding the State expenditure limitation(s) or the amount exceeding the overall expenditure limitation.

(3) *Failure to provide adequate documentation.* The Commission may determine that amount(s) spent by the candidate, the candidate's authorized committee(s), or agents were not documented in accordance with 11 CFR 9033.11. The amount of any repayment sought under this section shall be determined by using the formula set forth in 11 CFR 9038.2(b)(2)(iii).

(4) *Surplus.* The Commission may determine that the candidate's net outstanding campaign obligations, as defined in 11 CFR 9034.5, reflect a surplus. The Commission may determine that the net income derived from the investment of surplus public funds after the candidate's date of ineligibility, less Federal, State and local taxes paid on such income, is also repayable.

(c) *Repayment determination procedures.* Commission repayment determinations will be made in accordance with the procedures set forth at 11 CFR 9038.2(c) (1) through (4) of this section.

(1) *Initial determination.* The Commission will provide the candidate with a written notice of its initial repayment determination(s). This notice will be included in the Commission's publicly-released audit report, pursuant to 11 CFR 9038.1(d), and will set forth the legal and factual reasons for such determination(s). Such notice will also advise the candidate of the evidence upon which any such determination is based. If the candidate does not dispute an initial repayment determination of the Commission within 30 calendar days after service of the notice, such initial determination will be considered a final determination of the Commission.

(2) *Submission of written materials.* If the candidate disputes the Commission's initial repayment determination(s), he or she shall have an opportunity to submit in writing, within 30 calendar days after service of the Commission's notice, legal and factual materials to demonstrate that no repayment, or a lesser repayment, is required. The Commission will consider any written legal and factual materials submitted by the candidate within this 30-day period in making its final repayment determination(s). Such materials may be submitted by counsel if the candidate so desires.

(3) *Oral presentation.* A candidate who has submitted written materials under 11 CFR 9038.2(c)(2) may request that the Commission provide such candidate with an opportunity to address the Commission in open session. If the Commission decides by an affirmative vote of four (4) of its members to grant the candidate's request, it will inform the candidate of the date and time set for the oral presentation. At the date and time set by the Commission, the candidate or candidate's designated representative will be allotted an amount of time in which to make an oral presentation to the Commission based upon the legal and factual materials submitted under 11 CFR 9038.2(c)(2). The candidate or representative will also have the opportunity to answer any questions

from individual members of the Commission.

(4) *Final determination.* In making its final repayment determination(s), the Commission will consider any submission made under 11 CFR 9038.2(c)(2) and any oral presentation made under 11 CFR 9038.2(c)(3). A final determination that a candidate must repay a certain amount will be accompanied by a written statement of reasons for the Commission's actions. This statement will explain the reasons underlying the Commission's determination and will summarize the results of any investigation upon which the determination is based.

(d) *Repayment period.* (1) Within 90 calendar days after service of the notice of the Commission's initial repayment determination(s), the candidate shall repay to the Secretary amounts which the Commission has determined to be repayable. Upon application by the candidate, the Commission may grant an extension of up to 90 calendar days in which to make repayment.

(2) If the candidate submits written materials under 11 CFR 9038.2(c)(2) disputing the Commission's initial repayment determination(s), the time for repayment will be suspended until the Commission makes its final repayment determination(s). Within 30 calendar days after service of the notice of the Commission's final repayment determination(s), the candidate shall repay to the Secretary amounts which the Commission has determined to be repayable. Upon application by the candidate, the Commission may grant an extension of up to 90 days in which to make repayment.

(e) *Computation of time.* The time periods established by this section shall be computed in accordance with 11 CFR 111.2.

(f) *Additional repayments.* Nothing in this section will prevent the Commission from making additional repayment determinations on one or more of the bases set forth at 11 CFR 9038.2(b) after it has made a final determination on any such basis. The Commission may make additional repayment determinations where there exist facts not used as the basis for a previous final determination. Any such additional repayment determination will be made in accordance with the provisions of this section.

(g) *Newly-discovered assets.* If, after any initial or final repayment determination made under this section, a candidate or his or her authorized committee(s) receives or becomes aware of assets not previously included in any statement of net outstanding campaign obligations submitted pursuant to 11 CFR 9034.5, the candidate or his or her authorized committee(s) shall promptly notify the Commission of such newly-discovered assets. Newly-discovered assets may include refunds, rebates, late-arriving receivables, and actual receipts for capital assets in excess of the value specified in any previously-submitted statement of net outstanding campaign obligations. Newly-discovered assets may serve as a basis for additional repayment determinations under 11 CFR 9038.2(f).

(h) *Petitions for rehearing; stays pending appeal.* The candidate may file a petition for rehearing of a final repayment determination in accordance with 11 CFR 9038.5(a). The candidate may request a stay of a final repayment determination in accordance with 11 CFR 9038.5(c) pending the candidate's appeal of that repayment determination.

§ 9038.3 Liquidation of obligations; repayment.

(a) The candidate may retain amounts received from the matching payment account for a period not exceeding 6 months after the matching payment period to pay qualified campaign expenses incurred by the candidate.

(b) After all obligations have been liquidated, the candidate shall so inform the Commission in writing.

(c)(1) If on the last day of candidate eligibility the candidate's net outstanding campaign obligations, as defined in 11 CFR 9034.5, reflect a surplus, the candidate shall within 30 calendar days of the ineligibility date repay to the Secretary an amount which represents the amount of matching funds contained in the candidate's surplus. The amount shall be an amount equal to that portion of the surplus which bears the same ratio to the total surplus that the total amount received by the candidate from the matching payment account bears to the total deposits made to the candidate's accounts.

(2) For purposes of this subsection, total deposits means all deposits to all candidate accounts minus transfers between accounts, refunds, rebates, reimbursements, checks returned for insufficient funds, proceeds of loans and other similar amounts.

(3) Notwithstanding the payment of any amounts to the United States Treasury under this section, the Commission may make surplus repayment determination(s) which require repayment in accordance with 11 CFR 9038.2.

§ 9038.4 Extensions of time.

(a) It is the policy of the Commission that extensions of time under 11 CFR part 9038 shall not be routinely granted.

(b) Whenever a candidate has a right or is required to take action within a period of time prescribed by 11 CFR part 9038 or by notice given thereunder, the candidate may apply in writing to the Commission for an extension of time in which to exercise such right or take such action. The candidate shall demonstrate in the application for extension that good cause exists for his or her request.

(c) An application for extension of time shall be made at least 7 calendar days prior to the expiration of the time period for which the extension is sought. The Commission may, upon a showing of good cause, grant an extension of time to a candidate who has applied for such extension in a timely manner. The length of time of any extension granted hereunder will be decided by the Commission and may be less than the amount of time sought by the candidate in his or her application.

(d) If a candidate fails to seek an extension of time, exercise a right or take a required action prior to the expiration of a time period prescribed by 11 CFR part 9038 the Commission may, on the candidate's showing of excusable neglect:

(1) Permit such candidate to exercise his or her right(s), or take such required action(s) after the expiration of the prescribed time period; and

(2) Take into consideration any information obtained in connection with the exercise of any such right or taking of any such action before making decisions or determinations under 11 CFR part 9038.

§ 9038.5 Petitions for rehearing; stays of repayment determinations.

(a) *Petitions for rehearing.* (1) Following the Commission's final determination under 11 CFR 9033.10 or 9034.5(g) or the Commission's final repayment determination under 11 CFR 9038.2(c)(4), the candidate may file a petition for rehearing setting forth the relief desired and the legal and factual basis in support. To be considered by the Commission, petitions for rehearing must:

(i) Be filed within 20 calendar days after service of the Commission's final determination;

(ii) Raise new questions of law or fact that would materially alter the Commission's final determination; and

(iii) Set forth clear and convincing grounds why such questions were not and could not have been presented during the earlier determination process.

(2) If a candidate files a timely petition under this section challenging a Commission final repayment determination, the time for repayment of

the amount at issue will be suspended until the Commission serves notice on the candidate of its determination on the petition. The time periods for making repayment under 11 CFR 9038.2(d)(2) shall apply to any amounts determined to be repayable following the Commission's consideration of a petition for rehearing under this section.

(b) *Effect of failure to raise issues.* The candidate's failure to raise an argument in a timely fashion during the initial determination process or in a petition for rehearing under this section, as appropriate, shall be deemed a waiver of the candidate's right to present such arguments in any future stage of proceedings including any petition for review filed under 26 U.S.C. 9041(a). An issue is not timely raised in a petition for rehearing if it could have been raised earlier in response to the Commission's initial determination.

(c) *Stay of repayment determination pending appeal.* (1)(i) The candidate may apply to the Commission for a stay of all or a portion of the amount determined to be repayable under this section or under 11 CFR 9038.2 pending the candidate's appeal of that repayment determination pursuant to 26 U.S.C. 9041(a). The repayment amount requested to be stayed shall not exceed the amount at issue on appeal.

(ii) A request for a stay shall be made in writing and shall be filed within 30 calendar days after service of the Commission's decision on a petition for rehearing under paragraph (a) of this section, or, if no petition for rehearing is filed, within 30 calendar days after service of the Commission's final repayment determination under 11 CFR 9038.2(c)(4).

(2) The Commission's approval of a stay request will be conditioned upon the candidate's presentation of evidence in the stay request that he or she:

(i) Has placed the entire amount at issue in a separate interest-bearing account pending the outcome of the appeal and that withdrawals from the account may only be made with the joint signatures of the candidate or his or her agent and a Commission representative; or

(ii) Has posted a surety bond guaranteeing payment of the entire amount at issue plus interest; or

(iii) Has met the following criteria:

(A) He or she will suffer irreparable injury in the absence of a stay; and, if so, that

(B) He or she has made a strong showing of the likelihood of success on the merits of the judicial action.

(C) Such relief is consistent with the public interest; and

(D) No other party interested in the proceedings would be substantially harmed by the stay.

(3) In determining whether the candidate has made a strong showing of the likelihood of success on the merits under paragraph (c)(2)(iii)(B) of this section, the Commission may consider whether the issue on appeal presents a novel or admittedly difficult legal question and whether the equities of the case suggest that the status quo should be maintained.

(4) All stays shall require the payment of interest on the amount at issue. The amount of interest due shall be calculated from the date 30 days after service of the Commission's final repayment determination under 11 CFR 9038.2(c)(4) and shall be the greater of:

(i) An amount calculated in accordance with 28 U.S.C. 1961 (a) and (b); or

(ii) The amount actually earned on the funds set aside under this section.

§ 9038.6 Stale-dated committee checks.

If the committee has checks outstanding to creditors or contributors that have not been cashed, the committee shall notify the Commission. The committee shall inform the Commission of its efforts to locate the payees, if such efforts have been necessary, and its efforts to encourage the payees to cash the outstanding checks. The committee shall also submit a check for the total amount of such outstanding checks, payable to the United States Treasury.

PART 9039—REVIEW AND INVESTIGATION AUTHORITY

Sec.

Authority: 26 U.S.C. 9039.

§ 9039.1 Retention of books and records.

The candidate and his or her authorized committee(s) shall keep all books, records and other information required under 11 CFR 9033.11, 9034.2 and part 9036 for a period of three years pursuant to 11 CFR 102.9(c) and shall furnish such books, records and information to the Commission on request.

§ 9039.2 Continuing review.

(a) In reviewing candidate submissions made under 11 CFR part 9036 and in otherwise carrying out its responsibilities under this subchapter, the Commission may routinely consider information from the following sources:

(1) Any and all materials and communications which the candidate and his or her authorized committee(s) submit or provide under 11 CFR part 9036 and in response to inquiries or requests of the Commission and its staff;

(2) Disclosure reports on file with the Commission; and

(3) Other publicly available documents.

(b) In carrying out the Commission's responsibilities under this subchapter, Commission staff may contact representatives of the candidate and his or her authorized committee(s) to discuss questions and to request documentation concerning committee activities and any submission made under 11 CFR part 9036.

§ 9039.3 Examination and audits; investigations.

(a) *General.* (1) The Commission will consider information obtained in its continuing review under 11 CFR 9039.2 in making any certification, determination or finding under this subchapter. If the Commission decides by an affirmative vote of four of its members that additional information must be obtained in connection with any such certification, determination or finding, it will conduct a further inquiry. A decision to conduct an inquiry under this section may be based on information that is obtained under 11 CFR 9039.2, received by the Commission from outside sources, or otherwise ascertained by the Commission in carrying out its supervisory responsibilities under the Presidential Primary Matching Payment Account Act and the Federal Election Campaign Act.

(2) An inquiry conducted under this section may be used to obtain information relevant to candidate eligibility, matchability of contributions and repayments to the United States Treasury. Information obtained during such an inquiry may be used as the basis, or partial basis, for Commission certifications, determinations and findings under 11 CFR parts 9033, 9034, 9036 and 9038. Information thus obtained may also be the basis of, or be considered in connection with, an investigation under 2 U.S.C. 437g and 11 CFR part 111.

(3) Before conducting an inquiry under this section, the Commission will attempt to obtain relevant information under the continuing review provisions of 11 CFR 9039.2. Matching payments will not be withheld pending the results of an inquiry under this section unless the Commission finds patent irregularities suggesting the possibility of fraud in materials submitted by, or in

the activities of, the candidate or his or her authorized committee(s).

(b) *Procedures.* (1) The Commission will notify the candidate of its decision to conduct an inquiry under this section. The notice will summarize the legal and factual basis for the Commission's decision.

(2) The Commission's inquiry may include, but is not limited to, the following:

(i) A field audit of the candidate's books and records;

(ii) Field interviews of agents and representatives of the candidate and his or her authorized committee(s);

(iii) Verification of reported contributions by contacting reported contributors;

(iv) Verification of disbursement information by contacting reported vendors;

(v) Written questions under order; 1

(vi) Production of documents under subpoena;

(vii) Depositions.

(3) The provisions of 2 U.S.C. 437g and 11 CFR part 111 will not apply to inquiries conducted under this section except that the provisions of 11 CFR 111.12 through 111.15 shall apply to any orders or subpoenas issued by the Commission.

Dated: July 19, 1991.

John Warren McGarry,

Chairman, Federal Election Commission.

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Monday
July 29, 1991

Part III

Department of Health and Human Services

Office of Inspector General

42 CFR Part 1001

Medicare and State Health Care Programs: Fraud and Abuse; OIG Anti-Kickback Provisions; Rule

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Office of Inspector General

42 CFR Part 1001

RIN 0991-AA49

Medicare and State Health Care Programs: Fraud and Abuse; OIG Anti-Kickback Provisions

AGENCY: Office of Inspector General (OIG), HHS.

ACTION: Final rule.

SUMMARY: This final rule implements section 14 of Public Law 100-93, the Medicare and Medicaid Patient and Program Protection Act of 1987, by specifying various payment practices which, although potentially capable of inducing referrals of business under Medicare or a State health care program, will be protected from criminal prosecution or civil sanctions under the anti-kickback provisions of the statute.

EFFECTIVE DATE: This regulation is effective on July 29, 1991.

FOR FURTHER INFORMATION CONTACT:
Thomas S. Crane or D. McCarty Thornton, Office of the General Counsel, (202) 619-0335.
Joel Schaer, Office of Inspector General, (202) 619-3270.

SUPPLEMENTARY INFORMATION:

I. Background

A. The Medicare Anti-Kickback Statute

Section 1128B(b) of the Social Security Act (42 U.S.C. 1320a-7b(b)), previously codified at sections 1877 and 1909 of the Act, provides criminal penalties for individuals or entities that knowingly and willfully offer, pay, solicit or receive remuneration in order to induce business reimbursed under the Medicare or State health care programs. The offense is classified as a felony, and is punishable by fines of up to $25,000 and imprisonment for up to 5 years.

This provision is extremely broad. The types of remuneration covered specifically include kickbacks, bribes, and rebates made directly or indirectly, overtly or covertly, or in cash or in kind. In addition, prohibited conduct includes not only remuneration intended to induce referrals of patients, but remuneration also intended to induce the purchasing, leasing, ordering, or arranging for any good, facility, service, or item paid for by Medicare or State health care programs.

Since the statute on its face is so broad, concern has arisen among a number of health care providers that many relatively innocuous, or even beneficial, commercial arrangements are technically covered by the statute and are, therefore, subject to criminal prosecution.

B. Public Law 100-93

Public Law 100-93, the Medicare and Medicaid Patient and Program Protection Act of 1987, added two new provisions addressing the anti-kickback statute. Section 2 specifically provided new authority to the Office of Inspector General (OIG) to exclude an individual or entity from participation in the Medicare and State health care programs if it is determined that the party has engaged in a prohibited remuneration scheme. (Section 1128(b)(7) of the Act, 42 U.S.C. 1320a-7(b)(7)) This new sanction authority is intended to provide an alternative civil remedy, short of criminal prosecution, that will be a more effective way of regulating abusive business practices than is the case under criminal law.

In addition, section 14 of Public Law 100-93 requires the promulgation of regulations specifying those payment practices that will not be subject to criminal prosecution under section 1128B of the Act and that will not provide a basis for exclusion from the Medicare program or from the State health care programs under section 1128(b)(7) of the Act.

C. Notice of Intent

The legislative history of section 14 of Public Law 100-93 indicates that Congress expected the Department of Health and Human Services to consult with affected provider, practitioner, supplier and beneficiary representatives before promulgating regulations. In order to most effectively address issues related to this provision, we published a notice of intent to develop regulations (52 FR 38794, October 19, 1987) soliciting comments from interested parties prior to developing a proposed regulation. As a result of that notice, the OIG received a number of public comments, recommendations and suggestions on generic criteria that can be applied to particular types of business arrangements in order to determine if such arrangements are inappropriate for civil or criminal sanctions.

D. Notice of Proposed Rulemaking

The proposed regulation designed to implement section 14 of Public Law 100-93 was developed by the OIG and published in the **Federal Register** on January 23, 1989 (54 FR 8033). The regulation sets forth various proposed business and payment practices, or "safe harbors," that would not be treated as criminal offenses under section 1128B(b) of the Act and would not serve as a basis for a program exclusion under section 1128(b)(7) of the Act. As a result of that proposed rulemaking, we received a total of 754 public comments for consideration.

II. Summary of the Proposed Rule

A. Business Arrangements Not Exempt

The proposed regulation indicated that in order for a business arrangement to comply with one of the ten safe harbors, each standard of that safe harbor provision would have to be met. The proposed rule stated that if the business arrangement involves payments for different purposes (for example a single payment for personal services and for equipment rental) then each payment purpose would be analyzed to determine if all the standards of each applicable safe harbor provision have been fulfilled. The proposed rule further specified that where individuals and entities have entered into arrangements that are covered by the statute and where they have chosen not to fully comply with one of the exemptions proposed in these regulations, they would risk scrutiny by the OIG and may be subject to civil or criminal enforcement action.

B. Need for Continuing Guidance

Since there may be a need for the Department to respond to changes in health care delivery or business arrangements more quickly and informally than through the regulatory process to keep the industry abreast of our enforcement policy, the proposed rule invited public comment on how we can best achieve the dual goals of keeping the industry aware of our views of particular business practices, and assuring that our regulations remain current with new developments.

C. Notice to Beneficiaries

While we considered including in several of the proposed safe harbor provisions a requirement that a person notify each Medicare or Medicaid patient he or she refers to a related entity of the financial relationship that exists, we indicated that such notice requirements may be unduly burdensome compared with the potential benefits and, therefore, did not include the requirement in the safe harbors in the proposed regulation. Instead, we invited public comments on this issue.

D. Preferred Provider Organizations

We cited the increasing variety of arrangements among entities grouped under the generic headings "preferred provider organizations" (PPOs) or "managed care," and that unlike HMOs, there is often no single entity that is recognized as the "health care provider." The proposed regulations did not specifically delineate a safe harbor provision for these arrangements since we believed that one or more of the other proposed safe harbors would often cover relationships in preferred provider and managed care networks. We invited comments from the public, however, on the idea of adding additional safe harbors that would provide further protection to HMOs, PPOs, and other managed care plans.

E. Waiver of Coinsurance and Deductible Amounts for Inpatient Hospital Care

We noted that with the advent in 1983 of the prospective payment system for paying hospitals for inpatient care, some hospitals have advertised the routine waiver of Medicare coinsurance and deductible amounts as a means of attracting patients to their facilities. We solicited comments on defining a safe harbor for waiving coinsurance and deductible amounts that would be limited to inpatient hospital care, be available to all Medicare beneficiaries without regard to diagnosis or length of stay, and assure that any costs to the hospital of waiving the coinsurance and deductible amounts would not be passed on to any Federal program as a bad debt or in any other way.

F. Proposed Safe Harbors

The regulation published on January 23, 1989, proposing to amend 42 CFR part 1001 by adding a new § 1001.952, set forth "safe harbors" in ten broad areas:

1. Investment Interests

To reflect the view that Congress did not intend to bar all investments by physicians in other health care entities to which they refer patients, a safe harbor provision was proposed for investment interests in large public corporations where such investments are available to the general public. This safe harbor described a minimum number of shareholders and a minimum number of assets the company must have in order to qualify under this provision.

Safe harbors for limited and managing partnerships were considered under the proposed regulation, but were not included. These areas were discussed in the preamble of the proposed rule, and we specifically requested public comments on adopting these practices as safe harbors.

2. Space Rental

While many rental arrangements are legitimate, many situations exist where rental payments are simply a device used to mask illegal payments intended to induce referrals. Accordingly, a safe harbor provision was proposed for rental arrangements if: (a) Access to the space is for periodic intervals and such intervals are set in advance in the lease, rather than based on the number of referred patients; (b) the lease is for at least one year so it cannot be readjusted on too frequent a basis to reflect prior referrals; and (c) the charges reflect fair market value.

3. Equipment Rental

With the understanding that the payment for the use of diagnostic and other medical equipment may simply be a vehicle to provide reimbursement for referrals, a safe harbor was proposed for certain situations involving equipment rentals similar to those applied to real estate rentals cited above.

4. Personal Services and Management Contracts

While health care providers often have arrangements to perform services for each other on a mutually beneficial basis, some of these arrangements may vary the payment with the volume of referrals. The proposed regulation set forth a safe harbor provision for joint ventures and other arrangements involving payments for personal services or management contracts, but only if certain standards are met that limit the opportunity to provide financial incentives in exchange for referrals. This proposed provision required the services to be paid at fair market value, and was predicated on requirements similar to those set forth in the provisions for space and equipment rental.

5. Sale of Practice

Unlike the traditional sale of a practice by a retiring physician, a physician may sell, or appear to sell, a practice to a hospital while continuing to practice on its staff. A safe harbor provision was proposed for the sale of physician practices when occurring as the result of retirement or some other event that removes the physician from the practice of medicine or from the service area in which he or she was practicing, but not when the sale is for the purpose of obtaining an ongoing source of patient referrals.

6. Referral Services

Professional societies and other consumer-oriented groups often operate referral services for a fee. Because such a service fee could be construed as a payment in order to obtain a referral, we concluded that it was appropriate to establish a specific safe harbor for this type of practice. In order to safeguard against abuse, however, the provision is only available when several standards are met.

7. Warranties

It is in the public interest to have companies offer warranties as an inducement to the consumer to purchase a product. A safe harbor was proposed for such purposes.

8. Discounts

Safe harbors relating to discounts, employees and group purchasing organizations are specifically required by statute. The discount exception was intended to encourage price competition that benefits the Medicare and Medicaid programs. The proposed discount provision was limited in application to reductions in the amount a seller charges for a good or service to the buyer. The discount could take the form of a specified price break, or the inclusion of an extra quantity of the item purchased "at no extra charge." We did not propose to protect many kinds of marketing incentive programs such as cash rebates, free goods or services, redeemable coupons, or credits.

9. Employees

The proposed exception for employees permitted an employer to pay an employee in whatever manner he or she chose for having that employee assist in the solicitation of program business and applied only to bona fide employee-employer relationships.

10. Group Purchasing Organizations

The proposed group purchasing organization (GPO) exception was designed to apply to payments from vendors to entities authorized to act as a GPO for individuals or entities who are furnishing Medicare or Medicaid services. The proposed exception required a written agreement between the GPO and the individual or entity that specifies the amounts vendors will pay the GPO.

III. Response to Comments and Summary of Revisions

As indicated above, in response to the proposed rulemaking we received 754 public comments from various provider groups, medical facilities, professional and business organizations and associations, medical societies, State and local government entities, private practitioners and concerned citizens. The comments included both general and broadreaching concerns regarding the impact of this regulation, and specific comments on those areas and safe harbor provisions about which we requested public input. A summary of the comments received and our responses to those comments follows.

A. General Comments

Comment: A large number of commenters expressed concern about the implication of engaging in a business arrangement that does not comply fully with a provision of this regulation. Some of these commenters expressed the view that the safe harbor provisions are narrowly drawn and leave many lawful business arrangements unprotected. Moreover, the preamble to the proposed rule warns: "[W]here individuals and entities have entered into arrangements that are covered by the statute, where they have chosen not to comply fully with one of the exemptions in these regulations, they would risk scrutiny by the OIG * * *." These commenters urged the OIG to make clear that the failure to comply fully with a safe harbor provision is not *per se* illegal, and does not mean that prosecution will automatically follow. In addition, they requested safe harbor protection for business arrangements where there has only been a "technical violation" of the statute, where there has been "substantial compliance" with this regulation, or where the remuneration in question is "de minimis."

