



FEDERAL ELECTION COMMISSION  
WASHINGTON, D.C. 20463

December 31, 2002

**MEMORANDUM**

**TO:** Ron M. Harris  
Press Officer  
Press Office

**FROM:** Joseph F. Stoltz *JF.S.*  
Assistant Staff Director  
Audit Division

**SUBJECT:** Public Issuance of the Final Audit Report on Buchanan Foster, Inc.

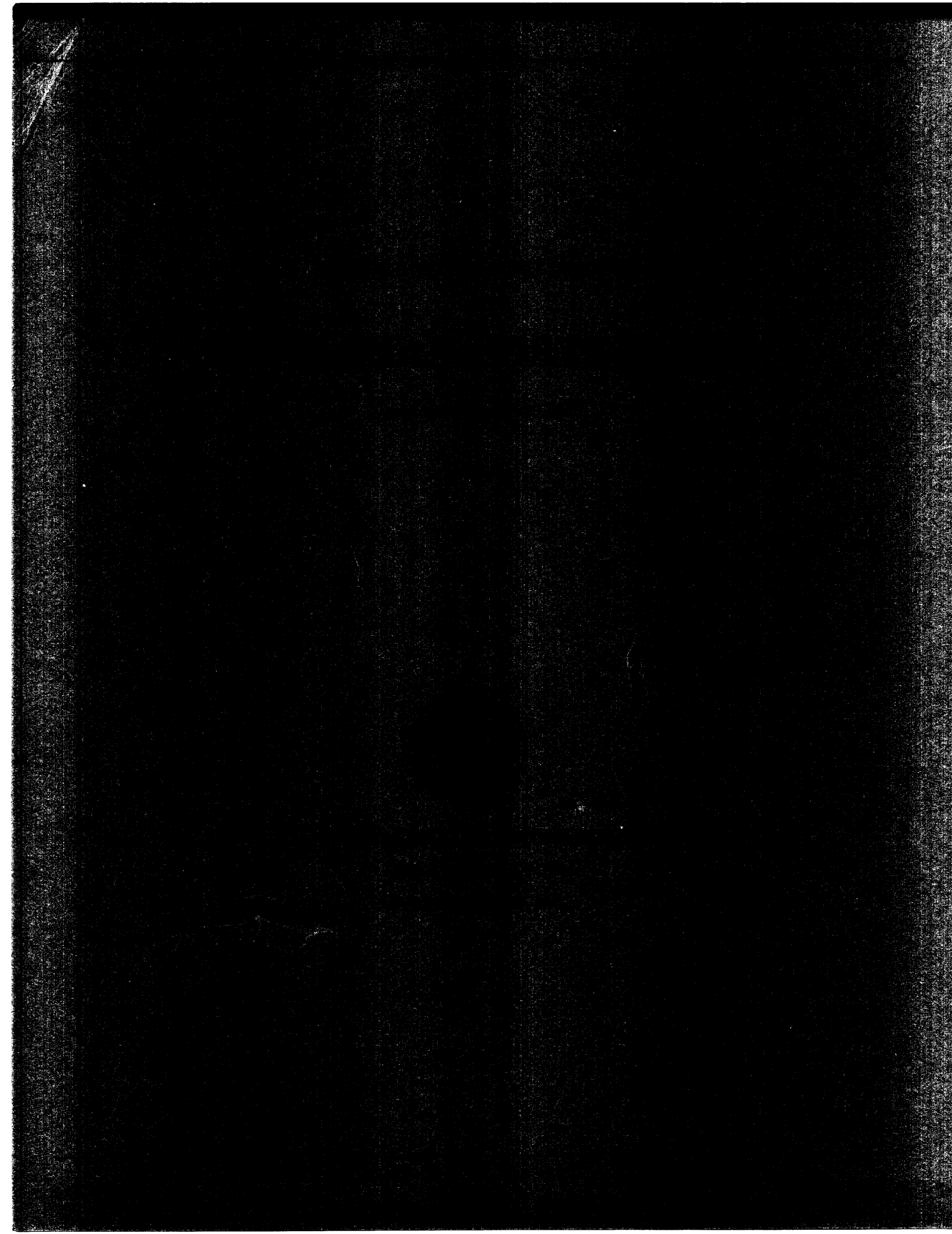
Attached please find a copy of the final audit report and related documents on Buchanan Foster, Inc. that was approved by the Commission on December 23, 2002.

