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JANUARY 29, 2003



Hagel's ethics filings pose disclosure issue
 By [Alexander Bolton](#)

On May 23, 1997, Victor Baird, who resigned Monday as director of the Senate Ethics Committee, sent a letter to Sen. Charles Hagel requesting "additional, clarifying information" for the personal financial disclosure report that all lawmakers are required to file annually.

Among other matters, Baird asked the Nebraska Republican to identify and estimate the value of the assets of the McCarthy Group Inc., a private merchant banking company based in Omaha, with which Hagel had a special relationship.

Hagel had reported a financial stake worth \$1 million to \$5 million in the privately held firm. But he did not report the company's underlying assets, choosing instead to cite his holdings as an "excepted investment fund," and therefore exempt from detailed disclosure rules.

Questioned by The Hill, several disclosure law experts said financial institutions set up in the same fashion as the McCarthy Group Inc. do not appear to meet the definition of an "excepted investment fund," — at least as the committee had defined the category until Monday.

Hagel has not been accused of any legal or ethical violation and his staff denies that there has been any wrongdoing.

William Canfield, a former Senate Ethics Committee staffer, said the committee originally intended an "excepted investment fund," an exemption to cover mutual funds that buy or sell thousands of different holdings over the course of a year.

Hagel, who was reelected last November by a lopsided majority, declined to comment on the ethics filing matter.

The McCarthy Group Inc. owns fewer than 20 assets.

Hagel's filing underscores the currently murky world of Senate disclosures rules in which definitions are subject to change and interpretations can be accepted without further question.

However, that definition has apparently changed under the panel's new staff director, Robert Walker, who met with Hagel's staff after The Hill began its inquiries.

Under either the old or new definition, Lou Ann Linehan, Hagel's chief of staff, denied that Hagel had failed to meet the Senate Ethics Committee's



[THOMAS BUTLER](#)

Sen. Charles Hagel (R-Neb.)

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reporting requirements in his annual financial disclosure forms.

Linehan emphasized that Hagel's financial forms had been reviewed and approved by the Ethics Committee.

"We did it according to what the Ethics Committee told us to do," she said: "I have box loads of paper from all the times we went down there and had them sign off on it. We went down and talked to them. If there is a mistake, we haven't made a mistake. The ethics people made a mistake."

One underlying issue is whether Hagel properly disclosed his financial ties to Election Systems & Software (ES&S), a company that makes nearly half the voting machines used in the United States, including all those used in his native Nebraska.

ES&S is a subsidiary of McCarthy Group Inc., which is jointly held by the holding firm and the Omaha World-Herald Co., which publishes the state's largest newspaper. The voting machine company makes sophisticated optical scan and touch-screen vote-counting devices that many states have begun buying in recent years.

An official at Nebraska's Election Administration estimated that ES&S machines tallied 85 percent of the votes cast in Hagel's 2002 and 1996 election races.

In 1996, ES&S operated as American Information Systems Inc. (AIS). The company became ES&S after merging with Business Records Corp. in 1997.

In a disclosure form filed in 1996, covering the previous year, Hagel, then a Senate candidate, did not report that he was still chairman of AIS for the first 10 weeks of the year, as he was required to do.

Under the ethics panel's regulations, an "excepted investment fund" is one that is: "publicly traded (or available) or widely diversified."

Hagel's compliance with prior Senate regulations hinges on whether the holding company is indeed publicly available and therefore may be properly listed as an excepted investment fund.

As recently as last Thursday, the committee defined a "publicly available" stock or investment as one that can be bought on a public market or for which information is publicly available.

For a stock or investment to be regarded as publicly available — under the panel's previous definition — the committee should be able to find publicly available information on the company's activities.

That definition comported with one provided by Stanley Brand, a prominent ethics lawyer who has advised many lawmakers on how to fill out their personal financial disclosure reports.

Brand said an investment is publicly available: "If it is purchasable. If there is a market for it."

"It could be a regional exchange. It could be a commodities market," he said.

Brand said it would be hard to show an investment is excepted if "it's so closely held that it doesn't have a readily ascertainable value and there's not a way to trade it on a market, even a regional market or in an electronic way."

That kind of information would be found in such standard reference outlets as Moody's Financial Services Information, Standard & Poor's register, or Barron's The Dow Jones and Financial Weekly.

A search's of all three revealed no references to the McCarthy Group Inc.

Furthermore, a comprehensive report ordered by The Hill from Dun & Bradstreet, a leading financial information firm serving creditors and investors, indicated that McCarthy Group Inc.'s financial information is not publicly available.