Response: This regulation covers many categories of business arrangements, providing standards to be met within each safe harbor provision. If a person participates in an arrangement that fully complies with a given provision, he or she will be assured of not being prosecuted criminally or civilly for the arrangement that is the subject of that provision.

This regulation does not expand the scope of activities that the statute prohibits. The statute itself describes the scope of illegal activities. The legality of a particular business arrangement must be determined by comparing the particular facts to the proscriptions of the statute.

The failure to comply with a safe harbor can mean one of three things. First, as we stated in the preamble to the proposed rule, it may mean that the arrangement does not fall within the ambit of the statute. In other words, the arrangement is not intended to induce the referral of business reimbursable under Medicare or Medicaid; so there is no reason to comply with the safe harbor standards, and no risk of prosecution.

Second, at the other end of the spectrum, the arrangement could be a clear statutory violation and also not qualify for safe harbor protection. In that case, assuming the arrangement is obviously abusive, prosecution would be very likely.

Third, the arrangement may violate the statute in a less serious manner, although not be in compliance with a safe harbor provision. Here there is no way to predict the degree of risk. Rather, the degree of the risk depends on an evaluation of the many factors which are part of the decision-making process regarding case selection for investigation and prosecution. Certainly, in many (but not necessarily all) instances, prosecutorial discretion would be exercised not to pursue cases where the participants appear to have acted in a genuine good-faith attempt to comply with the terms of a safe harbor, but for reasons beyond their control are not in compliance with the terms of that safe harbor. In other instances, there may not even be an applicable safe harbor, but the arrangement may appear innocuous. But in other instances, we will want to take appropriate action.

We do not believe the Medicare and Medicaid programs would be properly served if we assured protection in all instances of "substantial compliance," "technical violations," or "de minimis" payments. Unfortunately, these are vague concepts, subject to differing interpretations. In this regulation, we have attempted to provide bright lines, to the extent possible, for safe harbors in order to provide clarity and predictability as to what conduct is immune from government action. Our endorsement of the concepts mentioned above would only serve to blur these lines and produce litigation as to what "substantial," "technical" and "de minimis" really mean. The OIG therefore declines to adopt these concepts.

A recent decision of the United States Court of Appeals for the First Circuit provides an indication of the litigation problems that could arise if "substantial compliance" with a safe harbor provision was all that was required. *United States* v. *Bay State Ambulance and Hospital Rental Service, Inc.*, 874 F.2d 20 (1st Cir., 1989) involved an arrangement between an employee of a city owned hospital (Felci) and an ambulance company (Bay State). Felci was involved in the administration of the city's ambulance service contract. During this period, Bay State retained Felci as a consultant, provided him with two automobiles, and paid Felci's consulting company several thousand dollars. When it came time for renewal of the ambulance contract, Felci used his position and influence at the city hospital to assist Bay State in securing the new contract. Felci was prosecuted and convicted under the statute.

In affirming Felci's conviction (as well as that of Bay State's president, Kotzen), the First Circuit rejected Felci's contention that he had substantially complied with this regulation as published as a notice of proposed rulemaking, and thus should not be prosecuted. The court found: "The proposed regulation does not exempt every transaction in which the amount paid for services is an amount consistent with fair market value; rather it exempts only a small subset of such transactions * * *. [U]nder the circumstances such as the present case where the consulting arrangement is not full-time, * * * stringent requirements are necessary to meet the exemption from criminal liability. HHS has thus decided *not* to create a safe harbor for transactions such as the present case." (Emphasis in original; footnote omitted) *Id.* 874 F.2d at 31.

Comment: Several commenters described business arrangements that technically may violate the statute, but do not increase costs to the Medicare or Medicaid programs, or otherwise injure beneficiaries. They requested safe harbor protection for these arrangements because of concern of their risk of being scrutinized.

Response: Increased cost to the Medicare and Medicaid programs and harm to beneficiaries are not the only criteria we look at in determining whether a particular business arrangement is abusive. As the court in *United States* v. *Ruttenberg*, 625 F.2d 173, 177, n.9 (7th Cir. 1980) noted:

> [T]he law does not make increased cost to the government the sole criterion of corruption. In prohibiting "kickbacks," Congress need not have spelled out the obvious truisms that, while unnecessary expenditure of money earned and contributed by taxpaying fellow citizens may exacerbate the result of the crime, kickback schemes can freeze competing suppliers from the system, can mask the possibility of government price reductions, can misdirect program funds, and, when proportional, can erect strong temptations to order more drugs and supplies than needed.

Furthermore, it is unfortunately not possible to provide safe harbor protections for all business arrangements that are not abusive. There are certain arrangements that, although themselves legitimate, are structurally so similar to abusive arrangements that protection by way of new safe harbor provisions will inevitably also protect abusive practices as well. For example, equipment rental arrangements made between parties in a position to make and accept referrals do not receive safe harbor protection if the payments are based on utilization (sometimes known as a "wear and tear" clause). We recognize that equipment becomes less valuable the more it is used, and that its owner deserves compensation for such wear and tear. However, it is also a relatively easy matter to disguise such a wear and tear payment as a payment for referrals. Thus, we need to examine the intent of the parties on a case-by-case basis even though a large majority of such payments may represent only legitimate compensation to the owner of the equipment.

The recent case, *United States* v. *Bay State Ambulance and Hospital Rental Service, Inc.*, discussed above, emphasizes that the gravamen of a violation of the statute is "inducement" and not necessarily the structure of the arrangement. *Id.* 874 F.2d at 29. Thus, such case by case inquiries must necessarily focus on the intent of the parties.

The *Bay State Ambulance* case also illustrates the risk health care providers engage in when they enter into a business arrangement that violates the statute, but try to argue that the arrangement does not increase program costs or result in overutilization. The First Circuit rejected the defendants' arguments that there would have been no fiscal drain on public programs because ambulance services and Medicare reimbursement would have been required no matter which ambulance service company had received the contract. The court noted that it was unclear whether Medicare paid Bay State more for these services than it would have paid to the losing bidder even though that bidder's charges were lower. The court observed: "Although the reason for enacting the statute was to prevent drains on the public fisc, the statute does not require that there be a drain on the public fisc in order for payments to be illegal." *Id.* n.21, 874 F.2d at 32.

Comment: Numerous commenters expressed concern about the difficulty in revising a business arrangement that they entered into with a good-faith belief that the arrangement did not violate the statute, but which they now find does not qualify under one of the safe harbor provisions. They suggested that the OIG either "grandfather" these arrangements or provide a reasonable period of time before initiating enforcement action to enable health care providers to restructure their arrangements to meet the safe harbor provisions.

Response: The failure of a particular business arrangement to comply with these provisions does not determine whether or not the arrangement violates the statute because, as we stated above, this regulation does not make conduct illegal. Any conduct that could be construed to be illegal after the promulgation of this rule would have been illegal at any time since the current law was enacted in 1977. Thus illegal arrangements entered into in the past were undertaken with a risk of prosecution. This regulation is intended to provide a formula for avoiding risk in the future.

We also recognize, however, that many health care providers have structured their business arrangements based on the advice of an attorney and in good-faith believed that the arrangement was legal. In the event that they now find that the arrangement does not comply fully with a particular safe harbor provision and are working with diligence and good faith to restructure it so that it does comply, we will use our discretion to be fair to the parties to such arrangements.

Nonetheless, we believe that it would be inappropriate for us to provide a blanket protection, even for a limited period of time, for all business arrangements that do not qualify for a safe harbor. As we stated above, certain business arrangements that do not qualify may warrant immediate enforcement action.

Comment: Many commenters discussed the interrelationships between these safe harbor provisions and reimbursement rules promulgated by the Health Care Financing Administration (HCFA). A few of these commenters appeared to suggest that if a health care provider complied with a particular safe harbor provision, then its reimbursement may be affected.

Response: We wish to emphasize that nothing in this regulation changes reimbursement rules promulgated by HCFA or a State health care program. Clearly if a provider chooses to engage in one course of conduct in order to comply with these safe harbor provisions, such action may very well have reimbursement implications. However, such reimbursement is governed exclusively by HCFA or State regulations, and not by this regulation.

Comment: Several commenters requested that the OIG publish this regulation with an additional comment period because of the complexity of the issues involved and the revisions or additions of new safe harbor provisions created as a result of the comments.

Response: We believe that the disadvantages of providing an additional comment period outweigh the benefits. As we stated above, we received extensive comments in response to this proposed rule. In addition, due to the novelty and complexity of these issues, we started this process with a special notice of intent to develop regulations, (52 FR 38794, October 19, 1987) and received over 150 comments, which we used to develop the proposed rule.

Also weighing against any benefit of receiving additional comments on this rule is the desirability of providing the level of certainty that accompanies a final rule. This will permit individuals and entities to structure business arrangements under the provisions of this rule with the assurance that it will not change in the near future. Such assurance is delayed somewhat by providing an additional comment period.

We acknowledge the congressional expectation that we should "formally re-evaluate the anti-kickback regulations on a periodic basis, and, in so doing, * * * solicit public comment at the outset of the review process." H.R. Rep. No. 85, part 2, 100th Cong. 1st Sess. 27 (1987). We believe it is most appropriate to allow all parties time to obtain experience with these safe harbor provisions in their final form before we solicit additional public comments to start our formal re-evaluation process.

Nonetheless, we received many comments requesting safe harbor protection for a number of business arrangements, many of which deserve safe harbor protection. As discussed in more detail below in section III.B.3. of this preamble, the comments we received on HMOs, PPOs, and other managed care plans warrant the creation of two new safe harbor provisions. Because of the lack of specificity in those comments, we expect to publish these provisions as a separate interim final regulation at a later date. While this provision will be effective upon publication, the public will have an opportunity to submit their specific comments and concerns regarding this new safe harbor.

In addition, as discussed in more detail below in section III.B. of this preamble, many other arrangements brought to our attention were for arrangements on which we did not solicit comments. Because some of these arrangements may deserve safe harbor protection, we anticipate publishing additional safe harbor provisions in a separate notice of proposed rulemaking. Any discussion below indicating that we are considering a new safe harbor provision should in no way be construed as legalizing the business arrangement at this time.

Comment: Numerous commenters suggested that the OIG should employ a cease and desist mechanism. Some suggested that the OIG should be required to employ such a mechanism before it initiates a criminal prosecution or program exclusion. Others supported the use of this mechanism because they believed that many business arrangements that violate the statute do not warrant prosecution but should be stopped.

Response: We do not have the authority to seek or issue a legally enforceable order directing a person to cease and desist from a particular unlawful kickback activity. We recognize that there may be situations where it may be appropriate to inform a person that he or she is violating the statute, and request that the unlawful activity be stopped. Where the person takes immediate action to conform his activity to the law, we may decide that no further action is warranted. However, there may be other situations where criminal prosecution is appropriate even though the person has stopped the illegal activity. Since we lack the power to issue or seek a legally enforceable cease and desist order, we cannot rely on that mechanism as a significant enforcement tool.

Comment: Three commenters suggested that because many business arrangements will not meet the safe harbor provisions, the regulation was of limited value. They suggested that health care providers would be better aided if the OIG would provide examples of arrangements that violate the statute.

Response: As we stated above, the purpose of this regulation is not to describe illegal conduct, but rather to set forth standards for certain safe harbors. If an individual or entity engages in a business arrangement that is the subject of a safe harbor provision and complies with all of its provisions, that individual will be assured that he or she will not be prosecuted. However, we recognize the desirability of communicating to the public the existence of other business practices and arrangements that we believe are subject to serious abuse. Accordingly, we issued a special OIG Fraud Alert on joint venture arrangements that described various suspect features of these business ventures that may result in a violation of the statute. As the need arises, we intend to issue other fraud alerts that will provide guidance to the public on other types of arrangements.

Comment: In seeking guidance with respect to transactions or practices not covered by any specific safe harbor provision, many commenters requested the OIG to include within this regulation a list of generic criteria it would consider in evaluating business arrangements under the statute. These commenters cite a variety of positive and negative factors as relevant generic criteria, including on the positive side whether the arrangement has "a legitimate business purpose" or promotes the delivery of needed services, particularly to indigent, elderly, or rural populations; and on the negative side whether the arrangement promotes overutilization, interferes with patient freedom of choice, diminishes the quality of care provided, or increases costs to beneficiaries or to the government. Some commenters pointed out that the legislative history of Public Law 100–93 directs the Department to include in the rules "any generic criteria that might apply to business arrangements generally." H.R. Rep. No. 85, part 2, 100th Cong., 1st Sess. 27 (1987).

Response: We believe the same generic criteria applicable to all business arrangements would not provide useful guidance to the extent that they are based on value judgments regarding the relative advantages (e.g., lower cost or improved accessibility) and disadvantages (e.g., higher cost or overutilization) of the arrangement. It would be virtually impossible to set forth rules describing how we intend to apply them. For example, the determination of whether a joint venture has a legitimate business purpose, is a matter of subjective judgment, and we believe the use of such criteria would invite litigation because health care providers will not be sure if they are complying with them.

An example of the problems in using these types of generic criteria can be seen if we attempted to provide safe harbor protection for business arrangements that have a "legitimate business purpose." The statute proscribes the giving of rebates as a form of remuneration to induce referrals. Yet rebates are legitimate and common business practices outside the health care services business sector. For the numerous people who engage in both health care and non-health care lines of business, they may have become accustomed to providing various inducements to others in their non-health care activities. They may now start to provide similar inducements in their health care lines of business in a manner that violates the statute. To them, these inducements have a "legitimate business purpose," that is, to gain referrals and thereby make money, yet the practice is expressly prohibited by the statute.

We believe that Congress did not require us to specify such generic criteria. The House Committee Report so often cited by commenters directs us to promulgate rules that, "to the extent practical, contain * * * any generic criteria that might apply to business arrangements generally." *Id.* We believe that we have done so. It was only practical to include generic criteria for specific categories of arrangements, such as "fair market value" in the "space rental" safe harbor. We have concluded, however, that a single set of standards for all business arrangements would be of extremely limited value because the subjectivity or arbitrariness in applying the standards to individual fact situations would make such standards of extremely limited value.

We recognize that some of the factors cited by commenters are useful in determining the extent to which a particular arrangement is abusive, and therefore likely to be prosecuted. For example, the more an arrangement involving remuneration offered to induce referrals increases Medicare or Medicaid program costs or results in unnecessary utilization, the more likely it would be that we would have an interest in prosecuting the offense. It must be emphasized that these are not the only factors upon which a determination regarding prosecution is based, and as we have noted "the statute does not require that there be a drain on the public fisc in order for payments to be illegal." *United States* v. *Bay State Ambulance and Hospital Rental Service, Inc., supra,* 874 F.2d at 32, n. 21.

Comment: Several commenters objected to the regulation because they believed that the OIG had exceeded its statutory authority. In particular, they commented that the OIG does not have authority under section 14 of Public Law 100–93 to narrow the scope of the statutory exceptions, particularly the "discount" exception of section 1128B(b)(3)(A) of the Act. They cited the last sentence of section 14(a) which states, "Any practices specified in regulations pursuant to [sec. 14 of Pub. L. 100–93] shall be in addition to the practices described in subparagraphs (A) through (C) of section 1128B(b)(3)." This sentence led some commenters to conclude that our regulatory authority does not permit us to refine or clarify the statutory exceptions.

Response: We believe that these commenters have misconstrued the intent of this sentence. The plain language of the first sentence of section 14(a) of Public Law 100–93 requires the Secretary to promulgate regulations "specifying payment practices that shall not be treated as a criminal offense under section 1128B(b) of the Social Security Act and shall not serve as the basis for an exclusion under section 1128(b)(7) of such Act." We believe that the second sentence, which was quoted by many commenters, requires us to add to the exceptions provided in section 1128B(b)(3) of the Act. But we do not believe the intent of this sentence is to prohibit us from interpreting statutory terms used in these exceptions. The clear congressional intent behind the development of these safe harbor provisions is to define innocuous arrangements that should not be prosecuted, including the statutory exceptions. We believe it is in the public interest to provide the health care community with our interpretation of the meaning of certain important statutory terms, for example, "appropriately reflect" in the discount exception or "bona fide employment relationship" in the employee-employer exception.

Comment: One commenter asked the OIG to clarify how it expects health care providers to comply with this regulation when it engages in a business arrangement that may be covered by two or more of the provisions of this regulation.

Response: This comment addresses two potential situations. The first situation arises where a payment practice serves a single purpose (e.g., compensation for personal services), but potentially fits into more than one safe harbor (e.g., the employer-employee safe harbor and the personal services and management contracts safe harbor). In this situation, if the payment practice fits into either one of the safe harbors, it is exempt from criminal prosecution and program exclusion. In the example given, if the payment practice does not qualify as a bona fide employment relationship, it still may receive safe harbor protection under the personal services and management contract safe harbor.

The second situation arises where a payment practice serves multiple purposes (e.g., a payment to recompensate another party for personal services and equipment rental). Under these circumstances, it will be necessary to examine each aspect of the payment practice to determine compliance with each respective safe harbor provision. A person engaged in a "multi-purpose" payment practice who seeks protection will need to document separately his or her compliance with the safe harbor applicable to each purpose being served by the payment practice. Compliance with one provision (for one of the purposes of the payment practice) would not insulate the entire payment practice from criminal prosecution or program exclusion, where another purpose of the payment practice is implemented in a manner which violates the statute.

In the provision-by-provision analysis in section III.C. below, we will discuss specific comments and our responses to other special issues regarding the interrelationships of these provisions.

Comment: Two commenters requested that the OIG clarify the relationship between the statute and various State laws.

Response: Issues of state law are completely independent of the federal anti-kickback statute and these regulations. There is no federal preemption provision under the statute. Thus, conduct that is lawful under the federal anti-kickback statute or this regulation may still be illegal under State law. Conversely, conduct that is lawful under State law may still be illegal under the federal anti-kickback statute.

Comment: We received many comments on the proposed "Ethics in Patient Referrals Act" then pending in Congress aimed at restricting physicians from referring patients to entities in which they have a financial interest, the so-called "Stark Bill." Many of these commenters asked the OIG to either support or oppose this legislation. Others asked the OIG to clarify the relationship of this legislation to the anti-kickback statute and this regulation.

Response: This legislation was enacted as section 6204 of the Omnibus Budget Reconciliation Act of 1989, Public Law 101–239, adding a new section 1877 to the Act. With numerous exceptions, it generally restricts physicians from making referrals for clinical laboratory services to entities in which they have an ownership or other compensation arrangement. These referral restrictions become effective on January 1, 1992.

The legislation, although in many respects aimed at the same problems as we are addressing in this regulation, requires different elements of proof and has different remedies than under the anti-kickback statute. Generally, section 1877 is violated when a "financial relationship" exists between an entity furnishing clinical laboratory services and a physician, and a referral is made or a claim or bill is presented. For the anti-kickback statute to be violated, it must be shown that the remuneration between the two parties was intended to induce the referral of business payable under Medicare or Medicaid. Whereas the anti-kickback statute contains criminal penalties, violations under section 1877 will result in a denial of payment and may result in the imposition of civil money penalties and program exclusions under section 1128A of the Act.

Because of these differences between the two provisions, the conference report includes the following clarification:

> The conferees wish to clarify that any prohibition, exemption, or exception authorized under this provision in no way alters (or reflects on) the scope and application of the anti-kickback provisions in section 1128B of the Social Security Act. The conferees do not intend that this provision should be construed as affecting, or in any way interfering, with the efforts of the Inspector General to enforce current law, such as cases described in the recent Fraud Alert issued by the Inspector General. In particular, entities which would be eligible for a specific exemption would be subject to all of the provisions of current law.

H.R. Conf. Rep. 239, 101st Cong., 1st sess. 856 (1989).

This clear expression of legislative intent to keep enforcement under the anti-kickback statute separate from enforcement under section 1877 makes it inappropriate to adjust our safe harbor provisions to take into account any exception or prohibition under section 1877.

Comment: Thirty-three commenters reacted to our comments in the preamble of the proposed rule regarding the breadth and scope of the statute. Fourteen commenters suggested that these regulations should in no way undermine the scope or strength of the statute. These commenters believe that by adding the civil exclusion remedy for the kickback violations as part of Public Law 100–93, Congress sent a clear and appropriate message to the health care community not to place financial considerations above beneficiaries' interests. Two commenters requested that the statute's term "to refer" should be defined. Other commenters were concerned that diminishing the reach of the statute would create conflicts of interest between health care providers and their patients, and impugn the professional image of physicians. A few commenters opposed the implementation of any safe harbor provisions whatsoever.

Response: Our charge from Congress under section 14 of Public Law 100–93 is to clarify what payment practices will not subject a person to criminal prosecution or exclusion from the Medicare or State health care programs. The process involves both a determination of the scope of the statute and decisions as to how to draft the safe harbor provisions so that they protect only non-abusive relationships.

With respect to the scope of the statute, we do not believe that it is necessary to define any of the statute's terms in the regulation itself. However, the meaning of two of its terms deserve comment (1) "any remuneration (including any kickback, bribe, or rebate) directly or indirectly, overtly or covertly, in cash or in kind;" and (2) "to induce." These terms demonstrate congressional intent to create a very broadly worded prohibition. Our comments in the preamble to the proposed rule reflected our belief that Congress ratified this intent in their mandate to create these safe harbor provisions.

Congress's intent in placing the term "remuneration" in the statute in 1977 was to cover the transferring of anything of value in any form or manner whatsoever. The statute's language makes clear that illegal payments are prohibited beyond merely "bribes," "kickbacks," and "rebates," which were the three terms used in the original 1972 statute. The language "directly or indirectly, overtly or covertly, in cash or in kind" makes clear that the form or manner of the payment includes indirect, covert, and in kind transactions. Morecver, the statutory exception for discounts demonstrates that Congress prohibited transactions where there is no direct payment at all from the party receiving the referrals. The remuneration in a discount is merely a lowered price that a purchaser would otherwise obtain from a seller, which is made as an inducement to purchase larger quantities.

The statute's legislative history supports this reading of the term "remuneration," and makes clear that the fundamental analysis required of a trier of fact is "to recognize that the substance rather than simply the form of a transaction should be controlling" (123 Cong. Rec. 30,280 (1977), Statement of Chairman of the House Committee on Ways and Means and principal author of H.R. 3, Representative Rostenkowski). Also see H.R. Rep. No. 393, part II, 95th Cong., lst Sess. 53; reprinted in (1977) U.S. Code Cong. & Ad. News 3056; S.Rep. No. 453, 95th Cong., lst Sess. 12 (1977).

The meaning of the term "to induce," which describes the intent of those who offer or pay remuneration in paragraph (2) of the statute, is found in the ordinary dictionary definition: "to lead or move by influence or persuasion" (The American Heritage Dictionary (2d College Ed. 1982)).

The OIG's interpretation of the statute is fully supported by its case law. At the time that the proposed rule was issued, the leading case interpreting the breadth of the statute was *United States* v. *Greber*, 760 F.2d 68 (3d Cir.) *cert. denied*, 474 U.S. 988 (1985). Since publication of the notice of proposed rulemaking on January 23, 1989, two other circuit courts have lent further support to a broad reading of the statute: *Bay State Ambulance*, which was discussed above, and *United States* v. *Kats*, 871 F.2d 105 (9th Cir. 1989).

Kats involved an arrangement between physician offices or clinics, a phlebotomy service ("THC"), and a clinical diagnostic laboratory ("Tech-Lab"). Under the arrangement, THC collected blood and urine samples from physician offices and medical clinics, and forwarded these laboratory specimens to Tech-Lab. Tech-Lab performed the laboratory tests and billed the respective insurance programs, including Medicare and Medicaid. Tech-Lab kicked back 50 percent of its proceeds to THC, which in turn kicked back part of its proceeds to the various physician offices and clinics, including a clinic owned by Yan Kats. Kats and others were prosecuted and convicted under the statute.

In upholding Kats's conviction, the United States Court of Appeals for the Ninth Circuit became the first court specifically to adopt the holding in *Gerber* that "if one purpose of the payment is to induce future referrals, the [M]edicare statute has been violated." 760 F.2d at 69. The *Kats* court held that the statute is violated unless the payments are "wholly and not incidentally attributable to the delivery of goods or services." *Id.* 871 F.2d at 108. The court upheld a jury instruction that read, in part, "It is not a defense that there might have been other reasons for the solicitation of a remuneration by the defendants, if you find that one of the material purposes for the solicitation was to obtain money for the referral of services." *Id.* 871 F.2d at 108, n.1.

Because the statute is broad, the payment practices described in these safe harbor provisions would be prohibited by the statute but for their inclusion here. In mandating this regulation, Congress directed us to limit the reach of the statute somewhat by permitting certain non-abusive arrangements, while encouraging beneficial or innocuous arrangements. We believe that we have accomplished this task in a manner that will not restrict our ability to prosecute, either criminally or civilly, abusive schemes that violate the statute. However, these safe harbor provisions do not constitute a guarantee that a health care provider whose practice conforms to a particular safe harbor will not engage in abusive practices. For this reason, we intend to monitor business arrangements that comply with the terms of these safe harbor provisions, particularly investment interests (see section III.C.1.b.ii. below), to determine whether abusive arrangements exist within the parameter of a particular safe harbor. If abusive arrangements are found to exist, we will entirely withdraw or modify any provision as appropriate.