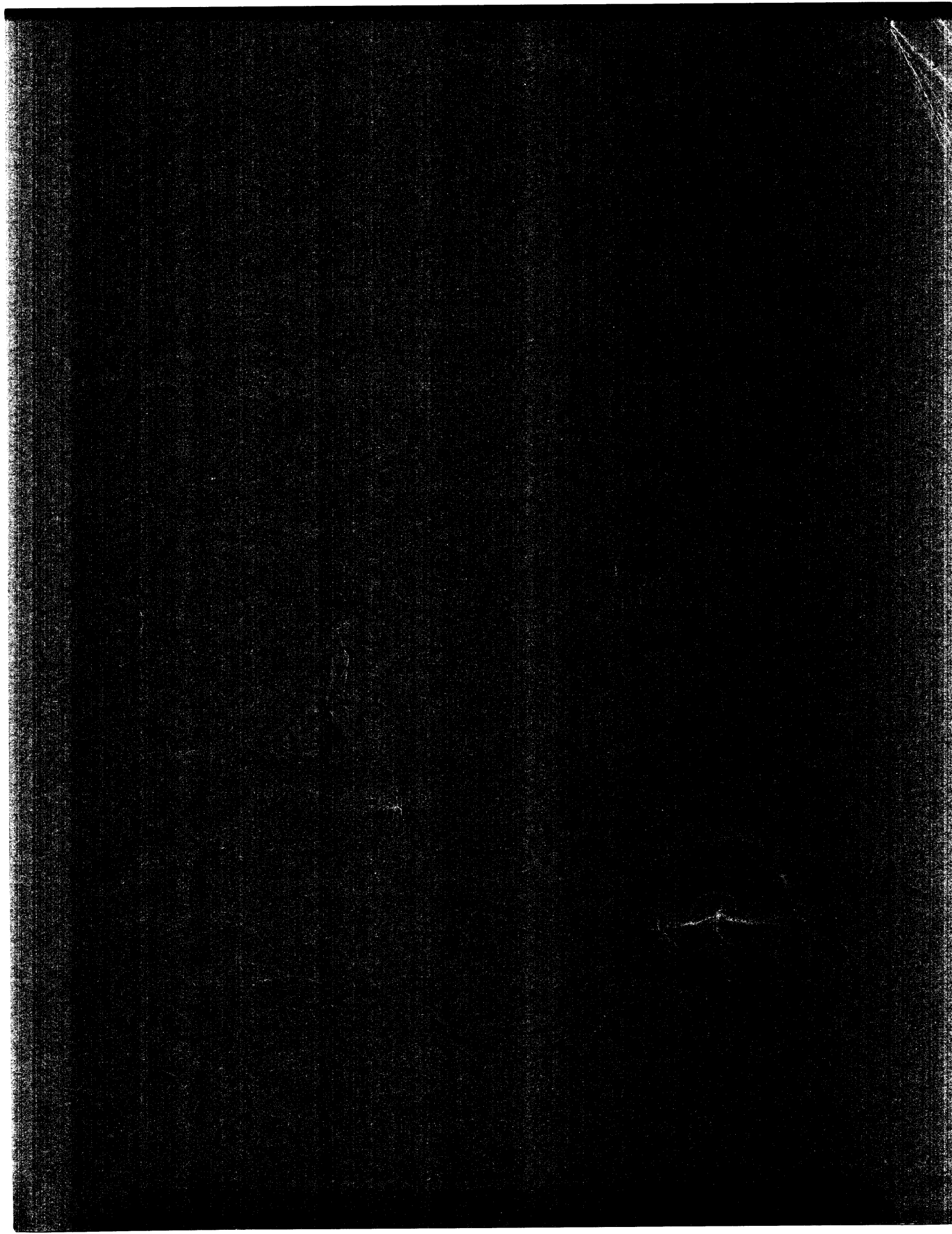
All parties involved have received informational copies of the report and the report may be released to the public.

Attachment as stated

cc: Office of General Counsel  
Office of Public Disclosure  
Reports Analysis Division  
FEC Library







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**REPORT OF THE AUDIT DIVISION**  
**ON**  
**BUCHANAN FOSTER, INC.**

Approved December 23, 2002



**FEDERAL ELECTION COMMISSION**  
**999 E STREET, N.W.**  
**WASHINGTON, D.C.**

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FEDERAL ELECTION COMMISSION  
WASHINGTON, D.C. 20463

**REPORT OF THE AUDIT DIVISION  
ON  
BUCHANAN FOSTER, INC.**

**EXECUTIVE SUMMARY**

The Committee to Elect Patrick J. Buchanan registered with the Federal Election Commission on August 31, 2000, as the principal campaign committee for Patrick J. Buchanan, candidate for the Reform Party's nomination for the office of President of the United States.<sup>1</sup>

The audit is mandated by Section 9007(a) of Title 26 of the United States Code, which requires the Commission to audit committees authorized by candidates of each political party for President and Vice President.