The report, dated last March, states that McCarthy Group Inc. controller Barb McQueen declined to provide any information of the kind that an outside investor would normally need in weighing the company's prospects.

To back up her argument that McCarthy Group Inc. need not be listed with a financial reference and yet still qualify as publicly available, Linehan noted the instructions that come with the Senate disclosure form.

They state: "If you are unable to ascertain through publicly available reference material or an investment advisor or broker whether an asset is publicly available, you may wish to report it, along with the additional information."

The instructional language suggests that a lawmaker report the underlying assets of an investment if it is difficult to determine whether it is "publicly available."

But Linehan claimed that she was sure at least one investment advisor and broker confirmed that McCarthy Group Inc. was publicly available. She was unable, however, to offer the name of any investment broker or advisor who consulted with Hagel or his staff on the matter.

Linehan was unable to provide any examples of outside trades in the firm's securities.

Instead she cited a revised standard implemented by the committee only this week, after The Hill began its inquiry.

On Monday, the committee changed its definition of "excepted investment fund" after Walker met with Linehan. Baird served as the panel's director for nearly 16 years.

The committee abandoned the more stringent definition of the term, which under the panel's rules, Hagel apparently failed to meet.

Under Walker's revised definition, the committee will decide, based on the specific facts of each case, whether an investment has been made in a publicly available firm, a circumstance that would allow it to be listed as an "excepted investment fund." But the panel will neither discuss any individual case nor offer any concrete standard under which a case may be judged.

Both definitions, while arcane, are at the core of the matter because they determine whether the two-term senator is obliged to disclose his underlying investment in ES&S, rather than merely cite McCarthy Group Inc., the holding company.

The newly weakened definition makes it virtually impossible to determine whether Hagel — or any other lawmaker — must report investments in non-traded private companies.

Several securities law experts, including Michael Perino, a professor teaching at Columbia University Law School, said “publicly available” is a term coined by the ethics panel that only it can define.

The evolving standard, which the Ethics Committee has yet to put down on paper or codify, reveals the murkiness of some ethics rules and how difficult it can be to determine if a lawmaker transgressed, even though a violation may seem unquestionable at first look.

Michael R. McCarthy, chairman of the McCarthy Group Inc. and Hagel’s campaign treasurer, acknowledged that the holding company is not publicly traded or widely diversified (under the committee’s definition), but claimed that it is publicly available.

“Our company is a privately held company where the shares are available to the public,” said McCarthy. “Our shares trade each year. It’s not SEC registered but it’s available to the public by private exchange or private treaty.”

McCarthy said Hagel’s \$1-5 million investment made him a “minor shareholder.”

Hagel’s ties to ES&S go beyond his financial stake. He served as its chairman when it was named AIS from the early ‘90s until March of 1995. He also was an investor in AIS Investors Inc. until the beginning of 1995, McCarthy said.

Hagel also served as president of McCarthy & Co, the financial advisory group, from July of 1992 until the beginning of 1996.

Campaign finance reports show that McCarthy has served as treasurer for Hagel for Nebraska and later Hagel for Senate from 1999 until as recently as December of 2002.

McCarthy’s son, Kevin, works in Hagel’s press shop.

Hagel’s unrecorded stake in the voting systems company poses an apparent conflict of interest on election reform issues.

Three companies, including ES&S, stand to make a large profits from election reform legislation enacted last year by Congress.

Many precincts around the country are expected to upgrade to optical scan and touch-screen voting machines as a result of recently enacted election reform.

“There’s the potential for a real gold rush for federal voting equipment manufacturers,” said Doug Chapin, director of Electionline.org, a clearinghouse of news on election reform sponsored by the Pew Charitable

Trusts.

ES&S is one of three companies, along with Diebold Election Systems and Sequoia Voting Systems, that will benefit from the trend.

Linehan called absurd the notion that Hagel attempted to hide his involvement in ES&S.

“There’s no secret here,” said Linehan. “The other big investor in ES&S is the Omaha World-Herald. It’s not a secret. They are the owners in McCarthy Group and ES&S.”

Linehan also noted that the Omaha World-Herald had previously reported Hagel’s ties to ES&S and that McCarthy Group Inc. reveals on its website that ES&S is a subsidiary.

However, Linehan acknowledged that McCarthy Group Inc. has provided that information on the web only since 2000. By then, Hagel had already filed five personal financial disclosure reports listing McCarthy Group Inc. as an “excepted investment fund.”