Comment: A small number of commenters requested clarification as to whether the statute prohibits remuneration in return for referrals or other arrangements to induce services or items reimbursed under Medicare alone, or whether the conduct prohibited by the statute includes referrals or other arrangements to induce services or items reimbursed by Medicaid and other State health care programs.

Response: We agree that clarification is needed, and have amended the final rule to make clear that the statute, and hence these safe harbor provisions, apply to items or services which may be paid in whole or in part under Medicare or a federally funded State health care program, such as Medicaid. However, because commenters have expressed particular concern about the applicability of these provisions to items and services payable under the Medicare and Medicaid programs, our discussion of comments and responses often refer solely to these two programs.

B. Comments on Areas That the OIG Invited Comments

In this section, we discuss four issues on which we specifically invited public comments: continuing guidance, notice to beneficiaries, preferred provider organizations (PPOs), and waiver of coinsurance and deductible amounts for inpatient hospital care. We also requested comments on suggested standards for two additional investment interest provisions that would protect investors, such as limited and general partners, investing in small entities. Our discussion of those comments and our responses are contained in the provision-by-provision analysis of investment interests (see section III.C.1. below).

1. Continuing Guidance

Comment: We received a large number of responses to our invitation for comments on how the OIG can best inform health care providers about fraudulent practices, and can best ensure that the safe harbor regulation remains current as new health care business practices develop. Many of these commenters suggested that the Department issue advisory opinions about the legality of proposed business arrangements under the statute. Some commenters requested that the Department implement a mechanism for informing health care providers about business practices that raise problems under the statute.

Proponents of advisory opinions argued that such a mechanism would provide guidance concerning activities unaddressed by the safe harbor regulation, curb illegal payment practices, and keep the Department informed of industry developments. These commenters asserted that the Department has authority to issue advisory opinions pursuant to its general statutory authority to promulgate regulations, and pursuant to the specific authority under Public Law 100–93 to promulgate this regulation. The commenters contended that advisory opinion rulings would not hamper the Department of Justice's prosecutorial discretion under the statute, because the immunizing effects of advice given would be limited to the facts disclosed. The commenters also claimed that several other agencies employ advisory opinion procedures in administering laws under their respective jurisdictions.

Response: We understand and appreciate providers' desire for legal security in their business relations. Consistent with our mandate under Public Law 100–93, we will continue to make efforts to inform health care providers about business practices that may subject them to criminal prosecution or program exclusion.

We have concluded that we will not provide a mechanism responding to individual requests for advisory opinions about the legality of a particular business arrangement under the statute. The statute is primarily a criminal statute, and the Department of Justice is vested with exclusive authority to enforce all criminal laws of the United States. See sections 516, 519 and 547 of title 28 of the United States Code. A plethora of case law holds that this exclusive authority extends to all decisions to initiate, or to decline to initiate, criminal prosecutions. See *Smith* v. *United States,* 375 F.2d 243, 247 (4th Cir. 1967), *cert. denied* 389 U.S. 841; *Powell* v. *Katzenbach,* 359 F.2d 234 (D.C. Cir. 1965), *cert. denied* 384 U.S. 906; *United States* v. *Wong Kim Bo,* 466 F.2d 1298 (5th Cir. 1972); *United States* v. *Kysar,* 459 F. 2d 422 (10th Cir. 1972). For these reasons, this Department cannot, through advisory opinions, immunize health care providers from criminal prosecution under the statute.

The general or specific statutory authorizations cited by commenters do not supersede the case law cited above. The Department's general authority as an executive agency to promulgate regulations governing conduct within the Department's jurisdiction does not, implicitly or explicitly, include authority to make judgments that are within the exclusive domain of another agency. Neither does our mandate, under Public Law 100–93, to promulgate this regulation provide such authority. Our charge to immunize, by regulation, conduct and arrangements potentially falling under the statute does not include judging whether the conduct of particular individuals violates the statute.

Aside from these legal impediments, it is impossible as a practical matter to give meaningful advice with respect to liability under the statute in the context of a letter ruling. The statute requires proof of a knowing and willful intent to induce or arrange for referrals or for other business reimbursable under the Medicare or Medicaid programs. See *United States* v. *Bay State Ambulance and Hospital Rental Service, Inc., supra,* 874 F.2d at 29 ("The gravamen of Medicare Fraud is inducement"); *United States* v. *Greber,* 760 F. 2d 68 at 71 ("The statute is aimed at the inducement factor"). Thus, the extent to which conduct is motivated by inducing or arranging for referrals will, in large part, determine liability under the statute. The types of factual summaries that typically accompany requests for advisory opinions—descriptions of proposed management contracts or lease agreements, or prospectuses of joint ventures—are likely, however, to be insufficient for purposes of understanding the motives of the parties.

In our experience, assessing whether parties to a particular scheme intend to induce referrals requires substantial investigation resources. Requests for advice typically do not furnish complete and objective accounts of all the facts necessary to determine the subjective intent of the parties. In addition, requests for advice involving business arrangements not yet consummated are especially difficult to analyze because the motives of the parties to induce referrals often become apparent only when the arrangement is operational.

Furthermore, we do not believe that an advisory opinion process is a necessary or appropriate mechanism for keeping the Department aware of new developments in industry business practices, and ensuring that the regulation remains current. As we have discussed above, the legislative history of Public Law 100–93 clearly directs the Secretary to "formally re-evaluate the anti-kickback regulations on a periodic basis and, in so doing, * * * solicit public comment at the outset of the review process." H.R. Rep. No. 85, *supra,* at 27. We believe that periodic updating of this regulation, with the opportunity for public input, is the best way to ensure that these regulations remain practical and relevant in the face of changes in health care delivery and payment arrangements. The need to clarify, interpret, fine tune, expand, or otherwise alter this regulation in response to public and industry input will provide an occasion for us to respond to unanticipated, newly developing, or other beneficial arrangements.

Despite commenters' arguments that other Federal agencies offer the public mechanisms for obtaining advisory opinions, only one other agency of which we are aware, the Federal Elections Commission (FEC), provides any advice with respect to a statutory provision that prohibits "knowing and willful" conduct. The FEC issues such advice under specific statutory authority (2 U.S.C. 437d(a)(7)). It is our understanding, however, that the FEC's advisory opinions do not inquire into whether any conduct is knowing and willful. Thus, the FEC's practice follows the general rule that agencies will refrain from rendering prospective advice on issues of intent. For example, the IRS has stated that it will not issue advice as to the "due diligence" or "good-faith" of parties. See Rev. Proc. 88–3, 1988–1 IRB 29.

As an alternative, we believe that OIG fraud alerts are the best mechanism for imparting practical and continuing guidance to individuals and entities seeking to avoid violations of the statute. The fraud alert program, implemented in March of 1984, was designed to increase our effectiveness in preventing fraud in this Department's programs by highlighting conduct likely to be illegal. Since 1984, we have issued over 100 fraud alerts on subjects unrelated to the anti-kickback statute. On April 24, 1989, we initiated distribution of a Special Fraud Alert on Joint Venture Arrangements to all individuals and entities participating in Medicare, which gave examples of specific characteristics of provider-owned entities that, in our view, might result in abusive or unlawful business arrangements. By identifying what we consider to be suspect features of limited partnerships and other joint ventures (including potentially abusive practices for selecting and retaining investors, for structuring the legal entity or entities involved, and for distributing profits), the Special Fraud Alert communicated our views about the legitimacy of potential or existing ownership arrangements. We believe that fraud alerts can be equally as educational about other areas of enforcement of the statute, and plan to distribute similar information as the need arises.

Comment: A few commenters inquired about the binding effect of advisory letters written by HCFA in the 1970s, when that agency was responsible for enforcing the statute. The commenters suggested that these letters may serve to protect health care providers who engage in a particular business arrangement that was approved by HCFA at that time even though the OIG has not now proposed a safe harbor for that arrangement.

Response: No person in the Department or with the fiscal intermediaries or carriers is, or ever has been, authorized to permit a practice that the statute makes illegal. The Department's lack of authority to provide legal advice on the application of the statute to specific factual situations has been consistently communicated to the public for years. Consequently, no person may reasonably rely on any such advice, especially when that advice is a letter written to a third party about a business arrangement different from the one in which the party is engaging. In sum, the so-called advisory letters may not be regarded in any way as authoritative.

The only authority to legalize conduct is this safe harbor regulation. This regulation supersedes any prior communications from the Department regarding business practices considered not subject to prosecution, and is the only formal mechanism to set forth business arrangements or payment practices that will not be prosecuted under the statute.

Comment: Two commenters requested the OIG to issue selective opinions on issues affecting a class of providers that arise under the statute and safe harbor regulations, even if we decline to provide advice about specific business arrangements or activities.

Response: As we have said, we plan to provide guidance on generic issues through fraud alerts distributed to the provider community. In addition, we remain open to examining the usefulness of other mechanisms for informing the public and health care provider groups about the types of new business arrangements to which the OIG will give investigative priority.

2. Notice to Beneficiaries

Comment: Commenters overwhelmingly supported requiring health care providers to disclose to patients any financial relationships with sources of referral. They argued that such disclosure would not be burdensome, and that many codes of professional ethics, as well as many state statutes, already mandate such disclosure.

Response: With one exception, we have decided not to require such disclosure to qualify under a particular safe harbor provision. First, the activities covered under each safe harbor provision are by definition activities that we deem have a low potential for abuse. Second, disclosure in and of itself would not provide a significant additional assurance that abuse would not occur, even though disclosure may reduce the potential for abuse somewhat by increasing consumer awareness of the relationship between health care providers. Finally, it is possible for a health care provider to cast a disclosure to fit that provider's promotional objective, which is exactly the opposite result from that which we would want to achieve.

The one provision in which we condition safe harbor protection on disclosure is that of referral services. Referral services help beneficiaries make their initial contact with the health care system before a relationship of trust is established with a particular health care provider. Without disclosure of the manner in which a provider of services was selected or rejected by a referral service and the relationship between the service and health care providers, a consumer has very little information upon which to base his or her trust in the practitioner to whom the consumer is being referred. For example, a consumer may well decide to put more trust in a surgeon referred by the referral service if the consumer knew that the referral service only uses board certified physicians. On the other hand, a consumer may feel less confidence in a referral if any physician, no matter what his or her disciplinary record, were one of the referral service's members. Consequently, we are confident that, in this instance, disclosure represents a meaningful added protection.

Although we are not requiring disclosure of financial interests under the other safe harbor provisions, we consider disclosure of financial interests in entities to which health care providers refer patients an ethical duty (See, for example, rule 8.03 of the Current Opinions of the Council on Ethical and Judicial Affairs of the American Medical Association, Chicago, Ill. 1989). Also, to the extent that disclosure affects a patient's freedom of choice and quality of care, it may be necessary to enable a patient to give informed consent.

3. Health Maintenance Organizations, Preferred Provider Organizations and Other Managed Care Plans

We received a number of responses to our invitation to comment on how to protect health maintenance organizations (HMOs), preferred provider organizations (PPOs), and other managed care plans. In addition, we received many other comments regarding HMOs that waive coinsurance and deductible amounts, and price reduction agreements negotiated by these and other types of health benefit plans. We are including these comments in this section.

Comment: Two commenters requested safe harbor protection for HMOs that waive the beneficiary's obligation to pay coinsurance and deductible amounts. They believed that this was a common practice among HMOs. In addition, a few commenters pointed out that some PPOs negotiate agreements with contract health care providers for those providers not to charge the health plan or enrollee for some or all of the coinsurance and deductible amounts they are owed for furnishing services to enrollees. Under such an agreement, when the contract provider bills the Medicare program directly (and not the health plan) and agrees to waive all coinsurance and deductibles, the commenters typically phrased the agreement as one "to accept Medicare payment as payment in full." One commenter specifically objected to this practice.

Response: We agree that protection should be given to prepaid plans with contracts and agreements with HCFA and State agencies for waiver of beneficiary obligations to pay coinsurance and deductible amounts. However, as will be discussed below, we do not agree that such protection is warranted at this time for PPOs and prepaid plans that do not have contracts or agreements with HCFA or State agencies.

Health plans offer a variety of incentives to attract beneficiaries to become enrollees. In many instances, HCFA permits such HMOs and competitive medical plans (CMPs) to waive the premiums attributable to the coinsurance and deductible amounts. Further, HMOs and CMPs under a risk contract with HCFA are required under certain circumstances to reduce coinsurance and deductible amounts or offer additional benefit options.

The routine waiver by a prepaid health plan of beneficiaries' obligation to pay coinsurance and deductible amounts is clearly distinguishable from such routine waiver by other health care providers, such as hospital outpatient departments, physicians, or durable medical equipment suppliers. Two principal characteristics distinguish a health plan's routine waiver of cost-sharing amounts from that of other health care providers. First, a health plan's routine waiver program is inextricably intertwined with the offering of a comprehensive package of covered benefits, and is not offered for the purchase of an individual item or service. Quite often, in the case of prepaid plans, the routine waiver of cost-sharing amounts is made in the form of a reduction or waiver of the beneficiary's premium and may also be combined with the offering of increased covered benefits. Thus, the routine waiver of cost-sharing amounts is generally not an incentive to use a particular item or service at the time it is furnished.

Second, although cost-sharing requirements can serve to control utilization, HMOs and other health plans under contract with HCFA or a State agency have built-in incentives to control unnecessary utilization, or have their utilization and costs monitored by HCFA or the State agency. Thus, the issue of potential overutilization (with increased costs to the programs) is adequately dealt with without resort to imposing the obligation on beneficiaries to pay coinsurance and deductible amounts.

Therefore, we expect to publish at a later date an additional safe harbor provision to protect prepaid health plans that have a contract or agreement with HCFA or a State agency where the health plan offers beneficiaries increased benefits coverage, reduced cost-sharing amounts (coinsurance, deductibles, or copayments), or reduced premiums where certain standards are met. Because of the limited scope of the comments we received on HMOs, PPOs and managed care plans, we expect to publish at a later date an interim final rule in order to solicit additional comments from the public on this new safe harbor provision.

This new safe harbor provision will not protect incentives offered to beneficiaries by health plans, such as PPOs, that are not operating under a contract or agreement with HCFA or a State agency. Unlike health plans with such contracts or agreements, we are not confident that all PPOs that engage in these negotiated waiver agreements properly protect the Medicare and Medicaid programs against overutilization. And we did not receive sufficient comments on the different types of PPOs for us to distinguish the characteristics of a PPO engaging in these negotiated waiver agreements where the Medicare and Medicaid programs are properly protected.

Comment: Several commenters requested the OIG to protect a variety of arrangements between HMOs, PPOs, competitive medical plans (CMPs), managed care plans, and other health plans on the one hand, and medical groups and other health care providers who furnish items and services to the health plans at a reduced price on the other hand. A few of these commenters observed the benefits that can be achieved when a health care provider offers discounts to these organizations. Several commenters recommended special treatment for relationships between HMOs and health care providers, such as physicians and hospitals, involving the leasing of space and equipment and contracting for personal services. One commenter requested special safe harbor protection for "[a]ll transactions between an HMO and contracting medical groups * * * if the medical group provides over 90 percent of its services to HMO members."

Response: We agree that there is a need to provide safe harbor protection for certain practices between managed care plans and health care providers. Thus, we are expecting to publish a rule that will protect many of these price reduction arrangements where certain standards are met. For the same reasons as stated above, we are expecting to publish this safe harbor provision as an interim final rule with an opportunity for additional comments from the public.

The safe harbor provision we are expecting to publish will only protect agreements between health plans and contract health care providers for the sole purpose of furnishing items and services covered by the health plan, Medicare, or Medicaid. In other words, for the reasons explained below, we are not protecting in this provision the contracts between health plans and contract health care providers for these providers to furnish services other than covered benefits, such as peer review and management services.

As with all safe harbor provisions, where two parties engage in a multi-faceted payment arrangement where protection is sought from more than one safe harbor, we expect separate justifications to be clearly set forth for each provision for which protection is sought. Where HMOs contract with physicians and other health care providers for the furnishing of services other than covered health care services, we believe that HMOs, PPOs and other prepaid health plans will be able to conform their arrangements to the appropriate safe harbor provisions. For example, many contract health care providers furnish peer review, marketing services, or pre-enrollment screening for HMOs. For the remuneration attributable to the furnishing of such services to be protected, it must comply with the personal service/management contracts safe harbor provision. Also for example, the remuneration attributable to the lease of space or equipment must comply with those respective safe harbor provisions.

We are not convinced that merely because a medical group has a large majority of its business with an HMO that a special across-the-board exemption for all transactions is warranted. HMOs operate under a variety of payment mechanisms, both with respect to the Medicare and Medicaid payments they receive and the payments they make to physicians. Although in many cases the incentive structure in which HMOs operate is designed to protect against overutilization of service, this incentive structure may not extend to fee-for-service arrangements.

Further, even though many HMOs have generally operated largely free of fraud and abuse problems, we are aware of some HMOs that have abused their contractual relationships with medical groups, where individuals in the groups have engaged in abusive activities on behalf of the HMO, or where the medical group has compromised the interest of beneficiaries in order to keep the vital HMO contract. In at least one case, a criminal conviction was obtained for such a practice. Although safe harbor protection is warranted for certain contractual relationships between health plans and contract health care providers, we also intend to use our authorities aggressively to monitor closely and, where appropriate, penalize any abusive relationships between these parties to assure that medically necessary services of a high quality are available and accessible to all enrollees.

4. Waiver of Beneficiary Deductible and Coinsurance Amounts

Comment: The OIG received numerous comments on the establishment of a safe harbor for waiver of hospital inpatient coinsurance and deductible (copayment) amounts owed by program beneficiaries. Many commenters requested the OIG to provide safe harbor protection for routine hospital waiver or partial reduction of inpatient fees not subsequently claimed as bad debts because the practice would benefit hospital inpatients without increasing program costs. Some commenters urged the OIG to protect the submission of bad debt claims where copayments were routinely waived for limited categories of patients, such as seniors. On the other hand, several commenters were concerned that permitting hospital waiver of inpatient copayments would encourage overutilization of hospital services and promote cost-shifting to patients with nongovernmental insurance policies.

Response: Since October 1, 1983, when the prospective payment system (PPS) for reimbursing hospital inpatient services was implemented, we have been aware of hospitals that routinely waive Medicare beneficiary deductibles and coinsurance charges for inpatient hospital services in order to attract patients. Because the waiver of patient charges constitutes an inducement to use services in exchange for something of value (the forgiveness of financial obligation), this practice violates the statute. However, assuming the waived amounts are not later claimed as bad debt, the practice appears to cause no direct financial harm to the Medicare program because hospitals receive a pre-determined payment amount under PPS regardless of their costs or charges. Moreover, due to hospital peer review requirements and the relatively fixed level of patient demand for hospital inpatient services, waiver of inpatient beneficiary fees is not likely to increase utilization significantly. Furthermore, if hospital waiver policies do not discriminate on the basis of length of stay or type of disease, the potential for program abuse appears minimal.

In addition, we know of no data, nor have commenters produced or referred us to any, indicating that routine hospital waivers of inpatient copayments owed by program beneficiaries will shift the costs of care to non-Medicare patients. Rather, we assume that most hospitals that choose to waive these amounts do so because the hospital more than makes up in increased volume for any initial "loss" resulting from not collecting the full amount to which it is entitled. Although we believe there is little risk of "cost-shifting" to the non-Medicare population, the first standard in this provision makes clear that any such cost-shifting is not protected.

We do not agree, however, that health care providers who choose to waive copayment amounts routinely for some or all of their patients should be permitted to claim such amounts as bad debt. Such a rule would muddle two very distinct Medicare policies. Traditionally, Medicare health care providers are reimbursed for uncollectible payments owed by beneficiaries. See 42 CFR 413.80. This rule requires, among other things, that health care providers make an indigence determination on a case-by-case basis, or reasonable collection efforts, prior to recouping bad debt losses from the program. See also Provider Reimbursement Manual, sections 310, 312, HCFA Pub. No. 15–1. Thus, payment of Medicare bad debts, unlike routine waivers of Medicare cost sharing amounts protected under this safe harbor regulation, are only authorized under certain conditions pertaining to the uncollectability of payments and the indigence of beneficiaries. Health care providers who routinely waive beneficiary copayments in accordance with this safe harbor regulation, and do not make case-by-case indigence determinations or otherwise prove uncollectability under 42 CFR 413.80, cannot deduct expenses as bad debt. Where such an unlawful expense is claimed, the hospital may be subject to civil or criminal prosecution.

Comment: Many commenters requested the OIG to extend safe harbor protection to waiver of patient fees imposed for a wide array of provider services. Several commenters sought protection for waiver of beneficiary copayments for part A services furnished by other cost-based health care providers, such as skilled nursing facilities and home health agencies. These commenters argued that where services are paid on a reasonable cost basis, just as where services are reimbursed under PPS, waiver of beneficiary copayments causes no financial harm to the program. Other commenters sought still broader protection under the safe harbor for copayments for services under part B, arguing that the limited protection granted for inpatient hospital copayments was discriminatory.

Response: We believe that protection is uniquely appropriate for waiver of patient charges related to hospital inpatient services. A routine waiver program will not likely increase patient demand for these services, since beneficiaries cannot admit themselves, and hospital overnight stays are inherently undesirable from a patient's perspective. Thus, it is unlikely that a routine waiver program will affect utilization. By contrast, cost-based fee-for-service health care providers, such as home health agencies and nursing homes, may be able to offset their losses resulting from their waiver of copayments by increasing their Medicare allowable costs. Such manipulation of reimbursement amounts would be virtually impossible to prevent. Thus, we do not believe that the protection offered under this safe harbor provision should be extended to routine waiver of beneficiary copayments by cost-based fee-for-service health care providers.

Routine waiver of beneficiary copayments by individuals or entities reimbursed on the basis of reasonable charges even more clearly affects program costs. When charge-based health care providers routinely fail to collect all or part of beneficiary copayments authorized by law, and then submit actual charges to Medicare as if copayment amounts were collected, these charges increase customary and prevailing rates which, in turn, inflate program costs. The Medicare Carriers Manual makes clear that in these situations, a health care provider is required to reduce his or her actual charge. See section 5220, HCFA Pub. No. 14. Thus, we believe that individuals and entities who fail to reduce actual charges submitted to Medicare are misrepresenting their charges, and may be subject to civil and criminal liability for submitting false claims.

We are aware that some local government health care providers, including county hospital outpatient departments, routinely reduce beneficiary payments at the time of service for the extremely indigent populations they serve. For these health care providers, offering patients the option of reduced payment at time of service may be a more successful collection strategy than subsequently billing patients for the entire copayment. This practice, while not protected by this safe harbor regulation, would not likely violate the statute so long as the partial forgiveness of the copayment obligation was strictly a pragmatic financial decision and not an inducement to patients to purchase medical services. We see no purpose in interfering in the mission of local governments or other hospitals that serve primarily indigent populations when they reduce beneficiary fees for those unable to pay. Such health care providers, typically, have no need to engage in sophisticated marketing strategies to induce more business.

Comment: One commenter advised the OIG that in accordance with 42 U.S.C. 254b(f)(3)(F) and 254c(e)(3)(F), federally qualified migrant and community health care centers are required to develop a sliding fee schedule for patients based upon ability to pay, which could result in waiver of part or all of the Medicare coinsurance and deductible amounts. These commenters argued that such waivers, although mandated under Public Health Service Act grant programs, could be deemed a violation of the statute.

Response: In section 4161(a)(4) of Public Law 101–508, the Omnibus Budget Reconciliation Act of 1990, Congress enacted a fourth statutory exception to the statute, which exempts a waiver of any Medicare Part B coinsurance by a Federally qualified health care center to any individual who qualifies for subsidized services under the Public Health Services Act. Thus, we are providing a safe harbor provision for this exception. In addition, we are making this safe harbor applicable to similarly situated individuals who receive services under the Maternal and Child Health Service Block Grant program (see section 505(2)(D) of the Act; 42 U.S.C. 705(2)(D), or who are Medicaid beneficiaries.

Comment: Six commenters argued that protecting routine waiver of beneficiary payments for inpatient hospital services would discourage competition from ambulatory surgical centers (ASCs).

Response: Although the granting of safe harbor protection for the waiver of inpatient copayments gives practitioners or their patients an incentive to choose inpatient hospital settings over outpatient settings, we believe that the activities of the PROs reasonably ensure that services are furnished in outpatient settings where appropriate. Therefore, we believe that the granting of safe harbor protection only for inpatient services is unlikely to draw patients away from ASCs and other outpatient settings.

Comment: A few commenters requested the OIG to protect waiver or discounts of inpatient copayments where hospitals and physicians offer this benefit not to patients directly, but to insurance companies, HMOs, or employer or union medical service plans, that have assumed liability for the beneficiary portion of payment under the terms of their insurance policies. Insurers offering these insurance benefits may attempt to negotiate with hospitals to reduce or eliminate the beneficiary portion of reimbursement in exchange for endorsing the hospital as a preferred provider or offering other tangible benefits.