The findings of the audit were presented to BFI at the exit conference held on April 23, 2002, and in the preliminary audit report. BFI's responses to the findings are contained in the audit report.

The following is an overview of the findings contained in the audit report.

**ITEMIZATION OF RECEIPTS** – 2 U.S.C. §434(b)(3)(A) and 11 CFR §104.18(f). BFI did not itemize 76 contributions from individuals, totaling \$34,230, as required. BFI filed amended electronic reports itemizing the contributions as requested.

**APPARENT NON-QUALIFIED CAMPAIGN EXPENSES** – 11 CFR §§9002.11(a)(1); 9003.5(a); 9007.2(b)(2)(i) and (iii); and 9004.4(a)(5).

- **DONOR LIST** – BFI purchased a mailing list from Buchanan Reform, Inc. for \$197,496 but did not provide sufficient documentation demonstrating that the amount paid represented the fair market value of the list. The Audit staff determined the fair market value to be \$50,000 and the overpayment (\$147,496) has been included in the Statement of Net Outstanding Qualified Campaign Expenses as a receivable due from Buchanan Reform, Inc. As such, no repayment is warranted.

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<sup>1</sup> The Committee to Elect Patrick J. Buchanan amended its Statement of Organization on November 29, 2000 changing its name to Buchanan Foster, Inc. (BFI).

- **BONUSES** – BFI paid \$70,000 in bonuses and was unable to document that they were provided for pursuant to a written contract with the recipients made prior to the date of the election. The Commission decided that, although BFI’s documentation was not a written contract, it offered sufficient documentary evidence of BFI’s attempt to comply with the “written contract” provision at 11 CFR §9004.4(a)(5). As such, no repayment is warranted.

**NOQCE SURPLUS REPAYMENT** – 11 CFR §§9004.4(b)(9); 9007.2(b)(2)(iii); and 9007.2(b)(3). A Statement of Net Outstanding Qualified Campaign Expenses (NOQCE) was prepared to determine BFI’s financial position as of the end of the expenditure report period, December 7, 2000. The NOQCE Statement reflects a surplus of \$34,738 of which \$33,479 is repayable to the United States Treasury.

**INCOME RECEIVED** – 11 CFR §§9004.5; 9007.2(b)(2)(iii); 9007.2(b)(4). BFI earned interest (net of taxes) of \$25,478. Since BFI received funding from the Presidential Election Campaign Fund, a pro-rata portion of any income earned is repayable to the United States Treasury. As a result, BFI is required to repay \$24,554.



FEDERAL ELECTION COMMISSION  
WASHINGTON, D.C. 20463

***REPORT OF THE AUDIT DIVISION  
ON  
BUCHANAN FOSTER, INC.***

**I. BACKGROUND**

**A. AUDIT AUTHORITY**

This report is based on an audit of Buchanan Foster, Inc. (BFI). The audit is mandated by Section 9007(a) of Title 26 of the United States Code. That section states "after each presidential election, the Commission shall conduct a thorough examination and audit of the qualified campaign expenses of the candidates of each political party for President and Vice President." Also, Section 9009(b) of Title 26 of the United States Code states, in part, that the Commission may conduct other examinations and audits as it deems necessary to carry out the functions and duties imposed on it by this chapter.

In addition to examining the receipt and use of Federal funds, the audit seeks to determine if the campaign has materially complied with the limitations, prohibitions, and disclosure requirements of the Federal Election Campaign Act of 1971 (FECA), as amended.

**B. AUDIT COVERAGE**

The audit covered the period from BFI's first financial transaction, August 14, 2000, through December 31, 2001. BFI reported an opening cash balance of \$-0-; total receipts of \$13,496,168; total disbursements of \$13,475,936; and a closing cash balance of \$20,178. In addition, the Audit staff conducted limited reviews of reported activity through September 30, 2002.

**C. CAMPAIGN ORGANIZATION**

The Committee to Elect Patrick J. Buchanan registered with the Federal Election Commission (the Commission) on August 31, 2000, as the principal campaign committee for Patrick J. Buchanan. On November 29, 2000, an amended statement of organization was filed which indicated a name change to Buchanan Foster, Inc. Patrick J. Buchanan was a candidate for the Reform Party's nomination for the office of President of the United States. The Treasurer was, and continues to be, Angela M. Buchanan.