Response: This safe harbor provision protects the waiver by hospitals of inpatient copayment amounts only where these amounts would otherwise be paid by Medicare beneficiaries themselves. In paragraph (k)(1)(iii), we have expressly made this provision inapplicable to negotiated price reduction agreements between health care providers and third-party payers, even where the reduction involves beneficiary copayments for which the third party payor has assumed liability as part of a Medigap policy. As we discussed in the section immediately above, we are expecting to publish an additional safe harbor provision to protect HMOs, CMPs and HCPPs under contract with HCFA or a State agency that waive coinsurance and deductible amounts owed by beneficiaries where certain standards are met.

Comment: Two commenters sought protection for the waiver of patient copayment amounts for the first eight days of care in a skilled nursing facility (SNF) after discharge from a hospital under the same ownership. These commenters stated that protection was needed to enable the smooth transfer of patients who were ill, and to allow hospital beds to be vacated for sicker patients.

Response: We understand that health care providers operating both hospitals and SNFs may, for entirely legitimate reasons, wish to continue waiving SNF copayment amounts when transferring hospital patients into the SNF for a brief period. In section III.D. below, we discuss in more detail the special considerations that exist where the hospital and SNF are wholly owned by a single "parent" entity, or where one of the facilities is the sole owner of the other.

Comment: One commenter requested the OIG to expand the safe harbor provision for waiver of hospital inpatient copayments to cover the provision of free items or services such as meals or presurgical overnight stays, samples of products from manufacturers, or blood screening and other testing services. The commenter suggested that such free gifts benefit patients without causing harm to the program, so long as there is no obligation to purchase additional items or services upon receipt of the free gifts.

Response: We decline to protect the offer of free gifts to beneficiaries within this safe harbor provision, as we have declined to protect this practice within the safe harbor provision governing discounts. The statute clearly contemplates that illicit remuneration may involve payments "in cash or in kind." The practice of offering free gifts may well induce beneficiaries to purchase additional or unnecessary items or services. Such inducements could easily become excessive, and there is no distinct financial or other cut-off point below which we could be sure that gifts remained non-abusive. Because we understand that such inducements are an area of significant abuse, we believe that protection of this practice would be unwarranted.

C. Provision-by-Provision Analysis of Safe Harbors

1. Investment Interests—§ 1001.952(a)

The OIG received close to three hundred comments on the issue of providing safe harbor protection for payments from investment interests. These comments are divided into three broad categories: (a) Comments on the proposed safe harbor provision for payments from investments in large publicly traded entities; (b) suggestions for safe harbors for payments from investments in small entities such as limited partnerships, about which we solicited comments, and (c) proposals for protecting payments from other investment interests. For convenience, we are discussing all of these comments in this section. Before discussing the comments and responses for these three broad categories of investment interests, we will discuss general issues raised with respect to investment interests.

Comment: We received a number of comments asking the OIG to clarify the types of investors and investment interests to be protected. In particular, we received many comments urging the OIG to protect indirect investment interests held by family members and to protect debt as well as equity investments.

Response: We are adding a definition of the terms "investor" and "investment interests" to this safe harbor provision. We are defining an "investor" to include both individuals and entities who either directly or indirectly hold an investment interest in an entity. Our definition includes examples, which are not intended to be an exhaustive list, of ways that investment interests may be indirectly held. For example, a family member of a referring physician may hold the investment interest in the joint venture entity, or a referring physician may have a legal or beneficial interest in an entity, such as his or her group practice, a trust or a holding company, where that entity directly holds the investment interest in the joint venture entity. In both cases, we view the physician as having the ownership interest in the joint venture entity.

In many cases we distinguish investors who do business with the entity in which they have invested from other investors who are exclusively seeking a return on their investment. We call an investor who does business with the entity as "an investor who is in a position to make or influence referrals to, furnish items or services to, or otherwise generate business for the entity." This classification is meant to include all investors who do business in any manner with the entity. Except as noted below, we do not limit this category to investors who actually make referrals. Rather, our focus is on the status of the investor and the ability to make or influence the referral stream or level of business activity for the entity. Such investors include not only physicians, but hospitals and other entities capable of influencing referrals.

We note that this category of investor doing business with the entity also includes those investors who furnish items and services to the entity as well as those investors who otherwise generate business for the entity. Thus for example, if a durable medical equipment (DME) supplier and hospital both enter into a joint venture to furnish DME to patients when they leave the hospital, both the DME supplier and the hospital fit within this category of investor doing business with the entity.

There are some very limited situations where, because of the special status or location of the investor, he or she does not fit within this category of investor doing business with the entity. For example, for the most part, retired physicians no longer make or influence referrals. In addition, typically a physician who resides and practices in a separate service area from the entity is similarly not "in a position to make or influence referrals." Or an investor could simply make an agreement barring him or her from actually making or influencing referrals to the entity. In all three examples, the determination whether an investor should be classified as doing business with the entity in which he or she has invested is a factual question. However, we will accept a written stipulation that for the life of the investment the investor will not make referrals to, furnish items or services for, or otherwise generate business for the entity. We emphasize that, because of the potential for abuse of this stipulation agreement, the investor must be bound to this agreement for the life of the investment as long as he or she remains an investor.

Finally, our definition of the term "investment interest" makes clear that debt as well as equity investments are protected.

a. *Large Publicly Traded Entities. Comment:* Several commenters questioned the relationship of this proposed safe harbor provision to the rules of the Securities and Exchange Commission (SEC) for the registration of securities. For example, some suggested that the OIG should exempt all investment interests that are traded on a publicly regulated exchange, while another suggested that public trading be an additional condition for protection. In addition, a variety of comments were received regarding the standards adopted from the SEC rules that, in order for payments from investment interests in an entity to be protected, the assets of the entity must exceed $5 million and the number of shareholders must exceed 500 persons (the so-called "$5 million asset/500 investor rule"). While some suggested the $5 million test was too high, one suggested that it was too low. One commenter suggested that the 500 shareholder test was too high, and another suggested that the OIG require either $5 million in assets or 500 shareholders, but not both. Finally, another commenter suggested that the OIG protect an investment in an entity any time the asset level was greater than $5 million.

Response: We intended to protect profit distributions made to referring investors in large publicly traded corporations where the investment interest was obtained at fair market value through trading on a publicly regulated exchange. The remuneration received by these investors is so tangentially related to their referrals that the potential for abuse is minimal.

As we stated in the preamble of the proposed rule, we adopted the SEC registration rules from 15 U.S.C. 78*l*(g) and 17 CFR 240.12g–1, which generally require entities with more than $5 million in assets and more than 500 investors to register with the SEC. At the time, we had believed that such a test would protect payments from only those entities that are actively traded on a national securities exchange.

Based on the comments we received and our experience in enforcing the statute, we believe that in many respects the SEC rules are not applicable for the purposes of protecting against abuse. In particular, the $5 million threshold is too low. An entity that owns two magnetic resonance imaging (MRI) machines may well meet this test. Thus, we are changing the asset threshold level from $5 million to $50 million. Publicly traded entities of this size are sufficiently large to assure that abuse is minimal.

In addition, the SEC's other criteria of 500 investors does not provide meaningful protection against abuse. We recognize that in many cases a large number of investors can dilute the influence of one investor's referral patterns on the level of payments that he or she receives. However, it has been our experience that many sham joint ventures try to obtain many investors, each of whom contribute nominal investments, as a mechanism to lock-in the loyalties of as many physicians as possible. Thus, depending on the factual circumstances of a particular joint venture, a large number of investors could either be abusive or minimize abuse.

We are making other revisions to this first investment interest safe harbor provision to provide greater clarity consistent with our original intent. Thus this safe harbor as revised contains two definitional prerequisites in paragraph (a)(1) for the type of entity we are protecting, and is followed by five standards, all of which must be met to the extent they apply to the investment interest in question.

For an entity to be protected under this safe harbor, it must meet two definitional prerequisites. The first prerequisite to qualify for protection is that the assets of the entity must be measured any time within the previous fiscal year or the previous 12 month period. This time period is different from the SEC rule, which we believe to be overly restrictive for the purposes of this safe harbor. The time period for measuring compliance which we are adopting will mean for all practical purposes that growing entities will be protected as soon as they reach compliance with all the preconditions and standards in this safe harbor, rather than having to wait for the next fiscal year as the SEC requires. In addition, the time period we are specifying permits an entity to retain safe harbor protection for a limited time period even though it is no longer in compliance with the $50 million asset threshold in this rule. During this time period, an entity will have the opportunity to bring itself back into compliance.

The second definitional prerequisite is that the entity must possess $50 million in the form of undepreciated net tangible assets. This clarification of what we mean by $50 million in assets removes many assets which we never intended to include within the scope of protection. We are excluding all intangible assets such as the company's valuation of its name recognition and stock and other forms of goodwill. We are excluding such assets because their valuation is too subject to "creative" accounting or appraisal techniques. The assets must also be reduced by any liabilities. Thus, a corporation only has $1 million of net tangible assets when it buys a $5 million piece of equipment with a $4 million loan. However, we are excluding from the calculation of assets any reductions in the value of assets due to depreciation. We believe it is inappropriate for an entity to lose safe harbor protection as a result of the aging of its assets. Further, we do not want to create incentives to replace equipment unnecessarily merely for the entity to regain safe harbor protection based on the value of new equipment. We are also clarifying that the reporting of net tangible assets must be based on net acquisition costs of purchasing such assets from an unrelated entity. The use of net acquisition costs in this rule is a generally accepted accounting principle, and makes clear that, for the purposes of this rule, we will not accept a company's use of current market valuations of assets. Further, we intend to use the Medicare related party rule, 42 CFR 413.17, to assure that the acquisition costs from the purchase of an asset is only based on a bona fide purchase through an arm's length transaction. Our final clarification in how to apply the $50 million asset test is that assets unrelated to a company's health care line of business cannot be used in the calculation of assets. For example, a nursing home corporation could be a subsidiary of a hotel chain. The hotel assets cannot be used for purposes of qualifying for the $50 million asset test. However, with the exception of the related party rule, it is not our intent to require corporations to be familiar with cost reimbursement rules of 42 CFR part 413. Tangible assets used in furnishing items and services may be counted even though they may not be allowable costs under part 413. The information necessary to determine compliance with this $50 million asset test is readily available in the accounting books of entities, and the accounting methods for determining compliance are fully consistent with generally accepted accounting principles. Thus, an independent certified public accountant should have little trouble certifying an entity's compliance with these requirements.

This safe harbor contains five standards, not all of which may be applicable in every instance. The first two standards, paragraphs (a)(1) (i)–(ii), which will be discussed here, focus on the nature of the investment interest. (The three remaining standards are being added in response to other comments which will be discussed below.)

The first standard (see paragraph (a)(1)(i)) applies only to an investment interest in an equity security, and requires such a security to be registered with the SEC under 15 U.S.C. 78*l* (b) or (g). We had considered but are rejecting an alternative standard that the investment interest must merely meet the SEC registration qualifications. This requirement of actual registration provides a clear bright-line rule, and is an indication of good-faith entry into the public securities markets, which is a significant factor underlying the rationale for this safe harbor. In addition, we are requiring the investment interest actually to be registered with the SEC because many exemptions exist to the SEC's $5 million asset/500 investor rule, which permit many entities to be actively traded but not to be registered with the SEC, and thus not under its oversight. See 15 U.S.C. 78*l*(g)(2). However, the SEC's reasons for granting an exception may not be consistent with the purposes of this rule, and thus we see no particular reason to protect securities simply because they qualify for an SEC exemption. We note that one such exemption under 15 U.S.C. 78*l*(g)(2) is for securities listed and registered on a national securities exchange. Such securities must comply with 15 U.S.C. 78*l*(b), and for the purposes of this rule we are requiring such securities to be registered with the SEC.

We are not applying the registration requirement to investment interests that involve debt securities because we believe that the extra safeguard of SEC registration is unnecessary. Publicly traded debt instruments, although protected under this safe harbor, are not the type of investment interests that are the focal point of this rule. Although the potential for abuse is present, we have not been apprised of the actual occurrence of abuse relating to these investment interests, and believe that their usefulness as instruments for inducing investors' referrals is more limited than equity investment interests.

The second standard (see paragraph (a)(1)(ii)) responds to the commenters' suggestions regarding public trading. We are adding a standard to this provision requiring the investment interest of an investor in a position to make or influence referrals to, furnish items and services to, or otherwise generate business for the entity to be obtained on terms equally available to the public through a registered national securities exchange, such as the New York Stock Exchange or the American Stock Exchange, or through the National Association of Securities Dealers Automated Quotation (NASDAQ) system. We note that we specifically intend to preclude safe harbor protection for securities traded through the so-called "pink sheets" or those "non-NASDAQ" securities that are traded through the OTC Bulletin Board Service. See, Securities Exchange Act Release No. 34–27975, May 1, 1990. This standard follows our original intent to assure that the investment interests of physicians or others in a position to influence referrals must be obtained through the kind of arms length trading that is normally associated with actively traded public securities at the fair market value through a publicly regulated exchange. Such public trading assures that the entity does not obtain capital by self-selecting investors based on their status as sources of referrals.

Although we are not requiring investment interests of other investors to be obtained through public trading, physicians and others in a position to influence referrals must strictly comply with this standard. We plan to closely scrutinize attempts to circumvent this standard. For example, any investment interest obtained before an entity becomes publicly traded is not protected under this provision. In addition, an investor is not protected by exchanging a limited partnership interest for shares in a newly formed entity that is publicly traded. Further, this standard precludes protection of payments from securities where physicians are afforded the opportunity to buy the available shares of an entity before other members of the public have the opportunity to invest in that entity. Such an entity would have only physicians as investors, and it is not our intent to protect payments from such entities. We expect the public to be afforded a genuine opportunity to invest in these publicly traded entities. Where referring sources (or their immediate families) hold a large proportion of the shares, we will presume that this standard has not been met.

Comment: A number of commenters suggested that the OIG expand this provision in a variety of ways to protect remuneration from debt as well as equity instruments and from entities other than corporations, such as partnerships.

Response: As discussed above, this safe harbor protects debt as well as equity instruments. We recognize that an ambiguity existed in our proposed rule in that our 500 investor test applied only to "a class of equity security" and thus appeared to prohibit debt instruments from qualifying under this safe harbor provision. However, this ambiguity is resolved by eliminating the 500 investor test. In addition as discussed above, we are exempting debt instruments from the SEC registration requirement contained in the first standard.

We also agree that investments in partnerships should be protected, and we are revising this provision accordingly, by adding a definition of investment interest.

Comment: A few commenters expressed concern that entities meeting the requirements contained in the proposed safe harbor provision could still be engaging in abusive relationships with individuals in a position to make referrals. One commenter suggested that we specifically protect against fraudulent cross-referral arrangements whereby investors in entity "A" are explicitly or implicitly encouraged to refer to entity "B" in return for entity "A" receiving the referrals from the investors of entity "B."

Response: We agree with the thrust of these comments, and are adding three standards (see paragraphs (a)(1) (iii)–(v)) to clarify our original intent and assure that investment interests are not used as inducements for referrals. One, the entity or any investor must not market or furnish the entity's items or services to passive investors in any manner differently than to non-investors. In other words, although an entity may seek referrals or other business from passive investors, it must promote and furnish its items or services to investors and non-investors in the same manner. An entity may not use a separate marketing approach or provide a different level of service to passive investors as opposed to non-investors. For example, in its promotional efforts, the entity may not in any manner appeal to or refer to such investor's position as an investor, and in serving customers it may not offer special arrangements to investors that are not available or are offered on different terms to non-investors. Any distribution to passive investors of individual or aggregate investor referral patterns would also not be protected under this provision. In addition, the entity or any investor must not promote the items or services of other entities as part of a cross referral agreement. One type of cross referral arrangement we are not protecting is the sham transaction described in the above comment.

Two, the entity must not loan funds to or guarantee a loan for an investor to use for the purpose of obtaining the investment interest. We do not believe protection should be afforded where an investor is loaned money from the entity, or from a parent or subsidiary corporation (or is guaranteed a loan by the entity or a related organization), and the investor makes an investment based on that loan. In such a situation, the investor is adding no real capital to the entity. We note, however, that safe harbor protection is available where the investor borrows from other sources, such as from his or her broker or a bank.

And three, the amount of payment in return for the investment interest must be directly proportional to the amount of the capital investment. Such payments are consistent with the type of corporate dividend payment that we are trying to protect.

We believe that these minor revisions, which are fully consistent with our original intent, should offer reasonable protection against the possibility of significant abuses without unduly restricting the types of entities that may qualify under this provision.

b. *Small Entities.* In the notice of proposed rulemaking we solicited comments on expanding the proposed investment interest safe harbor to protect payments from investments in small entities, particularly limited and general partnership interests. For limited partnership interests we suggested four standards for protection: (1) A bona fide opportunity to invest is made on an equal basis without regard to the investor's ability to make referrals, (2) no requirement is imposed on the investor to make referrals, (3) disclosure is made to the referred patient, and (4) payments are not related to referrals. As conditions for protection of payments from investments in general partnership interests, we suggested that disclosure of the investment interest be made to a referred patient and payments not be related to referrals.

Comment: A large number of people commented that, in view of the OIG's interpretation of the statute as not prohibiting all referrals to entities in which a physician has an investment interest, safe harbor protection should be provided for legitimate arrangements. While some commenters suggested that the OIG adopt generic criteria for analyzing these arrangements, others commented more directly on the proposed standards we suggested in the proposed rule. A few commenters suggested that any safe harbor protections should treat indirect ownership interests held by family members in the same manner as direct ownership interests to assure that investors who make referrals to that entity do not circumvent the intent of these requirements by having investments held in the name of family members instead of their own names.

The enormous response to this invitation for comment reflected the polarization of the health care community on this issue. Those supporting safe harbor protection emphasized that physician-investor joint ventures promote competition, provide quality services, promote patient convenience, bring needed services to communities, are cost effective, do not lead to over-utilization, do not compromise ethics, and enable services to be provided outside hospitals and physician offices. Those urging no safe harbor protection or expressing a need for stringent safeguards argued that these joint ventures hurt competition, compromise quality of care, are not in patients' best interests, increase costs, lead to over-utilization, and create conflict of interests between health care providers and patients.

A large number of commenters generally supported safe harbor protection for payments to those with managing partnership interests and agreed with the OIG's two suggested conditions for protection. However, a few commenters opposed such protection. In addition, a few commenters suggested that the OIG define which individuals would be protected under this provision.

Response: Because of the significant business investment activity in these small entities—typically joint ventures—and the advantages of permitting them in certain situations, we believe that safe harbor protection is warranted. However, we have also observed widespread abuses in many of these joint ventures. In particular, we believe that a large number of these newly formed entities are designed to have physicians as investors specifically to induce them to use the entity in which they have invested. Therefore, any safe harbor protection must include significant safeguards to minimize any corrupting influence the investment interest may have on the physician-investor's decision where to refer a patient. We are including a second investment interest provision (paragraph (a)(2)) that protects payments to investors who are limited and general partners, shareholders, or holders of debt securities where eight standards are met. We will discuss some of the definitional categories of persons who are protected under this provision, our response to comments recommending special protection for managing partnership interests, and our three categories that provide structure for the eight standards in this safe harbor.

We have classified "investors" as either "passive" or "active" because some of the standards apply only to those defined as "passive" investors. The definition of an "active" investor includes two categories of persons. The first category is modeled after a bona fide general partner in a partnership under the Uniform Partnership Act who is responsible for the day-to-day management of the entity.

We are including a second way to qualify as an "active" investor: the individual or entity must agree in writing to undertake the liability for the partnership, including the acts of its agents acting within the scope of their agency. We believe that such an affirmative act will assure that the individual or entity performs many of the same functions that general partners do who actively manage the day-to-day operations of the joint venture entity. For example, these active investors undertake the business risk that a typical general partner does, and will be interested in assuring that the day-to-day managers of the entity engage in sound business practices and not run afoul of the statute as well as other Federal and State laws and regulations.

"Passive" investors are those investors who are not active investors, such as limited partners in a partnership or shareholders in a corporation.

This second investment interest safe harbor provision includes some standards that must be met by both passive and active investors, and some standards that need only be met by passive investors, to the extent any exist in the joint venture. If an entity contains only active investors, the standards applicable only to passive investors would, of course, not apply. It must be emphasized, however, that the standards for this safe harbor must be met by all the investors in the entity. To the extent that one class of investors, such as active investors, qualifies, but the passive investors do not meet one of the standards, safe harbor protection is not given to payments to any investors in the entity.

In this regard, special attention must be paid to cases involving ownership interests held indirectly through other entities. Take a situation, for example, where a group of individuals are passive investors in entity "A", which in turn is the active investor in entity "B." For entity "B" to qualify under this safe harbor provision, entity "A" must meet all the requirements for active investor in entity "B," and the individual investors of entity "A" must meet all the requirements as passive investors in entity "B."

We believe that this provision will protect investment interests of those with managing partnership interests who establish limited partnerships that meet the standards of this provision. We have decided not to include a third investment interest provision at this time that would place fewer requirements on business structures composed entirely of active investors. We recognize that there are many legitimate small businesses structured in this manner where a group of individuals come together and all of them participate as hands-on managers in the day-to-day operations of the business and undertake personal liability for the entity. Historically, many hospitals were formed in this manner. And currently many group practices and other innovative health care delivery systems are being formed on a bona fide basis in this same manner. However, there are many new entities that have the same business structure, but that may be subject to abuse under the statute. Consequently, we have determined that it is inappropriate to implement a safe harbor provision at this time for entities composed exclusively of active investors that would not have to meet the standards we are implementing in this second investment interest provision. However, we are considering a new safe harbor provision for such investment interests which we anticipate publishing as a separate regulation.

The safe harbor provision we are including in this rule for investment interests in small entities was developed based on the standards we suggested in the proposed rule, the comments we received on our proposals and our continuing experience in enforcing the statute. This experience includes investigations of abusive joint venture arrangements, our Fraud Alert describing suspect features of these arrangements, and our Report to Congress entitled "Financial Arrangements Between Physicians and Health Care Businesses" (OIG, Office of Analysis and Inspections, May 1989). The Report to Congress disclosed in detail both the extensive ownership of joint ventures by physicians, and the additional services received by patients of these physicians as compared to all Medicare patients in general.

The standards for this provision are structured into three categories that we have identified as being of concern to us in joint venture arrangements: (1) The manner in which investors are selected and retained, (2) the nature of their business structure, and (3) the financing and profit distributions. To the extent possible, we have adopted bright line rules. We believe that this approach will facilitate compliance because investors will be able to determine easily whether they meet the conditions of safe harbor protection. As discussed in section III.A. above, we are not accepting commenters' suggestions for generic criteria. We believe that such criteria do not provide sufficient protection against abusive arrangements, nor do they provide meaningful guidance to delineate when a provider has complied with them.

The following discussion will be structured along the lines of the three problem areas we have identified.

(i) *Manner in which investors are selected and retained.* In this section we discuss the comments and our responses regarding the problem of the manner in which investors are selected and retained. The first five standards of this investment interest provision protecting small entities (paragraphs (a)(2)(i)–(v)) relate to this problem area.

Comment: The OIG received mixed comments on the first standard suggested in the proposed rule, that a bona fide opportunity to invest be provided on an equal basis to all investors without regard to their ability to make referrals. A large number of commenters expressed concern about the meaning and workability of this standard, particularly that it is vague and would be difficult to police. Several commenters construed this first suggested standard as a results-oriented test requirement, in other words, that joint ventures must be owned partly by individuals not in a position to make referrals. Some suggested that the OIG place a limit on the percentage of ownership of an entity that can be held by such referring investors. The percentages ranged from 5 percent to 85 percent ownership by referring investors. Others suggested that the OIG should not require these entities to have some amount of non-referring investors. One commenter specifically objected to a requirement that a joint venture have a majority of the ownership interests held by non-referring investors. Five commenters expressed concern that any requirement that investment interests be offered to non-referring individuals may be construed as requiring a public offering, thus triggering the necessity of complying with SEC rules (such as Regulation D governing the limited offering and sale of securities without registration under the Securities Act of 1933, 17 CFR 230.501 *et seq.*) or State "blue sky" laws which require public securities registration.

Response: We agree with the concerns expressed by most of the commenters about our first suggested standard. Thus, we are replacing it with three standards (paragraphs (a)(2)(i)–(iii)) in order to better address problems concerning the manner in which investors are selected. To comply with our first standard, investors who make referrals or who are in a position to make referrals or furnish items or services cannot own more than 40 percent of the value of investment interests within each class of investments in the entity. This standard requires not only that a bona fide opportunity to invest has been afforded to people not in a position to make referrals, but that these individuals hold at least 60 percent of the value of the investment interests in each class of investments.

In essence, we are switching a process measure with an outcome measure. As several commenters observed, our proposed standard of equal opportunity to invest contemplated that an equal number of referring and non-referring individuals would be given an opportunity to invest. Such a process-orientated test would have been virtually impossible to monitor. For example, such a standard would have required a joint venture to monitor all marketing solicitations, and determine the referral status of everyone who was solicited to make sure that an equal number of referring and non-referring potential investors were given the opportunity to invest. The alternative outcome measure we are adopting will provide a bright line test which will assist all the parties to the joint venture and the Department in determining whether compliance with this first standard has been achieved.

Although compliance with this "60–40 percent investment" standard will necessitate some monitoring data, we want to minimize the burden. Therefore, the joint venture is free to use any internal accounting principles it chooses to adopt so long as it uses such principles consistently over time so that it is not manipulating the data to obscure its noncompliance. In addition, we are establishing two alternative time periods in which compliance is to be measured. The measurement period can either be a joint venture's prior fiscal year or the previous 12 month period. For example, if a joint venture uses a calendar year as its fiscal year and wants to know in April 1990 whether it is in compliance with this standard, it may either look at the number and status of investors in 1989, or it may use its investor data from March 1989 through March 1990.

We expect that the parties to a joint venture will find it far preferable to use its prior fiscal year data because if that year's data shows compliance with this standard then the joint venture is in compliance for the entire current fiscal year. The alternative approach of a rolling 12 month average will enable a joint venture to reach compliance sometime within the current fiscal year so that it does not have to remain out of compliance for a full year. However, we also recognize that a joint venture using this rolling 12 month average that is being operated close to this 40 percent line may find itself in compliance one month and then out of compliance the next month. We emphasize that it is highly unlikely we will pursue an investigation of a joint venture where it complies with all the other standards in this safe harbor, is out of compliance with this 60–40 percent investment standard based on its prior fiscal year data, but is making a good-faith effort to reach compliance with this standard based on data showing compliance on a monthly basis for the most recent months of operation.

As previously discussed, for the purposes of complying with this 60–40 percent investment standard, we are classifying investors who provide items and services together with investors who make or influence referrals to the entity. This classification is necessary to preclude a supplier, such as a DME company, from forming a joint venture with referring physicians, giving them a 39 percent interest in the entity. It would be inappropriate to grant safe harbor protection to such an entity because all of the owners would be doing business with the joint venture by either furnishing items or making referrals. In order to remedy this problem, the DME supplier is classified with the referring physicians for the purposes of this 60–40 percent investment standard. Thus, for example, if a DME supplier and its referral sources want to be investors in an entity with which they will do business, to comply with this first standard, at least 60 percent of the value of the investment interests must be held by investors who will neither make referrals nor engage in business activity with the entity.

The second and third standards of this provision address the problems of discriminatory marketing strategies that result in the offer of better deals, for example, more shares or a better price, to individuals who will refer a high volume of patients. The second standard focuses on the *status* of investor and bars safe harbor protection where the terms of investment opportunities depend on whether a passive investor is in a position to influence referrals, furnish items or services, or otherwise generate business for the entity. The entity can offer investments to such investors only on the same terms as those offered to other passive investors not in a position to influence the flow of business to the entity. We are not imposing this standard on active investors because we recognize that it is precisely because of a physician's familiarity with the health care field that he or she may be chosen as a general partner and offered different investment terms from those offered to passive investors.

The third standard assumes that an investment interest is being offered to a person in a position to make referrals, but bars the offering of favorable terms based on his or her past or expected referrals or amount of business otherwise generated for the entity. This standard applies both to active and passive investors because we believe it is inappropriate to protect all investment interests where any investor, even general partners, can obtain more shares because they can be expected to generate more business for the entity. We recognize that there may be situations where it is not abusive to offer more shares based on this consideration, but we also believe that such a practice can have a serious potential for abuse.

With respect to the potential triggering of a public registration requirement under SEC rules or State "blue sky" laws, we believe that there is nothing in this provision that would compel such a result. Thus, we see no need to modify this provision.

Comment: In response to the OIG's proposal that no requirement be imposed on the investor to make referrals, many comments dealt with the issue of how investors are retained. Specifically, many commenters objected to requirements, which entities commonly place on investors, that investors must divest their interest if they no longer are able to make referrals to that entity. One commenter suggested that the OIG prohibit entities from distributing any information to investors about their referral patterns to that entity.

Response: We generally agree with these comments and have addressed them in the fourth and fifth standards of this safe harbor provision. (Paragraphs (a) (2) (iv) and (v)). The fourth standard bars the entity from requiring passive investors to make referrals or remain in a position to make referrals as a condition for retaining their investment. The fifth standard parallels the new standard for publicly traded entities and requires the entity and investors not to market or furnish items or services to passive investors in any manner differently than to non-investors. Some examples of practices that would not be protected are provided in the discussion above on the parallel provision for publicly traded entities. These two standards apply only to passive investors because, as we stated, we recognize that active investors are often sought out because they will help generate business for the joint venture.

This fifth standard also requires the entity and any investor not to promote the services of other entities as part of a cross referral agreement. As we noted in the previous section on publicly traded entities, an example of a cross referral arrangement that would not comply with this standard exists when investors in entity "A" are explicitly or implicitly encouraged to refer to entity "B" in return for entity "A" receiving the referrals from the investors of entity "B."

Comment: A large number of commenters supported the OIG's third proposal that disclosure of the investment interest be made to individuals for which a referral is made. However, some were opposed to such a requirement.

Response: For the reasons discussed in section III.B.2. above, we decline to adopt a disclosure requirement.

(ii) *Business structure.* In this section we discuss the comments and our responses regarding the problem of the nature of the business structure of joint ventures. The sixth standard (paragraph (a)(2)(vi)) relates to this problem area.

Comment: The OIG received a large number of comments relating to the business structure of joint ventures, and particularly on the problem that many abusive joint ventures exist primarily on the referrals from their investors. Many of these commenters alleged that such joint ventures are unable to compete for business in the open market on the basis of cost, quality and convenience. These commenters alleged that such joint ventures thereby hurt competition by unfairly "locking in" referrals from investors. However, one trade association reported from a survey of its members that, on average, 47 percent of the referrals to entities operated by its members came from non-investors. Many commenters also expressed concern that abusive joint ventures have no real business purpose, and that the four standards we suggested will not prevent abuse. Four commenters suggested that safe harbor protection be provided where the costs to Medicare and Medicaid are not increased. One commenter observed that, in many cases, the apparent lower costs of joint ventures are illusory because their hours of operation are shorter than those of hospitals. To assure that joint ventures do not raise costs or operate in an abusive manner, a large number of commenters suggested that the OIG require utilization review.

Response: We agree with the concern that entities protected under this safe harbor provision should not exist by relying on their business coming from referrals from investing physicians. In our experience, a large number of joint ventures are formed with the intent to encourage investors to refer patients to the joint venture. In many cases, the referrals from investing physicians dominate the joint venture's business so that it is does not have to compete for outside business and that it cannot survive without such referrals from its investing physicians. At that point, the business purpose of the joint venture becomes suspect.

We also agree with commenters who believed that the standards we suggested in the proposed rule will not sufficiently protect against abuse. Although some protection is afforded by the fifth standard we are promulgating which is discussed immediately above (that the entity may not treat a passive investor differently than non-investors), we believe that an additional bright line rule is necessary as a condition of safe harbor protection.

Therefore, the sixth standard in this provision requires that no more than 40 percent of an entity's gross revenue comes from referrals from, or items or services furnished by, investors. This "60–40 percent revenue" standard is reasonable, and, at least according to one commenter's survey of its members, appears to be achievable for many joint ventures.

This standard, as well as the first standard in this safe harbor provision, provide clear rules which assure that no protection is afforded to joint ventures that operate primarily on the referrals of physician investors. By requiring that no more than 40 percent of the joint venture's revenue come from investors' referrals, we help assure that revenues of these joint ventures come from a wider group than referrals from physician investors. And by limiting the number of investors who make referrals, we help assure that the profits from these entities are distributed to a wider group than referring physician investors. Thus, these two standards will help assure that joint ventures are not dependent on the capital and referrals of physician-investors.

As part of the Department's program to monitor business arrangements' compliance with these safe harbor provisions (see section III.A. above), we will report to the Secretary on the compliance with these two 60–40 rules (see § 1001.953). This report, which will be issued within 180 days of the publication of this rule, will evaluate whether compliance with these two 60–40 rules adequately controls abusive arrangements or whether more stringent requirements are needed.

As with the first 60–40 percent standard, we are permitting a joint venture to use any internal accounting principles it chooses to adopt so long as it uses such principles consistently over time so that it is not manipulating the data to obscure its non-compliance. In addition, we are establishing the same two alternative time periods in which compliance is to be measured. The measurement period can either be a joint venture's prior fiscal year or the previous 12 month period. Again, as with the first 60–40 percent standard, it is highly unlikely we will pursue an investigation of a joint venture where it complies with all the other standards in this safe harbor, is out of compliance with this 60–40 percent standard based on its prior fiscal year data, but is making a good-faith effort to reach compliance with this standard based on data showing compliance on a monthly basis for the most recent months of operation.

As noted above in the discussion of our definition of the term "investor," in applying these two 60–40 rules in situations where the joint venture entity is owned by other entities, we will examine the ownership structure of these other entities to determine whether they are owned by physicians who are referring to the joint venture entity. In such a situation, these physicians are considered to be investors of the joint venture entity, and their ownership interest must be offset by non-referring owners and the revenue they generate for the joint venture must be offset by referrals from non-investors.

We believe the suggestion that we require protected joint ventures to provide services at lower costs to Medicare and Medicaid is unworkable. Although such a feature is obviously a desirable goal, we believe that any analysis of the relative costs of services can only be accomplished meaningfully on a case-by-case basis. Examples of some of the areas such an analysis must examine include: (1) The reimbursement methodology of the service, (2) the patient population being served, (3) the hours of operation, (4) the bad debt and free care policies, and (5) the impact on costs and charges of depreciation of new equipment. These factors must be analyzed for both the joint venture entity and other competing entities to which a comparison is being drawn.

We believe that utilization review should be encouraged. However, there are many variables that distinguish a successful utilization review program from a sham. For example, utilization review may be conducted under contract by a Peer Review Organization or another independent contractor, or it may be conducted in-house. A critical feature of utilization review is that follow-up or corrective action occurs when a determination is made that a particular practitioner who is under review is engaging in aberrant or substandard behavior. Obviously this action can take many forms, ranging from barring the practitioner from further practice to taking no action at all. Because there are so many variables to an effective utilization review program, we believe it would be overly prescriptive and largely unproductive to impose such a requirement. Thus, we decline to include a utilization review requirement as part of this safe harbor.

(iii) *Financing and profit distributions.* In this section we discuss the comments and our responses regarding the problem of the financing and profit distribution of joint ventures. The last two standards (paragraphs (a)(2) (vii) and (viii)) relate to this problem area.

Comment: As discussed above, a large number of commenters argued that physician involvement in joint ventures is necessary because physicians provide needed capital. Several commenters, however, questioned whether investors are really generating capital for the joint ventures in which they invest. Many suggested that the OIG only protect an investor's capital in cases where the capital was genuinely at risk. In other words, if the investor's interest is obtained through a no-interest loan paid off through deductions from future dividend distributions, there was never really any capital placed in risk. Some suggested that the OIG protect investment interests even where the entity loans the investor funds which are then used to make the capital investment. One commenter reported results from a survey of its members that, on average, 60 percent of the investment from referring physician owners came in the form on non-cash investments (including debt guarantees).

Response: We agree that a new condition of safe harbor protection is needed to assure that the investments are bona fide, i.e., that investors' funds are genuinely at risk. Thus, the seventh standard of this provision parallels the new standard for the provision dealing with investments in large publicly traded entities: These entities cannot lend the funds or guarantee loans used to make the investment. Consistent with our first investment interest provision, other debt relationships are permitted. For example, the entity may borrow from the investor, and investors may borrow from other sources to obtain funds to use for the capital investment. But as we discussed above, where investors make their investment with money loaned from the entity, they are adding no real capital to it. Thus, this standard will help assure that physicians and other investors in fact provide new needed capital and that the joint venture is not in reality a sham to facilitate the distribution of payments for referrals.

Comment: The OIG received a large number of comments suggesting other protections to assure non-abusive financing arrangements and, in particular, urging the OIG to protect "nominal" investments. Many suggested that the OIG specify an upper limit on the amount an individual may invest, either in terms of a dollar amount or a percentage interest in the entity. Some specifically suggested a 5 percent limit. Three commenters took another approach and suggested a minimum capitalization amount, pointing out that many of the more abusive arrangements have minimal capital needs.

Response: We believe that individuals with a small investment in an entity may be just as likely as those with a large investment stake to be influenced to make referrals to the entity. Many of the more abusive joint venture arrangements of which we are aware offer only nominal investments to physicians. We believe that, in many cases, these nominal investment interests are designed to induce referrals or encourage the investor to otherwise generate business for the entity. In addition, by distributing the benefits of ownership to as wide a base of physician investors as possible, these joint ventures seek to lock-up their market, and thus operate in an insulated business environment largely free from normal competitive pressures such as pricing constraints.

We believe that it is not useful to impose a minimum capitalization requirement. Because each joint venture has different capital needs, it is not possible to specify one level of capitalization that would represent a reasonable floor for all joint ventures. For example, requiring at least $500,000 in capitalization would obviously be viewed very differently by a laboratory joint venture than by a magnetic resonance imaging joint venture. We do believe, however, that it is useful to analyze joint ventures on a case-by-case basis to determine what the real capital needs of the project are, and whether the capital that has been invested is merely a sham to pay investors for referrals.

Comment: We received a large number of comments on one of the standards suggested in the preamble to the proposed rule, that payments not be related to referrals. We also received other comments relating to the general problem of the manner in which profits are distributed. Many commenters suggested that the OIG limit the return on investment which will be subject to protection. Some suggested merely that the return be "reasonable," while another commenter stressed that there is no realistic way to determine an appropriate cut-off for a return on investment that would still be classified as "reasonable." One commenter suggested that, because there is less potential for abuse with repayments on debt instruments, the OIG should treat these payments differently from profit distributions.

Response: The eighth standard in this provision is that the amount of payment to each investor must be directly proportional to his or her capital investment. In other words, to receive protection, dividend payments can only be tied to the number of shares owned by an investor, and not to his or her referrals. Where investors, such as general partners, contribute capital in the form of pre-operational services or sweat equity, their dividend payments may reflect the fair market value of those services rendered.

This standard in no way protects payments to active investors for operational services they provide to the joint venture. By its very terms, this provision only protects payments that represent a return on investment. Safe harbor protection for the personal services that an active investor renders would be governed by the "personal services and management contracts" provisions (paragraph (d)).

With respect to limiting the return on investment, we believe that it would be arbitrary to specify a limitation applicable for all joint ventures, and that it would be meaningless to merely specify as a general criterion that the return "be reasonable." As many commenters pointed out, a reasonable return can be appropriately measured only in light of the risk of the investment. An investor would surely expect a much higher return from an investment in an expensive piece of diagnostic equipment that might soon become obsolete than from an investment in a relatively inexpensive piece of equipment that can be expected to generate a steady profit stream for the foreseeable future.

With respect to repayments on debt instruments, we believe that it is unnecessary to create a separate provision for debt instruments, but, as discussed in section III.C.1.a. above, this provision is written to protect a variety of payments in securities, including debt instruments.

c. Proposals for New Safe Harbor Provisions

A large number of comments were received urging the OIG to provide special protection for investments in certain special circumstances which would not qualify under the safe harbor provisions suggested in the proposed rule.

Note: Any discussion below indicating that we are considering a new safe harbor provision should in no way be construed as legalizing the business arrangement at this time.

Comment: A large majority of these commenters requested protection for ambulatory surgical centers (ASCs). Many of these commenters believed that the OIG was attempting to eliminate ASCs. In presenting the benefits of ASCs, these commenters made many of the same arguments discussed in section III.C1.b. above, regarding the positive features of joint ventures in general. In addition, many commenters emphasized the unique features of ASCs: (1) They are subject to peer review; (2) they provide services at lower prices than hospitals; (3) they were formed to a very large extent by physicians, and (4) in many cases, they are really an extension of a physician's practice. Several other commenters suggested protection for payments from other types of entities based on a rationale similar to this latter "extension of practice" argument. For example, commenters wanted protection for physicians providing inpatient services for their patients, nephrologists performing services at renal dialysis facilities, pathologists examining test results in laboratories, and radiation therapy oncologists performing radiation therapy services at outpatient centers.

Response: We understand that a special situation may exist when a physician sees a patient in his or her office, makes a referral to an entity in which he or she has an ownership interest and performs the service for which the referral is made. In such a situation, Medicare makes payment to the facility for the service it furnishes, which may result in a profit distribution to the physician. And the physician may also receive reimbursement from the program for performing the professional service.

We believe that, with respect to the physician's own fee, such a referral is simply a referral to oneself. It should not matter whether the patient is first seen at the office or at the facility. Consequently, we believe that, in this situation, both the professional service fee and the profit distribution from the associated facility fee that are generated from this referral may warrant protection. However, we remain concerned about the investing physician's ability to profit from any diagnostic testing that is generated from the services he or she performs. We are also concerned about the extent to which we should modify this second investment interest safe harbor to protect a physician-investor's profit in other joint venture entities where he or she both makes a referral and performs some level of service for the referred patient at the entity. Therefore, we are considering a safe harbor provision, that we anticipate publishing as a separate regulation to protect these payments where there is no likelihood of abuse.

We believe that a broader exemption at this time for payments from ASCs and similar entities is not appropriate. We recognize that many of these entities, and ASCs in particular, have operated under the Medicare and Medicaid programs largely without abuse and have saved these programs money when compared to some alternative treatment settings, particularly inpatient hospital care. We also recognize that one of the fundamental purposes of the statute is to prevent abusive business arrangements that increase cost to the Medicare and Medicaid programs. However, our approach is one of providing standards that define categories of business arrangements and business practices that will be given safe harbor protection. Our approach is not one of providing protection to particular categories of health care providers who earn it by being lawful or cost-effective.

We remain concerned about the widespread apprehension expressed by those commenters with an ownership interest in ASCs. Many commenters did not understand that the investment interest safe harbor provisions upon which we invited comment would protect many of the situations about which the commenters claimed no protection was being offered. In addition, as we made clear in section III.A. above, when an investment interest does not qualify under one of the safe harbor provisions, it does not mean that prosecution is imminent. The business arrangement may not even violate the statute, or, after examination on a case-by-case basis, we may conclude that prosecution is not warranted. Our disinclination to provide blanket protection for all investment interests in ASCs does not mean that we hold them in disfavor.

2. Space and Equipment Rental and Personal Services and Management Contracts—§§ 1001.952 (b), (c), and (d)

Comment: An overwhelming number of commenters criticized the restrictive definition of fair market value in the safe harbor provision for space rental. Many expressed concern that the safe harbor does not exempt rental payments that take into account added value attributable to a rental property's intended use as a facility for furnishing medical, laboratory, or other health services. Some were disappointed that this safe harbor provision does not appear to allow adjustments in rental charges for special construction or renovation costs incurred by the lessor to make the space suitable for furnishing medical services. Other commenters argued that the added value to providers of locating in a building or area proximate and convenient to other health care providers is a legitimate factor in calculating rent and may bear no relationship to prospective referrals of Medicare or Medicaid program business. They contended that the close proximity of rental property to other health care providers justifies elevated rent because both providers and their patients view such location as a convenience.

Response: The safe harbor provision for space rental does not contemplate a single figure for fair market value. Rather, it contemplates a rental fee falling within a reasonable commercial range, but not taking into account any value attached by either party based upon the property's proximity or convenience to referral sources. To the extent there is a nexus between the location of property and the opportunity to engage in business reimbursable under Medicare or Medicaid, rental charges that take location into account may impermissibly generate referrals or other health care business. For example, we believe that a fair inference may be drawn that impermissible payments are being made when a group of doctors owns a medical arts building and rents space in that building to a diagnostic laboratory, and the rent is substantially above the laboratory' s cost of renting the same sized space at a nearby location.

Consequently, we decline to extend safe harbor protection to space rental charges that take into account any value attached to property due to the proximity of referral sources. We have modified the definition of fair market value in this provision to clarify that protection does not extend to rental charges reflecting the value attributed by either party to the proximity or convenience of property to potential sources of referrals or other business from the other party. However, we would note that where the lessor is a real estate developer or other entity not involved in the delivery of health care services, any arrangements that encourage referrals between the lessee and other third parties would not likely be scrutinized by the OIG.

However, we recognize that there may be instances where rental fees for medical, laboratory or other health related office space are justifiably higher than the market price for comparable commercial property. For example, we agree with commenters who stated that the cost of leasehold improvements needed to make space suitable for the furnishing of medical services (such as extra plumbing or electrical costs) should be considered within the provision's definition of fair market value. Accordingly, we have further amended this safe harbor's definition of fair market value to delete the requirement that fair market value not take into account the intended use of rental space. However, we have retained the requirement that rental payments be commensurate with the fair market value of equivalent commercial property, and decline to extend blanket safe harbor protection to rental arrangements that reflect the added value a hospital places on having referring physicians located in a medical building the hospital owns on its property. We recognize that this requirement will preclude safe harbor protection for many health care providers who lease space to physicians or suppliers at a reduced rate due to the favorable location of the property. In particular, hospitals that give rent concessions to staff physicians leasing private office space may not fall within the safe harbor. For a discussion of how such payments may qualify as part of a physician recruitment effort, see section III.D. below.

Comment: A few commenters inquired whether rental arrangements involving both the use of office space and the furnishing of personal or management services must meet the requirements of both safe harbor provisions in order to be protected from liability under the statute.

Response: In section III.A. above, we addressed generally the circumstances under which the requirements of two relevant safe harbor provisions must be met in order to be protected under this regulation. However, because several commenters specifically requested guidance about contracts involving the rental of space and the furnishing of personal services, we are responding to their comments here.

To the extent that office rental payments include the value of other personal services furnished as part of a business arrangement, the payments must reflect the fair market value of the rent and these personal services in order to qualify under the safe harbor regulation. To be exempt from kickback liability, arrangements involving remuneration for rental and personal services must meet the conditions of each provision. For example, where a mobile business provides diagnostic services to patients in physicians' offices, and contracts for diagnostic equipment or for cleaning, billing or other services in addition to renting office space from these physicians, the arrangement must qualify under the provisions for space and equipment rental and personal services and management contracts.

Comment: Several commenters, expressing support for a strong and effective anti-kickback statute, stated that sham office leases in which the space is not actually used are among the most common and abusive kickback schemes. Examples of such abusive schemes cited by commenters included physicians who entered into office rental contracts with other referring physicians, solely in order to obtain the referrals, and diagnostic services companies and clinical laboratories that lease space from physicians which the laboratories in reality do not use, as kickbacks for the physicians' patient referrals.

Response: We agree that sham contracts in which remuneration is exchanged for property that does not exist or space which is not used are among the most egregious kickback arrangements. We have become aware of office rental arrangements in which the "space" rented may not be large enough or otherwise suitable to perform any services for which rent could legitimately be paid. For example, a physician may rent office space to a clinical laboratory, allegedly in order to provide space to furnish laboratory services, when the space (often a closet or anteroom not useable for such purposes) is not actually occupied by laboratory personnel at any time. If the physician refers most or all laboratory work to this lessee, the "rent" is simply remuneration for referring laboratory work.

We believe, however, that these safe harbor provisions are sufficient to protect against this abuse. These provisions require that the amount of payments for rent, equipment or personal services contracts not take into account the volume or value of referrals or other business generated between the parties. If a sham contract is entered into, which on paper looks like it complies with these provisions, but where there is no intent to have the space or equipment used or the services provided, then clearly we will look behind the contract and find that in reality payments are based on referrals. Thus, these contracts would not be protected under these provisions.

Comment: Two commenters stated that the safe harbor requirements for determining fair market value of rental space should be the same requirements of section 501(c)(3) of title 26 of the United States Code, the Internal Revenue Code section governing tax exemptions for nonprofit institutions. Under this section, fair market value assessments are necessary to determine whether hospital/physician arrangements result in the prohibited inurement of private benefit to individuals.

Response: We do not believe that procedures for assessing the fair market value of hospital/physician arrangements under the Internal Revenue Code are relevant to safe harbor requirements under the anti-kickback statute. The anti-kickback statute is concerned with prohibiting fraud and abuse by individuals and entities participating in the Medicare and Medicaid programs; a statute providing tax exemptions to nonprofit institutions under specified conditions does not share this focus. The requirements we have set forth for determining fair market value under the safe harbor regulation are not undermined by the fact that they do not replicate the requirements under the Internal Revenue Code. Moreover, we cannot see, nor has any commenter adequately explained, how these regulations impede health care providers' ability to obtain tax exempt status under the Internal Revenue Code.

Comment: Commenters requested clarification as to whether these safe harbor provisions protect any types of percentage, "per use" or "per procedure" leases or contracts in which the amount of compensation fluctuates in accordance with the actual use of premises or equipment, or the frequency of services performed. A few commenters inquired whether percentage leases between parties in a position to refer Medicare or Medicaid business were a *per se* violation of the statute. Many commenters urged the OIG to extend safe harbor protection to per use equipment leases, and to percentage contracts for personal services, in which total business, in contrast to referral business, is the basis for payment. With regard to equipment leases, several commenters argued that these provisions should protect equipment lessors who receive higher rent based on increased use, because the useful life and value of equipment depreciates with use.

Response: As we explained in section III.A. above, in discussing wear and tear clauses, percentage or per use agreements between health care providers in a position to refer Medicare or Medicaid business threaten to violate the statute because the payments in these arrangements are directly tied to the volume of business or amount of revenue generated, providing an improper incentive to refer. Moreover, historically, percentage leases and contracts have been rife with abuse.