During the audit period, BFI maintained its headquarters in Vienna, Virginia and moved to McLean, Virginia in February of 2001. BFI maintained depositories in Vienna,

Virginia and Washington, D.C. To handle its financial activity, BFI used nine bank accounts. From these accounts, BFI made approximately 1,300 disbursements.

On September 13, 2000, the Commission determined that, based on the votes received by the Reform Party in the 1996 general election, Mr. Buchanan was eligible to receive pre-election funding from the Presidential Election Campaign Fund; BFI received \$12,613,452 from the United States Treasury on September 14, 2000. Additional receipts received through December 31, 2001, included \$535,675 in contributions from individuals; \$220,819 from vendor refunds and rebates; \$73,036 from interest and other income; and \$53,132 in transfers received from Buchanan Reform, Inc., the Candidate's primary campaign committee.

#### **D. AUDIT SCOPE AND PROCEDURES**

In addition to a review of expenditures made by BFI to determine if they were qualified or non-qualified campaign expenses, the audit covered the following general categories:

1. the receipt of contributions or loans in excess of the statutory limitations;
2. the receipt of contributions from prohibited sources, such as those from corporations or labor organizations;
3. proper disclosure of contributions from individuals, political committees and other entities, to include the itemization of contributions when required, as well as, the completeness and accuracy of the information disclosed (see Finding II.);
4. proper disclosure of disbursements including the itemization of disbursements when required, as well as, the completeness and accuracy of the information disclosed;
5. proper disclosure of debts and obligations;
6. the accuracy of total reported receipts, disbursements and cash balances as compared to campaign bank records;
7. adequate recordkeeping for transactions (see Finding III.A.);
8. accuracy of the Statement of Net Outstanding Qualified Campaign Expenses (NOQCE Statement) disclosing its financial position (see Finding III.B.);<sup>1</sup>
9. compliance with spending limitations; and,

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<sup>1</sup> BFI did not file a Statement of Net Outstanding Qualified Campaign Expenses. The Audit staff generated the Statement of Net Outstanding Qualified Campaign Expenses presented at Finding III.B.

10. other audit procedures that were deemed necessary in the situation (see Findings III.C. & III.D.).

As part of the Commission's standard audit process, an inventory of records was conducted prior to the audit fieldwork to determine if BFI's records were materially complete and in an auditable state. The records were found to be materially complete and the audit fieldwork commenced immediately.

Unless specifically discussed below, no material non-compliance was detected. It should be noted that the Commission may pursue further any of the matters discussed in this report in an enforcement action.

## **II. AUDIT FINDING AND RECOMMENDATION – NON-REPAYMENT MATTER**

### **ITEMIZATION OF RECEIPTS**

Section 434(b)(3)(A) of Title 2 of the United States Code states, in part, that each report under this section shall disclose the identification of each person (other than a political committee) who makes a contribution to the reporting committee in an aggregate amount or value in excess of \$200 within the calendar year,<sup>2</sup> together with the date and amount of such contribution.

Section 104.18(f) of Title 11 of the Code of Federal Regulations states, in part, if a committee files an amendment to a report that was filed electronically, it shall also submit the amendment in an electronic format. The committee shall submit a complete version of the report as amended, rather than just those portions of the report that are being amended.

The Audit staff reviewed all contributions from individuals requiring itemization. Based upon this review, it was determined that 76 contributions from individuals totaling \$34,230 were not itemized on Schedule A-P (Itemized Receipts) as required. Forty-three of the errors totaling \$30,834 (90%) involved contributions in amounts greater than \$200. The Audit staff could not determine, nor could BFI representatives explain, why these contributions were not itemized.

At an exit conference held at the close of fieldwork, the Audit staff discussed this matter with BFI representatives and provided them with a schedule of those contributions from individuals that had not been itemized. BFI representatives indicated amended disclosure reports would be filed.

In the preliminary audit report, the Audit staff recommended that BFI file complete amended reports itemizing the contributions from individuals discussed above.

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<sup>2</sup> This was changed to "election cycle" in the case of an authorized committee of a candidate for Federal office, effective for reporting periods beginning after December 31, 2000 [amended by section 641 of the Treasury and General Government Appropriations Act, 2000, Pub. Law No. 106-58, signed into law on September 29, 1999].

In response to the preliminary audit report, BFI filed complete amended reports as requested.