These sorts of arrangements need to be examined on a case-by-case basis. For example, a lease to a hospital of major medical equipment, such as a magnetic resonance imaging scanner, may specify that higher rent is to be paid when more than a predetermined number of procedures is performed. Such an arrangement can be troublesome if the lessor is a partnership of radiologists on the hospital's medical staff, because the incentive for overutilization is clear. It is the nature of the relationship, if any, between overall volume of use and referrals, that triggers the statute. Thus, if the owner of equipment were not in a position to make referrals to the lessee, the agreement would not violate the statute.

For these reasons, we specifically decline to protect rental charges or compensation for personal services where the aggregate amounts of payments are not set out in advance. This does not mean, however, that percentage or per use leases and contracts that are based on overall volume (including business from referral sources with no financial interest to motivate them), are *per se* violations of the statute. We recognize that legitimate considerations, such as the depreciation of equipment, could result in some part of the payment to be based on a percentage or "per use" payment arrangement without these payments influencing or being influenced by Medicare or Medicaid referrals. However, the more the payments appear to reflect the volume of referrals from the financially-interested party, the more suspect the arrangement becomes and the more likely we will need to examine it carefully.

Comment: Many commenters were opposed to the condition that space and equipment leases and personal services and management contracts run for periods of not less than one year. They argued that the one year condition was superfluous, given additional restrictions relating to fair market value and referral relationships between the parties. They also argued that the one year rule would preclude many legitimate short-term arrangements, such as leases of state-of-the-art imaging equipment by health care providers who could not afford a full year's lease. Some health care providers claimed that the rule would cause them to forsake good business judgment in order to obtain needed equipment or services.

Commenters were most concerned about the one year requirement in the context of personal services and management contracts. Several commenters argued that many professional services typically contracted for by health care providers, from medical or surgical consulting services to peer review functions, involve projects or activities that require less than one year to complete. They argued that it is inefficient and wasteful for health care providers to enter into contracts for periods of one year under these circumstances. Additionally, a few commenters sought clarification as to the effect of the one year rule on leases terminated for cause prior to the expiration of a contract extending one year or longer. In particular, there was concern that the conditions of the space rental safe harbor not conflict with Internal Revenue Service guidelines governing advance determinations of tax exempt status. These guidelines require tax exempt facilities to be able to terminate, within 90 days notice, contracts with non-exempt persons where compensation is based on fees charged for services furnished by the non-exempt persons.

Response: We have retained the one year contract requirement as a condition for safe harbor protection under the space rental, equipment rental, and personal services and management contracts safe harbor provisions. We included the one year rule limitation in these provisions because we are concerned about abuse resulting from periodic renegotiation of ostensibly short term agreements, in response to changes in referral patterns. For example, if a health care provider rents office space to another individual or entity with whom he or she is in an ongoing referral relationship, and these providers alter their rental terms with frequency, the volume or value of referrals can influence the size of renegotiated rental payments. When rental charges are constantly subject to modification, the threat to the lessor of receiving reduced rent, or the threat to the lessee of paying higher rent, may improperly induce increased referrals. However, we recognize that health care providers may enter into short-term leases or services contracts for legitimate business reasons and not on account of referral opportunities. For example, an academic physician who spends one semester or school year visiting at another medical university may need to rent office space from the medical university for less than a year.

Several commenters expressed concern that contracts for the performance of activities or services that, by their very nature, take less than one year, would necessarily fall outside the safe harbor provision for personal services and management contracts. However, the one year contract requirement restricts the period within which contract terms may not be changed, and not the time within which services under a contract may be performed. So long as contract terms are not altered within a one year period, an agreement that is performed in less than one year's time will meet the one year requirement in the safe harbor provision.

With regard to the comments we received concerning early termination clauses in leases or contracts extending not less than one year, we acknowledge the customary use of such provisions for tax and other legitimate business purposes. The legitimacy of an early termination clause in a lease or contract which otherwise meets the conditions of these three provisions depends on the parties' intent. Termination "for cause" clauses drafted in compliance with Internal Revenue Service or other legal or regulatory requirements should not jeopardize safe harbor status, if the purpose of the termination clause is to comply with those requirements, and not to facilitate renegotiation of contract terms. If a contract is terminated in accordance with a legally enforceable termination clause, the failure to renew the contract would provide evidence that the termination was effectuated for a legitimate purpose.

Comment: The safe harbor provisions governing space and equipment rental and personal services and management contracts provide that when the property or service is to be provided on a periodic, sporadic or part-time basis, the agreement must specify precisely the timing and duration of rental periods and compensation charged for each period. Numerous commenters were troubled by these requirements. They argued that furnishing professional services and leasing space and equipment on an "as needed" basis are commercially acceptable, cost-effective business practices that should be protected so long as the rate of compensation is commercially reasonable. They also stated that under many periodic lease and contract arrangements, precise intervals of activity or use, and the exact compensation for these intervals, cannot feasibly be specified in advance. In addition, there was concern that requiring specificity of time intervals and compensation as conditions for safe harbor protection would interfere with the flexibility necessary to accommodate changing demand, and would increase costs in situations where the demand proved lower than expected at the time the contract was made. Finally, a few commenters asked for clarification of the meaning of the word "periodicity" in these three provisions when the space or equipment lease or personal services agreement is not on a full-time basis.

Response: Part-time contractual arrangements and periodic access leases between health care providers are especially vulnerable to abuse because they are subject to modification based on changing referral patterns between the parties. For example, an optometrist who pays *ad hoc* "rent" to an ophthalmologist for the time spent in the physician's office examining only referred patients, is impermissibly paying for the referrals. In order to avoid the potential for abuse inherent in part-time business arrangements between parties in actual or potential referral relationships, we have limited safe harbor protection under these three provisions to periodic leases and contracts which set forth the timing, frequency, and length of services or intervals of use.

We recognize that health care providers, for various reasons, may be unable to specify the timing or duration of business arrangements, or the precise compensation involved. For example, compensation under a management contract requiring the furnishing of supplies and the hiring of personnel may need to vary depending on the costs of the supplies and number of personnel. Or, a health care provider may contract with an allied health practitioner group (such as a physical therapy group) to pay a specific amount per hour of care provided, without being able to anticipate the scheduling of services in advance. We believe that part-time leases or service arrangements that do not meet safe harbor standards need to be analyzed on a case-by-case basis under the statute. Many periodic contracts of this sort would fall outside the statute because the compensation involved is not linked to referral opportunities. A contract to serve as medical director of a small clinic on a part-time basis, for example, is not likely to involve activities or compensation tied to the referral of patients or to arrangement for services reimbursable under Medicare or Medicaid programs.

Finally, we are deleting the word "periodicity" from these three provisions because it duplicates the requirements that the rental or equipment lease or personal services agreement specify the schedule of intervals, their precise length, and payments for the intervals.

Comment: Three commenters requested the OIG to protect marketing and advertising activities because such activities either promote competition or do not violate the statute.

Response: The statute on its face prohibits the offering or acceptance of remuneration, *inter alia*, for the purposes of "arranging for or recommending purchasing, leasing, or ordering any. . . service or item" payable under Medicare or Medicaid. Thus, we believe that many marketing and advertising activities may involve at least technical violations of the statute. We, of course, recognize that many of these advertising and marketing activities do not warrant prosecution in part because (1) they are passive in nature, i.e., the activities do not involve direct contact with program beneficiaries, or (2) the individual or entity involved in these promotions is not involved in the delivery of health care. Such individuals or entities are not in a position of public trust in the same manner as physicians or other health care professionals who recommend or order products and services for their patients. Thus, we agree that many advertising and marketing activities warrant safe harbor protection under the personal services and management contracts safe harbor.

However, we have experienced many instances where promoters and consultants have become involved in marketing activities that encourage health care providers and others to violate the statute, such as to develop impermissible joint venture arrangements or to routinely waive coinsurance and deductible amounts owed under Medicare Part B. It would be inappropriate to allow such activities to receive safe harbor protection.

Thus, we are adding paragraph (d)(6) to this safe harbor provision to make clear that the service that is contracted for is not protected if it involves the counselling or promotion of a business arrangement or other activity which itself constitutes a violation of any State or Federal law. However, the safe harbor (revised as indicated) protects contracts where the individual paid under the contract counsels or promotes business arrangements or other activities that are either specifically exempted under one of the provisions of this regulation or otherwise do not violate the statute.

Comment: Four commenters sought specific protection for commission sales arrangements between health care providers and independent contractors.

Response: We see no reason, nor has any commenter claimed to have provided one, for treating commission sales agreements differently under these regulations from other types of contracts for personal services performed by independent contractors. Therefore, commission sales agreements must meet the conditions of the safe harbor provisions governing personal services and management contracts.

3. Sale of Practice—§ 1001.952(e)

Comment: While many commenters supported the one-year limitation on the completion of a sale of a practice, others believed that it is too short. One commenter asserted that such a limitation would effectively ban ›ption agreements on sales of physicians' practices.

Response: We decline to protect option agreements or sales which extend beyond one year because, as we stated in the preamble to the proposed rule, we believe that this is an area of significant abuse. Often, sales and option agreements are designed solely to ensure referrals, and payments for the sale or option agreement are actually payments for referrals. The one-year limit serves to protect sales where the sale occurs because the physician is no longer going to be practicing and not because the purchaser seeks an ongoing stream of referrals. To the extent that one can enter into an option agreement, exercise that option and complete the purchase of the practice within one year from the date the option agreement is entered into, this aspect of the transaction will fall within this safe harbor provision.

Many commenters appeared confused about whether the provision requires payments from the sale to be completed within one year. This provision does not preclude a purchaser from making payments to a practitioner beyond the one-year period as long as the other conditions of this provision have been met.

Comment: Many commenters strongly supported the one-year grace period from the date of a purchase agreement to complete the purchase, and during which time referrals would be permissible. One commenter believed this period should be shortened to six months, but others stated that it should be longer than one year.

Response: We were presented with no persuasive reason to extend or shorten this one-year period and we therefore decline to revise this limitation period.

Comment: Several hospitals requested protection for their purchases of the practices of retiring physicians.

Response: When a hospital purchases a physician's practice and thereafter there are no referrals from that physician to the hospital, the statute would not appear to be implicated. Accordingly, in ordinary circumstances, a hospital is not in violation of the statute if it purchases the practice of a retiring physician who no longer makes referrals to that hospital.

However, many hospitals engage in this practice as part of a physician recruitment effort. Such activities do implicate the statute, but we are considering a new safe harbor provision, that we anticipate publishing as a separate regulation, to protect many such recruitment activities.

Comment: Several hospitals requested that their practice of buying physicians' practices for fair market value and then retaining the physicians on staff be afforded the protection of a safe harbor. They asserted that the financial pressures of maintaining private practices have drawn physicians to hospitals in order to get management assistance and capital.

Response: As we stated in the preamble of the proposed rule, hospitals often purchase physicians' practices in order to ensure the hospital of a steady stream of referrals. We continue to believe that such practices lead to increased program costs and potential conflicts between the patient's best interests and the physician's business relationship to the hospital. Accordingly, we decline to protect a practice that often leads to the very abuses that the statute is designed to prevent.

Comment: Several commenters requested safe harbor protection for the sale of an individual's practice to a group practice or the sale of part of a practice to another physician or group practice when the physician chooses to change the scope of his or her practice.

Response: We recognize that some buy-out arrangements are not abusive, and we would not want to prosecute such arrangements. However, we are also aware of abusive purchase arrangements, such as between ophthalmologists and optometrists, where one practitioner or group practice seeks to buy another practitioner's practice as a condition for continuing to make referrals. In essence, the sale becomes another mechanism for the buyer to profit from the stream of referrals made to the seller who previously practiced independently without dividing profits with the new "partner." No commenter proposed standards for a safe harbor provision that would cover only arrangements that are not abusive, and we are skeptical that such standards can be formulated. Accordingly, we have not protected this very diverse category of sales of practices. Rather, we are considering a limited new safe harbor provision for the purchase of group practices that we anticipate publishing as a separate regulation.

Comment: Two commenters asked the OIG to clarify the relationship between the safe harbor provision for the sale of a practice and the employee exception.

Response: Where a practitioner purchases another practitioner's practice, makes payments to that other practitioner which continue for some period of time, and retains that other practitioner on his or her staff as an employee, we believe that such payments are not protected under this provision or the employee exception. They do not qualify under this provision because the practitioner who sold the practice remains in a position to make referrals. The payments are not protected by the employee exception because that provision only protects payments "for employment in the provision of covered items or services * * * ." These payments, however, relate to the purchase of a practice and not to services provided pursuant to employment for the provision of items or services. Of course, the employing practitioner who has bought out the other practitioner is making other payments for such employment services, and if a bona fide employment relationship as defined in 26 U.S.C. 3121(d)(2) exists, then these payments are protected under the employee safe harbor provision. As noted in the General comments section in section III.A. above, where parties are attempting to comply with two safe harbor provisions, we would expect separate justifications for compliance with each provision.

4. Referral Services—§ 1001.952(*f*)

Comment: Many commenters urged the OIG to extend this safe harbor provision beyond only physicians to include payments by chiropractors, dentists, podiatrists, psychologists, nursing homes and other health care providers to entities that refer members of the public to them.

Response: We agree and have revised this provision to protect payments by practitioners and other health care providers who utilize referral services.

Comment: Many commenters requested that the OIG define the term "qualified" with respect to the requirement that a referral service not exclude any "qualified" health care provider from participation in the service.

Response: Whether a particular health care provider is "qualified" as a participant in a referral service will vary depending on how the service is organized. For instance, to be qualified as a participant in a referral service run by a hospital, it may be necessary that the participant be an employee of that hospital. On the other hand, a referral service run by a professional organization may require only that the participant be a dues-paying member of that organization to qualify for participation. The determination as to whether a particular health care provider is "qualified" to participate in the service may be made by the referral service according to its own criteria. To be protected under this safe harbor, the referral service must apply the eligibility criteria equally to all participants in the referral service.

In addition, the referral service must disclose to all persons seeking a referral the criteria it uses to determine who is qualified as a participant. The information that must be disclosed includes the manner in which it selects the pool of participants. In other words, if a pregnant woman calls a hospital's referral service, the referral service must disclose how it selects obstetricians to be qualified to receive referrals and whether the obstetrician has paid a fee to participate. The referral service must also disclose how the particular obstetrician is selected for the referral, for example, on a rotation basis. In addition, the referral service must disclose the relationship between the participant and the referral service, for example, that the obstetrician is on the active medical staff. Finally, the referral service must disclose what criteria it uses to exclude an individual or entity from continuing as a participant, for example, if a malpractice allegation is raised against the obstetrician or if he or she refuses to treat a certain level of uncompensated care cases.

The referral service must maintain a written record certifying that such disclosures have been made to each person seeking a referral. Such a record must be signed by either the person seeking the referral or by the individual making the disclosure on behalf of the referral service. This requirement will not be met if the referral service merely maintains a blank copy of the disclosure form or instructions to staff on how to make the disclosure.

Comment: One commenter suggested that a referral service should be permitted to require the practitioners or providers to charge clients that are referred by the service the same fees as they charge other clients.

Response: We agree and have revised paragraph (f)(3) to permit referral services to bar participants from engaging in discriminatory pricing practices.

Comment: A few commenters were uncertain about what fees could be charged for the referral service. They questioned whether the referral fee must be paid prior to the referral and whether a set amount could be charged for each referral.

Response: This provision protects fee payments that are related only to the cost of operating the referral service. This provision explicitly does not protect fees that in any manner are based on the volume or value of Medicare or Medicaid referrals or business otherwise generated by the participant for the referral service. While a referral fee need not be paid in full before any referrals are made, paragraph (f)(2) specifies that referral fees may not be based on the volume of referrals to the practitioner or provider.

Comment: One commenter asked whether the disclosure requirements of this provision could be satisfied by sending a letter to the referred person after the referral is made.

Response: Although the method of disclosure is not prescribed, to meet the requirements of this provision any disclosure must constitute effective disclosure. Effective disclosure requires that the relevant information is communicated in time for the information to be used by the beneficiary before an important decision is made. Accordingly, it is unlikely that disclosure after the referral has been made would constitute effective disclosure if the beneficiary had already seen the health care provider, or in some cases, if the appointment had already been made.

Comment: Several commenters questioned whether the statute and, therefore, this safe harbor provision, applies to referral services where health care providers are not charged for the services or where the services are provided pursuant to association dues.

Response: The statute applies to such referral services. The statute is implicated not only where direct payments are made in return for referrals, but also where indirect forms of remuneration are given for referrals. For example, hospitals often operate free referral services for members of their medical staffs as one of the benefits that comes with being on that hospital's staff. In return for the benefits of staff privileges (including the free referral service), physicians have a variety of obligations, such as sitting on various hospital committees. Depending on the circumstances, the services physicians furnish a hospital to assist in its operations may constitute a form of remuneration to the hospital for providing the referral service, and would be covered by the statute. As the United States Court of Appeals for the First Circuit found: "Giving a person an opportunity to earn money may well be an inducement to that person to channel potential Medicare payments towards a particular recipient." *United States* v. *Bay State Ambulance and Hospital Rental Service, Inc., supra,* 874 F.2d at 29. Therefore, staff physicians and hospitals seeking safe harbor protection must comply with this provision when they are engaged in a referral service that does not charge a specific fee.

5. Warranties—§ 1001.952(g)

Comment: Two commenters objected to the requirement that as a condition for protection the warranty include payments to compensate for any costs associated with the replacement of the product that is the subject of the warranty. These commenters pointed out that virtually no warranties now in existence pay for such expenses and that this requirement will necessitate the revision of warranty policies, which in turn must be paid for by price increases to cover this additional liability expense.

Response: We agree with the concern over the potential that this standard will increase costs, and are deleting it. We are revising this provision based on the Federal Trade Commission interpretation of 15 U.S.C. 2301(6), which does not require the manufacturer to make full payment to compensate for all costs associated with its defective product.

Comment: One pacemaker manufacturer noted that a particular warranty complied with the discount exception, implying that it need not comply with this warranty provision.

Response: We do not believe that warranty arrangements fit within the "discount" safe harbor provision, and are revising that provision accordingly. However, we agree that some of the policies underlying the discount exception should apply to warranties. Consequently, with respect to any reductions of equipment prices offered as part of a warranty agreement, we are requiring the same disclosure requirements as contained in the discount provision.

Comment: Two commenters urged the OIG to expand this safe harbor provision to protect "competitive replacement agreements." Under such an agreement, for example, a company offers various inducements to encourage hospitals (or other entities such as ASCs) and physicians to replace a defective pacemaker with one made by the company offering the inducements. These commenters argued that these arrangements should be protected because they make it easier to purchase the latest available technology. In addition, the comments pointed out that there is little potential for abuse because Peer Review organizations review virtually every pacemaker implant decision, and because competitive replacement programs put the beneficiary only in the same financial position he or she would be in if he or she purchased a replacement pacemaker from the original manufacturer pursuant to that manufacturer's warranty.

Response: We generally agree with these comments, but we remain concerned that many of these programs either provide additional incentives beyond the original warranty or impose additional costs on the Medicare and Medicaid programs. For example, while some competitive replacement programs replace the item, such as a pacemaker, only on the same terms as those in the warranty of the original manufacturer, others replace the item under other conditions as well; while some provide the replacement item free of charge, others provide a discount on the replacement item capped at a specified dollar amount; and while some make no payments for medical expenses, others assist patients (either directly or by paying the health care provider) with their unreimbursed medical expenses up to a specified dollar amount. Depending on the original manufacturer's warranty, some of these programs do much more than merely put the beneficiary in the same position he or she would be in if he or she bought a replacement item from the original manufacturer under the terms of that warranty.

We believe that safe harbor protection is proper where a replacement program honors the original manufacturer's warranty, which qualifies by itself under this provision, and the agreement provides remuneration on the same terms as the original manufacturer's warranty without providing additional incentives or shifting additional costs to the Medicare and Medicaid programs. Under such programs, any incentive to replace a product under warranty stems from the original warranty, and not from the competitive replacement agreement.

We remain concerned about potential abuse in one additional area. Some competitive replacement agreements pay the health care provider or practitioner directly for the beneficiary's medical expenses. We believe that such direct payments are potentially abusive because the health care provider or practitioner knows that the warranty insures against beneficiaries' bad debts. Thus, we are adding paragraph (g)(4) so that safe harbor protection is not provided when payments are made to any health care provider (such as a hospital or ASC) for expenses such as medical, surgical or hospital expenses incurred by the beneficiary. Payments made to the health care provider or practitioner for the item itself, or price reductions on that item, are protected.

Comment: One commenter suggested that the OIG should provide safe harbor protection for payments made by manufacturers or suppliers to settle claims or to satisfy judgments arising out of product liability claims regardless of whether such payments were included in the warranty at the time of the original sale of the item.

Response: Where such payments are not part of a warranty made at the time of the original sale of an item, they do not appear to be intended to induce the purchase of that item, and hence are not covered by the statute. Where such payments are included in a warranty given at the time of sale, they would only be protected if they were made as part of a warranty that complied with this provision.

Comment: One commenter suggested that the OIG should not provide safe harbor protection for middlemen suppliers that expand the protection afforded by the manufacturer' s warranty.

Response: We believe that warranties generally benefit consumers as well as the Medicare and Medicaid program, even though they may constitute a technical violation of the statute. As long as a supplier acting as a middleman wholesaler complies with this safe harbor provision, we fail to see the harm when it provides greater benefits than those provided by the manufacturer. Such expanded warranties are commonly provided by middlemen in industries other than health care, for example, by automobile dealers, and we believe such expanded warranties should be encouraged.

6. Discounts—§ 1001.952(h)

Comment: A few commenters expressed concern about the meaning of the word "discount." For example, four commenters asked us to clarify whether a discount includes a general price reduction offered across the board to all buyers. One commenter argued that a marketing strategy similar to a warranty, but not falling within that safe harbor provision was, in fact, a discount.

Response: We believe that this first statutory exception is intended to cover discounts and other price reductions offered by a seller through an arms length transaction to induce a buyer to order or purchase goods (including items) or services for which the discount applies or other goods or services payable under Medicare or Medicaid. A discount typically is the difference in the price at which a good or service is normally sold compared to the price at which it is actually sold when the inducement is given.

The statutory discount exception applies only to discounts obtained by health care providers who submit claims to the Medicare and Medicaid programs. We believe that this exception was not intended to cover the offering of discounts by health care providers who submit claims, for example, to beneficiaries as part of a routine waiver program for coinsurance and deductible amounts. We have changed the definition of the term "discount" to clarify the limited scope of this exception. A discussion of the limited safe harbor protection we are providing for routine waivers is found in section III.B.4. In addition, as discussed in section III.B.3., price reductions negotiated by HMOs, preferred provider organizations and other health care plans to protect such discounted fee arrangements are expected to be addressed at a later date in a separate interim final rule.

We believe discounts are distinct from across-the-board price reductions offered to all buyers where the inducement that is made is so diffuse that it does not appear intended to encourage a particular buyer to purchase or order a particular good or service payable under Medicare or Medicaid.

In addition, we believe that Congress did not intend for this discount exception to apply to price reductions offered to one payor but not to Medicare or Medicaid. For example, we are aware of cases where laboratories offer a discount to physicians who then bill the patient, but do not offer the same discount to the Medicare program. In some of these cases, the discount offered to the physician is explicitly conditioned on the physician's referral of all of his or her laboratory business. Such a "discount" does not benefit Medicare, and is therefore inconsistent with the statutory intent for discounts to be reported to the programs with costs and charges reduced appropriately to reflect the discounts.

Another problem exists when an entity, which is both a provider or supplier of items or services and a joint venture partner with referring physicians, makes discounts to the joint venture as a way to share its profits with the physician partners. Very often this entity furnishes items or services to the joint venture, and also acts as the joint venture's general partner or provides management services to the joint venture. For example, in some cases a reference laboratory performs testing for another laboratory at a discount price in accordance with a management contract. In other cases, the services the reference laboratory provides are paid on the basis of a percentage of revenues that the joint venture receives from Medicare. These arrangements are not arms length transactions where the joint venture entity shops around for the best price on a good or service. Rather, it has entered into a collusive arrangement with a particular provider or supplier of items or services that seeks to share its profits with referring physician partners. To clarify that we do not intend to protect these types of transactions which are sometimes made to appear as "discounts," we are clarifying the definition of "discounts" in paragraph (h)(3) of this section to permit only transactions made on an arms length basis.

Since many of these illegal transactions are made as part of personal services or management contracts, we are clarifying the definition of "discounts" to preclude discounts made as part of such transactions. We are making this revision for the additional reason that Congress did not intend to exempt such arrangements merely because those services were provided at a "discount." Since we believe that contracts for personal or management services do not fit within the ambit of the statutory discount exception, such arrangements must be analyzed under the respective safe harbor provision for those contracts. Of course, to the extent that the failure to report the actual price of the management contract implicates the civil monetary penalties law (section 1128A of the Act) liability may be imposed under that statute.

With respect to warranties, as we discussed in the warranty section immediately above, warranties are not discounts. Therefore to provide clearer guidance, we have modified the definition of the term "discount" in paragraph (h)(3) to exclude warranties and other examples of arrangements that do not constitute "discounts."

Comment: Many commenters urged the OIG to expand this safe harbor provision to include a variety of other discounting practices where the benefit received relates to something other than the specific good or service purchased or provided. Examples of the suggested permissible arrangements include bundled goods closely related to the purchased goods, such as free "surgical packs" (including such items as sutures, Healon, viscoelastics, and disposable gloves provided with purchases of intraocular lenses (IOLs), or credits toward free computers or other items that are useful in a physician's practice.

Response: We believe that such an interpretation goes well beyond the legislative intent of this statutory exception, and vitiates its purpose. We believe that Congress did not intend to include within this provision the practice of a seller giving away, or reducing the price of, one good in connection with the purchase of a different good. Such arrangements, for the most part, do not represent price reductions where the value of the goods received can be measured and fully reported to the Medicare and Medicaid programs.

Although there are many instances where these practices are cost effective arrangements that benefit the health care provider, there is enormous potential for abuse. One of the most common features of a serious kickback violation exists when a seller offers a valuable good, for example a car or a trip, to a person in return for that person's participation in activity prohibited under the statute, for example, referral of business payable by the Medicare and Medicaid programs. Thus, these commenters, while pointing to some potentially beneficial arrangements, are asking us to permit a broad class of arrangements that would include acts which have resulted in criminal convictions and at least one pending criminal prosecution. See *e.g., United States* v. *Bay State Ambulance and Hospital Rental Service, Inc., supra.*

Even where the particular item that is being given away may result in a more effective means of delivering the supplies to the health care provider, these types of "discounts" cause problems because they often shift costs among reimbursement systems or distort the true costs of all the items. As a result, it may be difficult for the Medicare and Medicaid programs to determine the proper reimbursement levels.

For example, in developing accurate pricing data to assist HCFA in setting the amount of reimbursement for IOLs, we found that bundled pricing arrangements similar to those suggested by our commenters were common, and made it difficult to determine the true acquisition cost of IOLs. (See Medicare certified Ambulatory Surgical Centers, Cataract Surgery Costs and Related Issues, at 9–12, March 1988, OAI–09–88–00490.) In addition, HCFA determined that its IOL pricing data obtained from the ASCs "revealed significant inconsistencies in reporting net IOL costs." 53 FR 31476. The necessity of accurately reporting the true acquisition costs of IOLs undistorted by bundling arrangements is underscored by HCFA's stated policy in its final rule promulgating a $200 add-on rate: "to continue to collect data on IOL acquisition costs and purchasing arrangements to ensure that the IOL rate appropriately reflects lens acquisition costs." 55 FR 436.

Finally, this practice of bundling IOLs with other goods is of sufficient seriousness that it is the subject of at least one pending criminal prosecution.

For these reasons, we decline to broaden the scope of this provision to include discounts on bundled goods and have clarified the definition of the term "discount" to specifically exclude such arrangements. Of course, where discounts are offered on goods that are unbundled and the discount otherwise complies with the rules of this provision, safe harbor protection is granted.

For purchasing practices involving the free provision of another type of item, we will examine the surrounding circumstances to determine the desirability of prosecuting that arrangement. Examples of potential factors which we may consider include: (1) The amount of the benefit that was reported and passed along to the programs, (2) whether the good is separately reimbursable, and (3) the intent behind the arrangement.

A related issue is the practice of giving away free computers. In some cases the computer can only be used as part of a particular service that is being provided, for example, printing out the results of laboratory tests. In this situation, it appears that the computer has no independent value apart from the service that is being provided and that the purpose of the free computer is not to induce an act prohibited by the statute. Rather, the computer is part of a package of services provided at a price that can be accurately reported to the programs. In contrast, sometimes the computer that is given away is a regular personal computer, which the physician is free to use for a variety of purposes in addition to receiving test results. In that situation the computer has a definite value to the physician, and, depending on the circumstances, may well constitute an illegal inducement.

Comment: A large number of commenters urged the OIG to broaden this safe harbor provision to include other reductions in price, such as "rebates" and "credits." These commenters argued that such programs are equivalent to price reductions and are capable of being properly reported.

Response: We generally agree with the thrust of these comments and have revised the definition of discount in paragraph (h)(3) to protect rebate checks, redeemable coupons and credits, subject to the following conditions. First, because of our continued concern about the potential for improper use of redeemable coupons, we are limiting the ability of recipients of such discounts to negotiate these instruments to third parties. As revised, this provision requires these instruments to be redeemed only by the seller. Second, the rebate check, redeemable coupon, or credit can only be applied to the same good or service that was purchased or provided. Thus, a redeemable coupon or credit obtained on the purchase of one good cannot be used toward the purchase of a different good. Third, like other discounts covered under this provision, these forms of discounts must be fully and accurately reported. Finally, except as noted below, such discounts must be given at the time the good or service was purchased or provided.

The reporting of credits presents an unusual situation because the monetary value of the credit only applies to future purchases of goods or services. Thus, to comply with this provision, the buyer must report the credits on the applicable cost report or claim form covering the goods or services for which the credit is being used.

Comment: A large number of commenters urged the OIG to expand this safe harbor provision to include other types of discount mechanisms where the value of the discount is not calculated until after some period of time has passed. Examples of such a discount mechanism include end-of-year discounts and prompt pay discounts. These commenters believed that these discounting mechanisms encourage legitimate, beneficial business practices that do not harm the program. In addition, many commenters pointed out that such discounting practices have long been encouraged through HCFA's prudent buyer guidelines. (Provider Reimbursement Manual, part I section 2103, HCFA Pub. No. 15–1)

Response: We recognize that there are many legitimate discount programs where the value of the discount is only reported after the good is purchased or the service is provided. Unfortunately, due to the nature of some reimbursement systems, it is sometimes not possible to determine retrospectively how much such discounts reduce the price of the goods or services previously purchased or provided. For example, it would be virtually impossible to take the numerous claims for cataract surgery submitted by a physician in a given year and determine the true acquisition cost of an IOL provided to that physician when the discount is only calculated at year end. Thus, paragraph (h)(1)(iii) of this section, which governs discounts on items and services paid on the basis of charges or acquisition costs, does not permit end-of-year discounts. On the other hand, where the Department or a State agency requires a health care provider to maintain cost reports (including HMOs, CMPs and health care prepayment plans (HCPPs pursuant to agreements under sections 1876(h) or 1833 of the Act), we believe that end of year calculations of discounts on purchases of the same good or service can be fully and accurately reported, as well as those discounts obtained at the time of the purchase.

Therefore, we are revising this provision in paragraph (h)(1)(i) of this section (which applies only to cost report providers) to protect such end-of-year discounts when all of the following conditions are met. One, end-of-year discounts can only be calculated based on purchases of the same good or service in a single fiscal year. Of course, the discount may be obtained at the time of purchase as well. Two, the entity must claim the benefit of the discount from the seller in the fiscal year in which the discount is earned or the following year. In many cases, a seller will be able to calculate the amount of the discount and give the buyer the benefit of the discount (for example, in a credit or reduced price on future purchases of that same good) in the same fiscal year in which the credit was earned. However, in many other cases, the seller may take several weeks after the end of a fiscal year to give the buyer the necessary information. Under either circumstance, this prong of the safe harbor is satisfied. Three, the buyer must fully and accurately report the discount in the cost report for the fiscal year in which the benefit of the discount is received. And four, if the Secretary or a State Medicaid agency requests information, the buyer must provide the appropriate invoices from the seller. (See discussion below of seller's separate reporting requirements.)

We believe that this revision complies with the most important statutory requirement of the discount exception—full reporting—and accommodates many of these end-of-year discounting programs. In addition, we believe that this revision is consistent with HCFA's prudent buyer rules, which are not applicable to charge-based health care providers.

With respect to prompt pay discounts, we have made no change to include such discount arrangements. No change is necessary because, by definition, they are designed to induce prompt payment, and thus do not appear to violate the statute. Of course, we will continue to scrutinize closely "prompt pay" discounts to make sure that they are not payments made for an illegal purpose cloaked under a legitimate label.

Comment: Three commenters requested the OIG to provide various kinds of special treatment for HMOs and PPOs. For example, one commenter urged the OIG to broaden this provision as it applies to HMOs to permit cash grants and training assistance. Another commenter urged the OIG to change the definition of discount to permit discounts offered to HMOs and PPOs by contract health care providers.

Response: We recognize that HMOs and CMPs paid in accordance with a risk contract with HCFA or a State health care program deserve special attention, and paragraph (h)(1)(ii) follows the proposed rule recognizing their special status. These HMOs and CMPs need not report discounts they receive except as may otherwise be required under their risk contract.

In addition, we have expanded this provision in significant ways that should be of assistance to all health care providers, including HMOs. However, we do not believe that it would be appropriate to provide special safe harbor protection for purchasing arrangements that go beyond the intended purpose of this statutory exception. As with all arrangements that drift from a safe harbor out to sea, we will examine them on a case-by-case basis to determine whether the statute has been violated in such a way as to warrant prosecution.

With respect to discounts offered to HMOs, CMPs and PPOs by contract health care providers, as discussed in section III.B.3. above, we are expecting to promulgate a new interim final safe harbor provision to protect arrangements between these parties for the furnishing of covered items and services to beneficiaries where certain standards are met.

Comment: Many commenters objected on a variety of grounds to the requirement that charge-based health care providers reduce their charges by the full amount of the discount. These commenters pointed out that historically the Medicare program has not sought to regulate the discrete components that make up a particular charge. In addition, many suggested that the OIG will destroy the incentive of obtaining discounts if it requires health care providers to pass along the full amount of the discount to the programs. Another rationale for suggesting a change in this safe harbor provision is that the OIG should treat cost and charge-based health care providers in the same manner, and because this safe harbor provision does not require a reduction in reported costs for cost-based health care providers, no parallel requirement should be placed on charge-based health care providers.

Response: We agree with the thrust of these comments, and are revising paragraph (h)(1)(iii) of this safe harbor provision to delete the requirement that charge-based health care providers reduce their charges by the full amount of the discount. Such a provision would be largely unenforceable. As many commenters pointed out, the Department has never monitored the various input costs that make up a health care provider's charge. Therefore, we are not in a position to know a health care provider's base from which he or she was reducing the charge. Thus, for example, if a physician receives a discount as defined in this provision valued at $4 per service, the physician could argue that he or she is not required to reduce the charge by that amount because other costs included in that charge had increased to offset the $4 discount. We are generally not in a position to prove otherwise.

Although we continue to believe that individuals and entities have an obligation to pass along to the Medicare and Medicaid programs the value of discounts they receive, we believe that the actual savings that would result from requiring such charge reductions would be offset by the cost of enforcement. In many areas of reimbursement, for example, physician or laboratory services and purchases of IOLs, Congress has steadily moved away from charge-based reimbursement or has imposed limitations on charges. We believe that those statutory reforms are better suited to address the problem of excessive charging practices. Nonetheless, even though we are deleting this requirement for the purposes of this safe harbor provision, we strongly encourage charge-based health care providers to pass along discounts to the programs.

With respect to the different treatment of health care providers based on the type of reimbursement system, we believe that reasonable safe harbor rules for discounts must be closely tailored to the various reimbursement principles and cost reporting mechanisms. Just as we believe it is appropriate to treat HMOs reimbursed on a capitated basis differently from other health care providers, we now believe that it is appropriate to treat charge-based health care providers differently from cost-based health care providers for the purposes of requiring the discount to be passed along to the program. Such an approach is far preferable than a blind adherence to uniform treatment of health care providers. We believe that such a position is a reasonable reading of the statutory requirement that "the reduction in price [be] * * * appropriately reflected in the costs claimed or charges made by the provider or entity * * *." (Section 1128B(b)(3)(A) of the Act.)

We emphasize, however, that paragraph (h)(1)(iii) still requires charge-based health care providers to comply with the respective rules regarding full and accurate reporting of discounts as defined in this provision. This reporting requirement is limited to items or services that are separately claimed as a line item for payment with the Department or a State agency. As discussed below, under paragraph (h)(1)(iii) of this section, we will not require health care providers to report discounts they receive on goods purchased for which a line item charge is not separately made, but rather is included within their professional charge.

In addition, we note that some commenters were confused about the requirements we are placing on health care providers reimbursed on the basis of costs. The regulation need not specify that a health care provider must separately reduce its cost by the amount of the discount because the cost reporting requirements accomplish the statutory purpose of having the amount of the discount "appropriately reflected in the costs claimed." Whether a provider submits cost reports (and complies with paragraph (h)(1)(i) of this section) or submits a seller's invoice to demonstrate its acquisition costs (and complies with paragraph (h)(1)(iii) of this section), the amount of the discount is passed along to the Medicare and Medicaid programs. As a result, this revised discount provision treats items and services reimbursed on the basis of charges differently from those reimbursed on the basis of costs, because costs will be reduced by the amounts of discounts whereas charges will not be affected.

Finally, although we have attempted to tailor this discount provision to make sense within the context of the varying reimbursement rules, as we have explained in section III.A. above, compliance with this safe harbor provision in no way affects Medicare or Medicaid reimbursement rules.

Comment: Five commenters discussed the requirement in the proposed rule that the discount appear on the seller's invoice or statement and the consequent liability of the seller for failing to make such disclosure. They questioned the apparent inconsistency with the preamble to the proposed rule that no requirements need be placed on sellers in order for their discounts to qualify under this exemption.

Response: We agree with the comments that we should clarify the requirement for a seller to report the value of the discount on the invoice or statement provided to a purchaser, and we are modifying this provision in paragraph (h)(2) accordingly. As discussed above, such standards are necessary to assist the Department and State agencies in verifying that the buyer has fully and accurately reported the value of the discount.

This paragraph describes the requirements we are placing on sellers. With respect to those who sell goods or services to risk contract HMOs and CMPs at a discount, paragraph (h)(2)(i) makes clear that the seller is under no obligation to report the discount to the HMO or CMP for purposes of this safe harbor. Paragraph (h)(2)(ii) sets out the seller's requirements with respect to its sales to all other health care providers. It must either fully and accurately report the discount on the invoice or statement. In addition, it must inform the buyer of its obligations under paragraph (h)(1). With respect to permissible end-of-year discounts, this paragraph, as revised, requires the seller's invoice or statement to show clearly the existence of a discount program, and the seller must inform the buyer of its obligations under paragraph (h)(1). The seller is also required to provide the buyer with a separate document, such as a reconciliation statement, showing the calculation of the discount and identifying the specific goods or services purchased to which the discount is attributed.

It was our original intent not to hold sellers liable for the reporting omissions of health care providers, and we believe such a policy remains appropriate. However, we agree with the commenters that some rules should apply to sellers. We believe that the limited conditions we are placing on sellers seeking safe harbor protection will not place an undue burden on them, but are sufficient to prevent them from avoiding liability when they engage in unlawful schemes disguised as discounts.

Comment: Many commenters questioned what information must be reported to the program and the methods to be used in reporting such information. Among the questions that were asked is whether the list price, discount, and final actual price all need to be reported on the invoice, claim, or statement. In addition, many commenters suggested that it was unrealistic to require practitioners to report all discounts on goods they purchase, such as office supplies and surgical gloves, for which they do not charge separately, but rather include within their professional service charge.

Response: The fundamental test for complying with the reporting requirement is whether the actual purchase price net of any discount is fully and accurately reported by the seller on the invoice or statement (or, where applicable for end-of-year discounts, on a reconciliation statement) and by the purchaser on the claim or request for payment submitted to Medicare and Medicaid. We do not necessarily require all the information in the calculation of the discount to be noted specifically on the invoice, statement, claim or request for payment; rather, a notation may be made that the actual purchase price is "net discount." Such reporting is acceptable for the purpose of satisfying this provision.

We agree that no purpose would be accomplished if we were to require practitioners to report the discounts they receive on office supplies where there is no requirement to separately report the item on which the discount is received. Thus, we are clarifying the requirements for reporting discounts under paragraph (h)(1)(iii) of this section to make clear that where a practitioner obtains a discount, defined in this provision, for a good that is included as part of his or her professional service charge, such discounts need not be reported. Where a practitioner, however, purchases an item or service at a discount and such item or service is separately claimed as a line item on the applicable claim form, the discounted price must be fully and accurately reported. For example, where a surgeon performs cataract surgery in his or her office and implants an intraocular lens (IOL), the surgeon must report any discount received on the price of the IOL.

Finally, it is noted that where the discount in question does not qualify as a discount under this provision, no safe harbor protection applies. For example, as we stated above, we are not expanding this safe harbor provision to protect the offering of a free good different from the one that is being purchased. Thus, consistent with that position, we are not willing to protect the offering of free computers even when named as "office supplies" to induce the purchase of other items that are reimbursable separately.

7. Employees—§ 1001.952(i)

Comment: Many commenters urged the OIG to extend this exception to apply to independent contractors paid on a commission basis. Two commenters asserted that the legislative history of the statute makes clear that Congress intended to include independent contractors in the employee exception. In support of this contention, they quoted remarks made by Representative Rostenkowski when the House was considering the Medicare-Medicaid Anti-Fraud and Abuse Amendments of 1977. (123 Cong. Rec. 30,280 (1977))

Response: We continue to reject this approach because of the existence of widespread abusive practices by salespersons who are independent contractors and, therefore, who are not under appropriate supervision and control. Although two commenters asserted that they could achieve appropriate supervision and control of independent contractors by including restrictive terms in the contract, we cannot expand this provision to cover such relationships unless we can predict with reasonable certainty that they will not be abusive. We are confident that the employer-employee relationship is unlikely to be abusive, in part because the employer is generally fully liable for the actions of its employees and is therefore more motivated to supervise and control them.

Furthermore, we believe that Representative Rostenkowski's remarks do not reflect congressional intent in this case. His comments related to the House version of the employee exception that was rejected by the Conference Committee. Instead, Congress passed the Senate version, which expressly limited the exception to bona fide employment relationships (See H.Conf.Rep. No. 673, 95th Cong., 1st Sess. 41 (1977)). Consequently, we find no support for the position that Congress intended to cover independent contractors under this exception.

Comment: Two commenters questioned the wisdom of the employee exception, stating that health care providers should not be able to refer patients to other health care providers within their own offices because abuse could be worse than when individuals or entities make referrals to outside sources.

Response: The exception for bona fide employment relationships is clear on the face of the statute, and we are not free to ignore that statutory mandate.

Comment: One commenter asserted that we do not have the statutory authority to limit the definition of "employee" to the meaning it has under 26 U.S.C. 3121(d)(2).

Response: As we have discussed, Congress expressly limited the scope of the employee exception to "bona fide employment relationship[s]" between an employer and an employee. The Secretary clearly has the power, and indeed the duty, to establish the criteria for a bona fide employment relationship. The Internal Revenue Service's (IRS) definition of employee is a longstanding one that has been developed by both agency and court rulings. Furthermore, this definition is sufficiently narrow that it excludes certain types of relationships that we believe tend to be associated with violations of the statute. We are clarifying this safe harbor provision to make clear that the meaning of the term "employee" is defined not only by 26 U.S.C. 3121(d)(2) itself, but also by the IRS's interpretation of that provision as codified in its regulations and other interpretive sources.

Comment: One commenter inquired whether a part-time employee paid on a commission-only basis falls within the employee exception.

Response: As long as a bona fide employer-employee relationship exists between the part-time employee and the employer, such a relationship falls within the scope of this provision.

Comment: Some commenters asserted that many legitimate employment relationships that are common in the health care industry are not protected from prosecution under this exception. One commenter suggested that the employee exception include independent contractors where beneficiaries are being induced to participate in cost-containment programs because such programs are beneficial to Medicare and State health care programs, and therefore should be protected.

Response: We recognize that this provision does not cover some types of personal service arrangements, but our position is necessary to protect the program from abuse to a reasonable degree. However, many of these other arrangements could be protected under the personal services and management contracts safe harbor provision.

Comment: One commenter stated that hospitals are often compelled by State "corporate practice of medicine" requirements to employ physicians and other health care personnel as independent contractors, and that these employment relationships should be afforded safe harbor protection.

Response: We understand that there may be circumstances where, because of State laws, health care providers may not be able to enter into arrangements with health care personnel that comply with the IRS definition of employee. In such cases, however, health care providers may obtain protection for payments from these arrangements by drafting their personal contracts to satisfy the safe harbor provision for personal services and management contracts.

8. Group Purchasing Organizations—§ 1001.952(j)

Comment: One commenter urged the OIG to further define what constitutes a group purchasing organization (GPO) for purposes of this provision. This commenter specifically questioned whether a nursing home chain that requested percentage payments from laboratories as "GPO fees" in return for the referral of laboratory services from member nursing homes fit this definition.

Response: As stated in the preamble to the proposed rule, this exception applies to payments made by a vendor of goods or services to a person authorized to act on behalf of a group of individuals or entities who are furnishing Medicare or Medicaid services. Our definition of the term "GPO" makes clear that a nursing home chain requesting fees for referrals would not qualify for this safe harbor because a chain of nursing homes that are wholly owned subsidiaries of a single corporate entity for all practical purposes constitutes a single entity and not a "group" of entities. As we discuss in section III.D. below, because of the special relationship wholly-owned subsidiaries have with their parent corporation, we are considering separate protection for payments between these entities. However, following this reasoning, we do not believe it appropriate for a nursing home chain to qualify as a GPO and request "GPO fees" for referrals. If a nursing home directly requested such a fee it would appear to represent an illegal inducement. We see no reason how such a solicitation sanitizes the illegality when it is made indirectly by a wholly-owned subsidiary of the nursing home, instead of directly by the nursing home itself.

In addition, we believe that Congress did not intend this exception to apply where it is the vendor and not the health care provider who is furnishing services and directly billing the Medicare or Medicaid program. For example, in addition to services furnished by the nursing home, other health care providers furnish many part B services to nursing home patients, such as laboratory services and durable medical equipment (DME). We believe that a GPO, acting on behalf of a group of nursing homes, is not serving as a GPO when it receives a "GPO fee" from a laboratory or DME supplier that is supplying goods or services to nursing home patients and billing Medicare or Medicaid directly.

Comment: Several commenters objected to the requirement that a purchasing agent, i.e., a GPO, have a written agreement with each individual or entity in the group that specifies the amount the agent will be paid by each vendor. This requirement, they asserted, would be burdensome and expensive.

Response: We agree with the general thrust of these comments and have modified paragraph (j)(1)(ii). The statutory exception requires that written contracts specify the amount the GPO will be paid by the vendor. We believe that this statutory mandate is satisfied if the GPO discloses to a health care provider the fees it will receive from only those vendors that provide goods or services to that provider. This obviates the need for the GPO to divulge fees from vendors that do not provide goods or services to that particular individual or entity.

Comment: To promote administrative convenience, efficiency, and cost-containment purposes, several commenters requested that the GPO should be permitted to specify the range of fees to be paid by the potential vendors instead of the actual amount. One commenter asserted that because of the varying contracts between GPOs and their vendors, it was impossible to determine and disclose in advance the amount the GPO would receive from its vendors.

Response: We agree that it is not necessary, in all circumstances, to specify the exact fees the GPO will receive from its vendors as a result of a particular member's purchases. The legislative history to this exception, however, shows Congress's concern for excessive GPO fees, particularly those exceeding 3 percent. (See, H.Conf. Rep. 1012, 99th Cong., 2d Sess. 310–11 (1986)) For this reason, we are revising this provision (see paragraph (j)(1)(i)) so that a GPO needs to specify the administrative fee it is paid from vendors only if any fee will be above 3 percent.

In the event that the fee cannot be ascertained at the time of the contract or the fee is not fixed at 3 percent or less, the contract must state the maximum amount that could be paid to the GPO by the vendor. This mechanism will permit some flexibility in payments made to the GPO, yet retain the focus on excessive fees about which Congress was concerned.

Comment: Several commenters questioned the interrelationship of this provision to the discount safe harbor.

Response: Several commenters appeared confused about the relationship between these two provisions. This is an example of an arrangement where two safe harbor provisions could apply, i.e., one applicable to discounts, and one applicable to GPOs. However, the GPO provision applies only to payments made by a vendor of goods or services to a person authorized to act as a GPO. Payments, such as discounts, made by vendors of goods or services to health care providers must qualify under the discount exception.

D. Comments on Proposals for New Safe Harbor Provisions

In sections III.B.3. and III.C.1. we discussed proposals and our responses regarding new safe harbor provisions for negotiated price reductions and investment interests. In this section we discuss the remaining proposals and our responses regarding potential new safe harbors.

Note: Any discussion below indicating that we are considering a new safe harbor provision should in no way be construed as legalizing the business arrangement at this time.

Comment: A large number of commenters urged the OIG to adopt a safe harbor provision to protect certain physician recruitment activities. They commented that subsidy payments to physicians for recruitment purposes provide important benefits to many communities that have difficulty in obtaining and retaining physicians. Some urged that we also protect hospital recruitment activities even though a physician does not need to move his or her residence to join the medical staff of the new hospital. Others urged a variety of other provisions, for example, that we not require the physician to disclose to his or her patients the relationship between the physician and the hospital, and that we not specify how long the payments may continue.

Response: We agree with the need to protect some recruitment activities for physicians and other practitioners, and we are considering a new safe harbor provision for practitioner recruitment that we anticipate publishing as a separate regulation.

Comment: Three commenters requested the OIG to adopt a safe harbor provision that will protect all payments that subsidize malpractice premiums. These commenters stressed that such payments have an overwhelming public benefit with limited potential for abuse. One of these commenters argued that obstetrician-gynecologists are facing significant difficulty in paying for malpractice insurance, and suggested that many communities are facing a cut-off of obstetrical services as a result.