### **III. AUDIT FINDINGS AND RECOMMENDATIONS — AMOUNTS DUE TO THE UNITED STATES TREASURY**

#### **A. APPARENT NON-QUALIFIED CAMPAIGN EXPENSES**

Section 9002.11(a)(1) of Title 11 of the Code of Federal Regulations states, in part, that *qualified campaign expense* means any expenditure incurred to further a candidate's campaign for election to the office of President or Vice President of the United States.

Section 9003.5(a) of Title 11 of the Code of Federal Regulations states, in part, that each candidate shall have the burden of proving that disbursements made by the candidate or his authorized committee(s) are qualified campaign expenses as defined in 11 CFR 9002.11.

Section 9007.2(b)(2)(i) of Title 11 of the Code of Federal Regulations states, in part, that if the Commission determines that any amount of any payment to an eligible candidate from the Fund was used for purposes other than to defray qualified campaign expenses, 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.

Section 9007.2(b)(2)(iii) of Title 11 of the Code of Federal Regulations states, in part, that in the case of a candidate who has received contributions pursuant to 11 CFR 9003.3 (b) or (c), the amount of any repayment 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.

Section 9004.4(a)(5) of Title 11 of the Code of Federal Regulations states, in part, that monetary bonuses for committee employees and consultants in recognition for campaign-related activities or services shall be considered qualified campaign expenses, if provided for pursuant to a written contract made prior to the date of the election and are paid during the expenditure report period. Further Section 9002.12 of Title 11 of the Code of Federal Regulations states that the expenditure report period, in the case of a minor or new party, will be the same as that of the major party with the shortest expenditure report period. Therefore, BFI's expenditure report period would be August 16, 2000 through December 7, 2000.

The Audit staff conducted various reviews of BFI disbursements that resulted in the identification of the apparent non-qualified campaign expenses categorized below.

## 1. Purchase of Mailing List

The Audit staff noted that BFI purchased a mailing list (71,784 names) from the Primary Committee by check dated September 21, 2000, in the amount of \$197,496. To document this disbursement, BFI provided a memorandum from one of its direct mail vendors valuing the names on this list at \$2.75 per name. In a May 10, 2002, memorandum, the vendor states that:

“My recollection is that my recommendation of a \$2.75 per name purchase price by Buchanan Foster from Buchanan Reform of the latter’s donor list was based on the 1997 purchase, at \$3.00 per name, of the 1996 Buchanan campaign donor list by a private group of investors, headed by Richard Norman.

I believed that the private group, a disinterested group of businessmen intending to turn a profit on the list by renting it, had set a fair market price for the purchase of a donor list three years before the Buchanan Reform Buchanan Foster transaction. Wanting to make sure that this was a transparent transaction, I recommended a purchase price that was 25 cents per name less than the 1997 purchase.”

Absent additional details such as the size of that list and the basis for the \$3.00 valuation for each name by the private investors, the Audit staff is unable to assess the reasonableness of this valuation as a basis for pricing the list purchased from the Primary Committee. BFI also provided a written estimate dated January 5, 2001 from another direct mail vendor. The estimate addressed the potential rental income that could be derived from use of the list and estimated that income of \$156,780 could be earned over a period of 12 months. BFI later entered into an agreement with this vendor to market its mailing list. However, total income received by BFI from rental of the mailing list during 2001 was only about \$14,402. Prior to the estimate, both BFI and the Primary Committee utilized the services of this vendor bringing to question the independence of the valuation.

Reference materials are readily available to determine the market value for the use of a mailing list by another entity. For example, the Buchanan list is available for \$135 per thousand names.<sup>3</sup> The sale of all rights to a mailing list is more difficult, such sales are not common among campaigns. Neither the publisher of the rental guide nor two firms who market mailing lists were able to suggest a source for such a valuation. Further, the Audit staff was unable to locate reference materials to independently calculate a value for the sale versus rental of the mailing list. However, an analogous situation was found with the

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<sup>3</sup> Rate is according to SRDS Street Marketing List Source, December 2001, Volume 35, Number 6 for a list offered by Precision Marketing entitled Buchanan Campaign 2000 Donors. Since there are several Buchanan lists, the Audit staff cannot state with certainty that this is the same list as the one purchased.

Quayle 2000, Inc. Primary committee (Quayle 2000) where it purchased a mailing list from a political action committee. In order to establish fair market value, that committee obtained two independent valuations that valued the list at \$40,000 and \$50,000. The Audit staff notes that Quayle 2000 purchased the mailing list, which was of comparable size, for \$45,000; in this case, the apparent average of the two valuations.