Response: We understand the need to assist certain physicians in making malpractice insurance more affordable, and we are considering a new safe harbor provision which we anticipate publishing as a separate regulation, that would protect certain arrangements that subsidize the costs of a practitioner's malpractice insurance premiums where there is no likelihood of abuse.

Comment: Several commenters asked the OIG to provide a new safe harbor provision to protect different types of cross-referral arrangements where no money is exchanged between the parties, for example, traditional referral patterns between a primary care practitioner and specialist, between a hospital and nursing home, and among practitioners within a group practice.

Response: We agree that a large majority of these relationships benefit patients by assuring either proper continuity of care or convenient access to a specialist in whom the primary care physician has confidence. Thus, we are considering a new safe harbor provision, that we anticipate publishing as a separate regulation, that would protect many such arrangements where there is no likelihood of abuse.

Comment: Two commenters suggested that the regulation protect payments related to cooperative hospital service organizations qualified under section 501(e) of the Internal Revenue Code of 1986. Under this statute and implementing Internal Revenue Service regulation, these organizations are formed by one or more hospitals (known as "patron-hospitals") to provide specifically enumerated services, such as purchasing, billing, and clinical services solely for the benefit of its patron-hospitals. In addition, these entities are required to distribute "all net earnings to patrons on the basis of services performed." (26 U.S.C. 501(e)(2)) The commenters believed that although such a distribution requirement runs afoul of the anti-kickback statute, the services they perform are beneficial to rural communities in particular, and there has been no indication of abuse by these organizations.

Response: We agree and are considering a new safe harbor provision, that we anticipate publishing as a separate regulation, that would protect payments between cooperative hospital service organizations and patron-hospitals.

Comment: Many commenters requested the OIG to clarify that payments between corporations which have common ownership are not subject to the statute. Commenters cited as examples intracorporate discounts and payments between two wholly-owned subsidiaries. Some commenters argued that referral arrangements between two related corporations do not constitute "referrals" within the meaning of the statute, and suggested that the OIG define the word "referral" to exclude such activity.

Response: We agree that much of the activity described in these comments is either not covered by the statute or deserves safe harbor protection. We believe that the statute is not implicated when payments are transferred within a single entity, for example, from one division to another. Thus, no explicit safe harbor protection is needed for such payments.

Because the statute is implicated when payments are made from one entity to another even though the payments are made between entities with common ownership, we believe that safe harbor protection may be appropriate. However, we remain concerned about wholly-owned shell entities that are established for a fraudulent purpose, for example, to help hide the identity of the owners or to shield assets. Nonetheless, we are considering a new safe harbor provision, that we anticipate publishing as a separate regulation, that would protect payments between wholly owned subsidiaries and other payments between entities where exclusive ownership control is present and the practice is not otherwise abusive.

We do not, however, believe that the situations commenters described require us to define the word "referral." The commenters do not appear concerned with any unusual conduct that warrants special attention. Rather the commenters have focused on the source and recipient of the payment in question. Thus, our consideration in any proposed rule will be focused on the relationship of the parties making and receiving payments.

IV. Additional Information

A. Regulatory Impact Statement

Executive Order 12291 requires us to prepare and publish a final regulatory impact analysis for any regulation that meets one of the Executive Order criteria for a "major rule," that is, that which would be likely to result in (1) an annual effect on the economy of $100 million or more; (2) a major increase in costs or prices for consumers, individuals, industries, Federal, State, or local government agencies or geographic regions; or, (3) significant adverse effects on competition, employment, investment, productivity, innovation, or on the ability of United States-based enterprises to compete with foreign-based enterprises in domestic or export markets. In addition, we generally prepare a regulatory flexibility analysis that is consistent with the Regulatory Flexibility Act (5 U.S.C. 601–612), unless the Secretary certifies that a final regulation would not have a significant economic impact on a substantial number of small entities.

In the proposed rule published on January 23, 1989, we indicated that this provision was designed to specify the various business and payment practices that would not be considered a kickback for purposes of criminal or civil remedies, and served to clarify departmental policy as to the legality of various commercial arrangements. We stated that the great majority of health care providers and practitioners do not engage in illegal remuneration schemes, and that the aggregate economic impact of this provision should, in effect, be minimal, affecting only those who have chosen to engage in prohibited payment schemes in violation of the statutory intent. As indicated in the proposed regulation's impact statement, the rulemaking is a result of a statutory requirement and not a Department initiative.

The two comments we received on the cost impact indicated that the safe harbors for discounts and personnel services contracts would cast a cloud over a substantial number of legitimate business practices and existing contractual arrangements. Both commenters believed that a comprehensive regulatory flexibility analysis should be performed and a statement added disclosing the possible financial impact of this rulemaking.

Consistent with the intent of the statute, this regulation has been designed to permit individuals and entities to freely engage in business practices and arrangements that encourage competition, innovation and economy. However, the regulation imposes no requirements on anyone. Health care providers and others may voluntarily seek to comply with these provisions so that they have the assurance that their business practices are not subject to any enforcement action under the anti-kickback statute. Thus, it is impossible to predict how many individuals and entities will be affected by this regulation. For these reasons, we have determined that a regulatory impact analysis is not required. Further we have determined, and the Secretary certifies, that this final rule will not have a significant economic impact on a number of small business entities, and we have, therefore, not prepared a regulatory flexibility analysis.

B. Department of Justice Review

In accordance with the provisions of Public Law 100–93, this regulation has been developed in consultation with the Department of Justice.

List of Subjects in 42 CFR Part 1001

Administrative practice and procedure, Fraud, Health facilities, Health professions, Medicare.

TITLE 42—PUBLIC HEALTH

CHAPTER V—OFFICE OF INSPECTOR GENERAL—HEALTH CARE, DEPARTMENT OF HEALTH AND HUMAN SERVICES

42 CFR part 1001 is amended as set forth below:

1. The heading for part 1001 is revised to read as follows:

PART 1001—PROGRAM INTEGRITY—MEDICARE AND STATE HEALTH CARE PROGRAMS

2. The authority citation for part 1001 is revised to read as follows:

Authority: 42 U.S.C. 1302, 1320a–7, 1320a–7b, 1395u(j), 1395u(k), 1395y(e), and 1395hh, and section 14 of Public Law 100–93, unless otherwise noted.

3. Section 1001.1 is revised to read as follows:

§ 1001.1 Scope and purpose.

(a) This part sets forth provisions for the detection of fraud and abuse in the Medicare and certain State health care programs. It implements statutory sections, specifically identified in each subpart, aimed at protecting the integrity of the Medicare and certain State health care programs.

(b) This part also sets forth provisions addressing the OIG's authority to exclude any individual and entity that it determines has committed an act described in section 1128B of the Social Security Act, subject to the exceptions set forth in this part.

4. A new Subpart E is added to read as follows:

Subpart E—Permissive Exclusions

Subpart E—Permissive Exclusions

§ 1001.951 Fraud, kickbacks and other prohibited activities.

The OIG may exclude any individual or entity that it determines has committed an act described in section 1128B of the Social Security Act, subject to the exceptions set forth in § 1001.952.

§ 1001.952 Exceptions.

The following payment practices shall not be treated as a criminal offense under section 1128B of the Act and shall not serve as the basis for an exclusion:

(a) *Investment Interests.* As used in section 1128B of the Act, "remuneration" does not include any payment that is a return on an investment interest, such as a dividend or interest income, made to an investor as long as all of the applicable standards are met within one of the following two categories of entities:

(1) If, within the previous fiscal year or previous 12 month period, the entity possesses more than $50,000,000 in undepreciated net tangible assets (based on the net acquisition cost of purchasing such assets from an unrelated entity) related to the furnishing of items and services, all of the following five applicable standards must be met—

(i) With respect to an investment interest that is an equity security, the equity security must be registered with the Securities and Exchange Commission under 15 U.S.C. 78*l*(b) or (g).

(ii) The investment interest of an investor in a position to make or influence referrals to, furnish items or services to, or otherwise generate business for the entity must be obtained on terms equally available to the public through trading on a registered national securities exchange, such as the New York Stock Exchange or the American Stock Exchange, or on the National Association of Securities Dealers Automated Quotation System.

(iii) The entity or any investor must not market or furnish the entity's items or services (or those of another entity as part of a cross referral agreement) to passive investors differently than to non-investors.

(iv) The entity must not loan funds to or guarantee a loan for an investor who is in a position to make or influence referrals to, furnish items or services to, or otherwise generate business for the entity if the investor uses any part of such loan to obtain the investment interest.

(v) The amount of payment to an investor in return for the investment interest must be directly proportional to the amount of the capital investment of that investor.

(2) If the entity possesses investment interests that are held by either active or passive investors, all of the following eight applicable standards must be met—

(i) No more than 40 percent of the value of the investment interests of each class of investments may be held in the previous fiscal year or previous 12 month period by investors who are in a position to make or influence referrals to, furnish items or services to, or otherwise generate business for the entity.

(ii) The terms on which an investment interest is offered to a passive investor, if any, who is in a position to make or influence referrals to, furnish items or services to, or otherwise generate business for the entity must be no different from the terms offered to other passive investors.

(iii) The terms on which an investment interest is offered to an investor who is in a position to make or influence referrals to, furnish items or services to, or otherwise generate business for the entity must not be related to the previous or expected volume of referrals, items or services furnished, or the amount of business otherwise generated from that investor to the entity.

(iv) There is no requirement that a passive investor, if any, make referrals to, be in a position to make or influence referrals to, furnish items or services to, or otherwise generate business for the entity as a condition for remaining as an investor.

(v) The entity or any investor must not market or furnish the entity's items or services (or those of another entity as part of a cross referral agreement) to passive investors differently than to non-investors.

(vi) No more than 40 percent of the gross revenue of the entity in the previous fiscal year or previous 12 month period may come from referrals, items or services furnished, or business otherwise generated from investors.

(vii) The entity must not loan funds to or guarantee a loan for an investor who is in a position to make or influence referrals to, furnish items or services to, or otherwise generate business for the entity if the investor uses any part of such loan to obtain the investment interest.

(viii) The amount of payment to an investor in return for the investment interest must be directly proportional to the amount of the capital investment (including the fair market value of any pre-operational services rendered) of that investor.

For purposes of paragraph (a) of this section, the following terms apply. *Active investor* means an investor either who is responsible for the day-to-day management of the entity and is a bona fide general partner in a partnership under the Uniform Partnership Act or who agrees in writing to undertake liability for the actions of the entity's agents acting within the scope of their agency. *Investment interest* means a security issued by an entity, and may include the following classes of investments: Shares in a corporation, interests or units of a partnership, bonds, debentures, notes, or other debt instruments. *Investor* means an individual or entity either who directly holds an investment interest in an entity, or who holds such investment interest indirectly by, including but not limited to, such means as having a family member hold such investment interest or holding a legal or beneficial interest in another entity (such as a trust or holding company) that holds such investment interest. *Passive investor* means an investor who is not an active investor, such as a limited partner in a partnership under the Uniform Partnership Act, a shareholder in a corporation, or a holder of a debt security.

(b) *Space Rental.* As used in section 1128B of the Act, "remuneration" does not include any payment made by a lessee to a lessor for the use of premises, as long as all of the following five standards are met—

(1) The lease agreement is set out in writing and signed by the parties.

(2) The lease specifies the premises covered by the lease.

(3) If the lease is intended to provide the lessee with access to the premises for periodic intervals of time, rather than on a full-time basis for the term of the lease, the lease specifies exactly the schedule of such intervals, their precise length, and the exact rent for such intervals.

(4) The term of the lease is for not less than one year.

(5) The aggregate rental charge is set in advance, is consistent with fair market value in arms-length transactions and is not determined in a manner that takes into account the volume or value of any referrals or business otherwise generated between the parties for which payment may be made in whole or in part under Medicare or a State health care program.

For purposes of paragraph (b) of this section, the term *fair market value* means the value of the rental property for general commercial purposes, but shall not be adjusted to reflect the additional value that one party (either the prospective lessee or lessor) would attribute to the property as a result of its proximity or convenience to sources of referrals or business otherwise generated for which payment may be made in whole or in part under Medicare or a State health care program.

(c) *Equipment rental.* As used in section 1128B of the Act, "remuneration" does not include any payment made by a lessee of equipment to the lessor of the equipment for the use of the equipment, as long as all of the following five standards are met—

(1) The lease agreement is set out in writing and signed by the parties.

(2) The lease specifies the equipment covered by the lease.

(3) If the lease is intended to provide the lessee with use of the equipment for periodic intervals of time, rather than on a full-time basis for the term of the lease, the lease specifies exactly the schedule of such intervals, their precise length, and the exact rent for such interval.

(4) The term of the lease is for not less than one year.

(5) The aggregate rental charge is set in advance, is consistent with fair market value in arms-length transactions and is not determined in a manner that takes into account the volume or value of any referrals or business otherwise generated between the parties for which payment may be made in whole or in part under Medicare or a State health care program.

For purposes of paragraph (c) of this section, the term *fair market value* means the value of the equipment when obtained from a manufacturer or professional distributor, but shall not be adjusted to reflect the additional value one party (either the prospective lessee or lessor) would attribute to the equipment as a result of its proximity or convenience to sources of referrals or business otherwise generated for which payment may be made in whole or in part under Medicare or a State health care program.

(d) *Personal services and management contracts.* As used in section 1128B of the Act, "remuneration" does not include any payment made by a principal to an agent as compensation for the services of the agent, as long as all of the following six standards are met—

(1) The agency agreement is set out in writing and signed by the parties.

(2) The agency agreement specifies the services to be provided by the agent.

(3) If the agency agreement is intended to provide for the services of the agent on a periodic, sporadic or part-time basis, rather than on a full-time basis for the term of the agreement, the agreement specifies exactly the schedule of such intervals, their precise length, and the exact charge for such intervals.

(4) The term of the agreement is for not less than one year.

(5) The aggregate compensation paid to the agent over the term of the agreement is set in advance, is consistent with fair market value in arms-length transactions and is not determined in a manner that takes into account the volume or value of any referrals or business otherwise generated between the parties for which payment may be made in whole or in part under Medicare or a State health care program.

(6) The services performed under the agreement do not involve the counseling or promotion of a business arrangement or other activity that violates any State or Federal law.

For purposes of paragraph (d) of this section, an agent of a principal is any person, other than a bona fide employee of the principal, who has an agreement to perform services for, or on behalf of, the principal.

(e) *Sale of practice.* As used in section 1128B of the Act, "remuneration" does not include any payment made to a practitioner by another practitioner where the former practitioner is selling his or her practice to the latter practitioner, as long as both of the following two standards are met—

(1) The period from the date of the first agreement pertaining to the sale to the completion of the sale is not more than one year.

(2) The practitioner who is selling his or her practice will not be in a professional position to make referrals to, or otherwise generate business for, the purchasing practitioner for which payment may be made in whole or in part under Medicare or a State health care program after one year from the date of the first agreement pertaining to the sale.

(f) *Referral services.* As used in section 1128B of the Act, "remuneration" does not include any payment or exchange of anything of value between an individual or entity ("participant") and another entity serving as a referral service ("referral service"), as long as all of the following four standards are met—

(1) The referral service does not exclude as a participant in the referral service any individual or entity who meets the qualifications for participation.

(2) Any payment the participant makes to the referral service is assessed equally against and collected equally from all participants, and is only based on the cost of operating the referral service, and not on the volume or value of any referrals to or business otherwise generated by the participants for the referral service for which payment may be made in whole or in part under Medicare or a State health care program.

(3) The referral service imposes no requirements on the manner in which the participant provides services to a referred person, except that the referral service may require that the participant charge the person referred at the same rate as it charges other persons not referred by the referral service, or that these services be furnished free of charge or at reduced charge.

(4) The referral service makes the following five disclosures to each person seeking a referral, with each such disclosure maintained by the referral service in a written record certifying such disclosure and signed by either such person seeking a referral or by the individual making the disclosure on behalf of the referral service—

(i) The manner in which it selects the group of participants in the referral service to which it could make a referral;

(ii) Whether the participant has paid a fee to the referral service;

(iii) The manner in which it selects a particular participant from this group for that person;

(iv) The nature of the relationship between the referral service and the group of participants to whom it could make the referral; and

(v) The nature of any restrictions that would exclude such an individual or entity from continuing as a participant.

(g) *Warranties.* As used in section 1128B of the Act, "remuneration" does not include any payment or exchange of anything of value under a warranty provided by a manufacturer or supplier of an item to the buyer (such as a health care provider or beneficiary) of the item, as long as the buyer complies with all of the following standards in paragraphs (g)(1) and (g)(2) of this section and the manufacturer or supplier complies with all of the following standards in paragraphs (g)(3) and (g)(4) of this section—

(1) The buyer must fully and accurately report any price reduction of the item (including a free item), which was obtained as part of the warranty, in the applicable cost reporting mechanism or claim for payment filed with the Department or a State agency.

(2) The buyer must provide, upon request by the Secretary or a State agency, information provided by the manufacturer or supplier as specified in paragraph (g)(3) of this section.

(3) The manufacturer or supplier must comply with either of the following two standards—

(i) The manufacturer or supplier must fully and accurately report the price reduction of the item (including a free item), which was obtained as part of the warranty, on the invoice or statement submitted to the buyer, and inform the buyer of its obligations under paragraphs (a)(1) and (a)(2) of this section.

(ii) Where the amount of the price reduction is not known at the time of sale, the manufacturer or supplier must fully and accurately report the existence of a warranty on the invoice or statement, inform the buyer of its obligations under paragraphs (g)(1) and (g)(2) of this section, and, when the price reduction becomes known, provide the buyer with documentation of the calculation of the price reduction resulting from the warranty.

(4) The manufacturer or supplier must not pay any remuneration to any individual (other than a beneficiary) or entity for any medical, surgical, or hospital expense incurred by a beneficiary other than for the cost of the item itself.

For purposes of paragraph (g) of this section, the term *warranty* means either an agreement made in accordance with the provisions of 15 U.S.C. 2301(6), or a manufacturer's or supplier's agreement to replace another manufacturer's or supplier's defective item (which is covered by an agreement made in accordance with this statutory provision), on terms equal to the agreement that it replaces.

(h) *Discounts.* As used in section 1128B of the Act, "remuneration" does not include a discount, as defined in paragraph (h)(3) of this section, on a good or service received by a buyer, which submits a claim or request for payment for the good or service for which payment may be made in whole or in part under Medicare or a State health care program, from a seller as long as the buyer complies with the applicable standards of paragraph (h)(1) of this section and the seller complies with the applicable standards of paragraph (h)(2) of this section:

(1) With respect to the following three categories of buyers, the buyer must comply with all of the applicable standards within each category—

(i) If the buyer is an entity which reports its costs on a cost report required by the Department or a State agency, it must comply with all of the following four standards—

(A) the discount must be earned based on purchases of that same good or service bought within a single fiscal year of the buyer;

(B) the buyer must claim the benefit of the discount in the fiscal year in which the discount is earned or the following year;

(C) the buyer must fully and accurately report the discount in the applicable cost report; and

(D) the buyer must provide, upon request by the Secretary or a State agency, information provided by the seller as specified in paragraph (h)(2)(ii) of this section.

(ii) If the buyer is an entity which is a health maintenance organization or competitive medical plan acting in accordance with a risk contract under section 1876(g) or 1903(m) of the Act, or under another State health care program, it need not report the discount except as otherwise may be required under the risk contract.

(iii) If the buyer is not an entity described in paragraphs (h)(1)(i) or (h)(1)(ii) of this section, it must comply with all of the following three standards—

(A) the discount must be made at the time of the original sale of the good or service;

(B) where an item or service is separately claimed for payment with the Department or a State agency, the buyer must fully and accurately report the discount on that item or service; and

(C) the buyer must provide, upon request by the Secretary or a State agency, information provided by the seller as specified in paragraph (h)(2)(ii)(A) of this section.

(2) With respect to either of the following two categories of buyers, the seller must comply with all of the applicable standards within each category—

(i) If the buyer is an entity described in paragraph (h)(1)(ii) of this section, the seller need not report the discount to the buyer for purposes of this provision.

(ii) If the buyer is any other individual or entity, the seller must comply with either of the following two standards—

(A) where a discount is required to be reported to the Department or a State agency under paragraph (h)(1) of this section, the seller must fully and accurately report such discount on the invoice or statement submitted to the buyer, and inform the buyer of its obligations to report such discount; or

(B) where the value of the discount is not known at the time of sale, the seller must fully and accurately report the existence of a discount program on the invoice or statement submitted to the buyer, inform the buyer of its obligations under paragraph (h)(1) of this section and, when the value of the discount becomes known, provide the buyer with documentation of the calculation of the discount identifying the specific goods or services purchased to which the discount will be applied.

(3) For purposes of this paragraph, the term *discount* means a reduction in the amount a seller charges a buyer (who buys either directly or through a wholesaler or a group purchasing organization) for a good or service based on an arms length transaction. The term *discount* may include a rebate check, credit or coupon directly redeemable from the seller only to the extent that such reductions in price are attributable to the original good or service that was purchased or furnished. The term *discount* does not include—

(i) Cash payment;

(ii) Furnishing one good or service without charge or at a reduced charge in exchange for any agreement to buy a different good or service;

(iii) A reduction in price applicable to one payor but not to Medicare or a State health care program;

(iv) A reduction in price offered to a beneficiary (such as a routine reduction or waiver of any coinsurance or deductible amount owed by a program beneficiary);

(v) Warranties;

(vi) Services provided in accordance with a personal or management services contract; or

(vii) Other remuneration in cash or in kind not explicitly described in this paragraph.

(i) *Employees.* As used in section 1128B of the Act, "remuneration" does not include any amount paid by an employer to an employee, who has a bona fide employment relationship with the employer, for employment in the furnishing of any item or service for which payment may be made in whole or in part under Medicare or a State health care program. For purposes of paragraph (i) of this section, the term *employee* has the same meaning as it does for purposes of 26 U.S.C. 3121(d)(2):

(j) *Group purchasing organizations.* As used in section 1128B of the Act, "remuneration" does not include any payment by a vendor of goods or services to a group purchasing organization (GPO), as part of an agreement to furnish such goods or services to an individual or entity as long as both of the following two standards are met—

(1) The GPO must have a written agreement with each individual or entity, for which items or services are furnished, that provides for either of the following—

(i) The agreement states that participating vendors from which the individual or entity will purchase goods or services will pay a fee to the GPO of 3 percent or less of the purchase price of the goods or services provided by that vendor.

(ii) In the event the fee paid to the GPO is not fixed at 3 percent or less of the purchase price of the goods or services, the agreement specifies the amount (or if not known, the maximum amount) the GPO will be paid by each vendor (where such amount may be a fixed sum or a fixed percentage of the value of purchases made from the vendor by the members of the group under the contract between the vendor and the GPO).

(2) Where the entity which receives the good or service from the vendor is a health care provider of services, the GPO must disclose in writing to the entity at least annually, and to the Secretary upon request, the amount received from each vendor with respect to purchases made by or on behalf of the entity.

For purposes of paragraph (j) of this section, the term *group purchasing organization* (GPO) means an entity authorized to act as a purchasing agent for a group of individuals or entities who are furnishing services for which payment may be made in whole or in part under Medicare or a State health care program, and who are neither wholly-owned by the GPO nor subsidiaries of a parent corporation that wholly owns the GPO (either directly or through another wholly-owned entity).

(k) *Waiver of beneficiary coinsurance and deductible amounts.* As used in section 1128B of the Act, "remuneration" does not include any reduction or waiver of a Medicare or a State health care program beneficiary's obligation to pay coinsurance or deductible amounts as long as all of the standards are met within either of the following two categories of health care providers:

(1) If the coinsurance or deductible amounts are owed to a hospital for inpatient hospital services for which Medicare pays under the prospective payment system, the hospital must comply with all of the following three standards—

(i) The hospital must not later claim the amount reduced or waived as a bad debt for payment purposes under Medicare or otherwise shift the burden of the reduction or waiver onto Medicare, a State health care program, other payers, or individuals.

(ii) The hospital must offer to reduce or waive the coinsurance or deductible amounts without regard to the reason for admission, the length of stay of the beneficiary, or the diagnostic related group for which the claim for Medicare reimbursement is filed.

(iii) The hospital's offer to reduce or waive the coinsurance or deductible amounts must not be made as part of a price reduction agreement between a hospital and a third-party payor.

(2) If the coinsurance or deductible amounts are owed by an individual who qualifies for subsidized services under a provision of the Public Health Services Act or under titles V or XIX of the Act to a federally qualified health care center or other health care facility under any Public Health Services Act grant program or under title V of the Act, the health care center or facility may reduce or waive the coinsurance or deductible amounts for items or services for which payment may be made in whole or in part under part B of Medicare or a State health care program.

§ 1001.953 OIG report on compliance with investment interest safe harbor.

Within 180 days of the effective date of this subpart, the OIG will report to the Secretary on the compliance with §§ 1001.952(a)(2)(i) and 1001.952(a)(2)(vi).

Dated: July 19, 1991.

R.P. Kusserow,

Inspector General, Department of Health and Human Services.

Approved: July 22, 1991.

Louis W. Sullivan,

Secretary.

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