As noted above, one valuation proffered to BFI was equivalent to 12 months rental. The Audit staff calculated the present value of the list based on an anticipated stream of rental income payments. The first month's rental income received by BFI was \$3,222, which was the largest monthly rental income payment received during 2001. The present value of monthly rental income payments of \$3,222 received for 12 months with an interest rate of 6%<sup>4</sup> is \$27,000. Considering that BFI is not an ongoing entity and could be expected to terminate in about two years, increasing the time period during which rental payments would be received to 24 months results in an increased present value for the list of \$40,437.<sup>5</sup> This present value analysis may be relevant, if BFI's intent was to market the list to recover the cost to purchase the list.

Therefore, it is the opinion of the Audit staff that BFI paid more than fair market value for the mailing list. Based upon the available information, we feel \$50,000, the highest appraisal value of a similar list, is a reasonable value for the list.

In the preliminary audit report, the Audit staff recommended that BFI provide documentation (such as appraisals from independent and qualified sources) or comments relative to the purchase of the mailing list. Absent such evidence, the Audit staff included an overpayment of \$147,496 in the NOQCE Statement as a receivable from the Primary Committee.

In response to the preliminary audit report, Counsel reiterates many of the facts already detailed above. Counsel offers additional information from BFI's Treasurer regarding the value of the list. Counsel states "Ms. Buchanan estimates that the Committee raised a net of almost \$400,000 from direct mail, more than defraying the cost of the list and further supporting the Committee's estimate of the list's value to the Committee."

In addition, Counsel contends that since the Audit staff conceded that it was unable to "locate reference materials" to calculate a fair market value, it is unreasonable for the Audit staff to substitute their valuation of \$50,000 for the Committee's valuation. Counsel states that as a general rule, the Commission has not examined the prices paid by a committee for goods and services, unless the price paid by the committee appeared to be too low. However, Counsel did not provide any documentation or examples to support this statement.

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<sup>4</sup> The average monthly prime interest rate for the period January 2001 through July 2002, the same time frame the mailing list was available for rent.

<sup>5</sup> Increasing the expected number of monthly payments or the monthly rental rate would result in an increased present valuation, as would a decrease in the interest rate.



The Audit staff, however, contends that the burden of proof regarding the value paid for goods or services rests with BFI. BFI is responsible for documenting that expenditures meet the definition of a “usual and normal charge” for goods and services, i.e., meaning the price of those goods in the market from which they ordinarily would have been purchased. As discussed above, Quayle 2000 purchased a comparable size mailing list for \$45,000. That campaign established fair market value by obtaining two independent valuations that valued the list at \$40,000 and \$50,000. The Audit staff agreed that Quayle 2000 had provided sufficient documentation to support the value paid for the list.

The Audit staff does not support the view that a value for a list should be established based upon how much income was raised using that list. Thus far, BFI has not provided sufficient documentation to support the value paid for its list. As such, the Audit staff’s position remains unchanged and \$50,000, the highest appraisal value of a similar list, is a reasonable value for the list.

As noted above, the Audit staff included an overpayment of \$147,496 in the NOQCE Statement as a receivable from the Primary Committee. Therefore, no pro-rata repayment to the United States Treasury is warranted.

## **2. Bonuses**

BFI paid \$70,000 in bonuses to six employees on November 2, 2000. An internal memorandum dated October 20, 2000, which listed the six recipients and the amounts they were to receive, refers to these payments as “general election bonuses.” However, BFI was unable to document that the bonuses were provided for pursuant to a written contract with the recipients made prior to the date of the election (November 7, 2000).

The Audit staff discussed this matter with BFI representatives at the exit conference. BFI representatives indicated they would provide additional documentation.

In the preliminary audit report, the Audit staff recommended that BFI submit documentation to demonstrate that the bonuses were provided for in written contracts with the recipients made prior to the date of the election. Absent such evidence, the Audit staff would recommend that the Commission make a determination that BFI make a pro-rata repayment of \$67,463 ( $\$70,000 \times .963751^6$ ) to the United States Treasury.

In response to the preliminary audit report, Counsel for BFI (Counsel) refers to these payments as “salary adjustments” and not bonuses. Counsel offers the explanation that BFI decided to continue its six top employees at their Buchanan Reform, Inc. (the Primary Committee) salary levels rather than raise their salaries to a level commensurate with their increased responsibilities in the general election campaign. He further explains that BFI promised these employees an increase in their compensation through a lump sum payment if federal funds became available and provides a written declaration from BFI’s

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<sup>6</sup> This figure (.963751) represents BFI’s repayment ratio as calculated pursuant to 11 CFR §9007.2(b)(2)(iii).

Treasurer to support this statement. Counsel also references the October 20<sup>th</sup> internal memorandum (as mentioned above) as support for the compensation adjustments.

Counsel contends that the Audit staff's reliance on 11 CFR §9004.4(a)(5) is misplaced. Counsel states "The Commission created 9004.4(a)(5) to ensure that committees do not give out, simply because they have surplus, public funds at the end of the campaign. Section 9004.4(a)(5) does not apply to adjustments to salary that are paid before the date of the election. Payments made prior to the date of the election are not subject to this provision. Only payments made after the date of the election. Campaign committees are free to adjust the salaries of their employees prior to the election."

The Audit staff concluded that the information provided in response to the preliminary audit report did not establish that the bonuses had been paid in accordance with 11 CFR §9004.4(a)(5) and recommended that a pro-rata repayment of \$67,463 be required. At its December 12, 2002 meeting, the Commission decided that, although the memorandum discussed above was not a written contract, it offered sufficient documentary evidence of BFI's attempt to comply with the "written contract" provision at 11 CFR §9004.4(a)(5) cited above.

#### **B. DETERMINATION OF NET OUTSTANDING QUALIFIED CAMPAIGN EXPENSES**

Section 9004.9(b) of Title 11 of the Code of Federal Regulations requires that, within 30 calendar days after the end of the expenditure reporting period, the candidate shall submit a statement of net outstanding qualified campaign expenses. The statement shall contain all outstanding obligations for qualified campaign expenses as of the date of the election; an estimate of the winding down costs and any campaign expenses that will be incurred by the end of the expenditure report period; and, the amount of cash on hand, assets and receivables as of the last day of the expenditure report period.

BFI did not file a Statement of Net Outstanding Qualified Campaign Expenses. As a result, the Audit staff prepared the NOQCE Statement presented below. The NOQCE Statement is as of December 7, 2000, the end of the expenditure report period, and is based on a review of BFI's financial activity through December 31, 2001, and a limited review of reported activity through September 30, 2002.

**BUCHANAN FOSTER, INC.**  
**STATEMENT OF NET OUTSTANDING QUALIFIED CAMPAIGN EXPENSES**  
As of December 7, 2000  
As Determined at September 30, 2002

**ASSETS**

Cash in Bank	\$587,298	
Accounts Receivable	174,209	
Amounts Due from Buchanan Reform, Inc.	350,097 (a)	
Capital Assets	<u>12,203</u>	
<b>Total Assets</b>		<b>\$1,123,807</b>

**OBLIGATIONS**

Accounts Payable	\$378,449 (b)	
Amounts Due to Buchanan Reform, Inc.	261,968 (c)	
Interest Payable to U.S. Treasury (see Finding III.D.)	24,554	
Winding Down Costs:		
Dec. 8, 2000 to September 30, 2002: Actual	393,298	
Oct. 1, 2002 to Dec. 31, 2004: Estimated	<u>30,800</u>	
<b>Total Obligations</b>		<b><u>1,089,069</u></b>
Net Outstanding Qualified Campaign Expenses – SURPLUS		<b><u>\$ 34,738</u></b>

**FOOTNOTES TO NOQCE**

- (a) This amount includes \$196,178 for half of the winding down costs paid by BFI for the period December 8, 2000, through September 30, 2002. In addition, the Audit staff has included an apparent overpayment (\$147,496) for the purchase of a mailing list, as discussed in Finding III.A.1.above, and an overpayment (\$6,423) for equipment and health insurance.
- (b) This figure represents disbursements paid during the period December 8, 2000, through September 30, 2002, for goods and/or services received prior to December 8, 2000. This figure also includes \$60 for estimated taxes on net income earned in 2002.
- (c) This amount includes half of the winding down costs paid by the Primary Committee for the period December 8, 2000, through September 30, 2002, or \$15,410, and all of the winding down costs (\$95,281) paid by the Primary Committee for the period August 12, 2000, through December 7, 2000. In addition, this amount includes \$151,277 for general election expenses paid by the Primary Committee after August 11, 2000.

### **C. NOQCE SURPLUS REPAYMENT**

Section 9007.2(b)(3) of Title 11 of the Code of Federal Regulations states, in part, that if the Commission determines that a portion of payments from the Fund remains unspent after all qualified campaign expenses have been paid, the candidate shall pay the United States Treasury that portion of surplus funds.

Section 9007.2(b)(2)(iii) of Title 11 of the Code of Federal Regulations states, in part, that in the case of a candidate who has received contributions pursuant to 11 CFR 9003.3 (b) or (c), the amount of any repayment 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. In the preliminary audit report, the Audit staff calculated that BFI had a surplus of \$239,171 and recommended that BFI provide evidence that it was not in a surplus position.

In response to the preliminary audit report, BFI provided documentation supporting that expenses totaling \$38,658 related to payables as of December 7, 2000, not winding down costs. Winding down costs are allocated equally between BFI and the Primary Committee while accounts payable are solely obligations of BFI. The Audit staff reviewed the documentation, agreed with this assessment and the NOQCE Statement was adjusted accordingly. In addition, the Audit staff reviewed reported activity through September 30, 2002, in order to update the NOQCE Statement. Finally, as a result of the Primary Committee's response to its audit report, the Amounts Due to Buchanan Reform, Inc. figure on the NOQCE Statement increased \$151,277 for general election expenses (primarily ballot access payments) paid by the Primary Committee and by \$47,837 for additional wind down expenses the Primary Committee could not incur during the expenditure report period. As a result, the NOQCE Statement reflects a surplus of \$34,738 of which \$33,479 ( $\$34,738 \times .963751$ ) is repayable to the United States Treasury.

#### **Recommendation #1**

The Audit staff recommends that the Commission determine that a pro-rata repayment of \$33,479 ( $\$34,738 \times .963751$ ) is due the United States Treasury.

### **D. INCOME RECEIVED**

Section 9004.5 of Title 11 of the Code of Federal Regulations states, in part, that investment of public funds or any use of public funds that results in income is permissible, provided that an amount equal to all net income derived from such use, less Federal, State and local taxes paid on such income, shall be paid to the United States Treasury.

Section 9007.2(b)(4) of Title 11 of the Code of Federal Regulations states that if the Commission determines a candidate received any income as a result of an investment or other use of payments from the fund pursuant to 11 CFR 9004.5, it shall so notify the

candidate, and such candidate shall pay to the United States Treasury an amount equal to the amount determined to be income, less any Federal, State or local taxes on such income.

Section 9007.2(b)(2)(iii) of Title 11 of the Code of Federal Regulations states, in part, that in the case of a candidate who has received contributions pursuant to 11 CFR 9003.3 (b) or (c), the amount of any repayment 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.

From its inception through December 31, 2001, BFI earned interest totaling \$41,638 from funds deposited into its bank and investment accounts. Documentation was provided indicating that federal and state taxes of \$16,332 had been paid. Therefore, BFI earned net income of \$25,306 (\$41,638 – \$16,332).

At an exit conference held at the close of fieldwork, the Audit staff discussed this matter with BFI representatives.

In the preliminary audit report, the Audit staff indicated that absent any additional documentation or comments submitted by BFI, the Audit staff would recommend that the Commission make a determination that BFI make a pro-rata repayment of \$24,389 ( $\$25,306 \times .963751$ ) to the United States Treasury.

In response to the preliminary audit report, Counsel contends that the requirement that net interest earned on deposits be refunded to the Treasury was intended to apply only to the campaigns of the major parties, which are prohibited from spending more money than they receive from the Presidential Election Campaign Fund. Since Mr. Buchanan did not receive the full federal payment, Counsel argues that BFI has the right to raise funds from other sources, and should have the right to retain interest on funds deposited in financial institutions.

The Audit staff's position is that the Code of Federal Regulations as cited above related to investment of public funds does not distinguish between fully funded and partially funded general election campaigns. In addition, relative to 11 CFR §9007.2, the Explanations and Justifications for Federal Election Commission Regulations dated June 16, 1995, states in part, "This amendment clarifies that receiving income from investment or any other use of payments from the Fund is a basis for requiring payment to the Treasury. The Commission will require the committee to pay any such income received, less taxes paid, to the Treasury. The revisions to sections 9004.5 and 9007.2 ensure that any income received through the use of public funds benefits the public financing system." Based upon the regulations as cited above, the opinion of the Audit staff remains unchanged.

As a result of our review of reported activity through September 30, 2002, net income of \$171 (\$231 - \$60) was identified. Therefore, BFI earned net income of \$25,478 (\$41,870 - \$16,392).

**Recommendation #2**

The Audit staff recommends that the Commission determine that a pro-rata repayment of \$24,554 ( $\$25,478 \times .963751$ ) is due the United States Treasury.

**IV. SUMMARY OF AMOUNTS DUE TO THE UNITED STATES TREASURY**

Finding III.C.	NOQCE Surplus Repayment	33,479
Finding III.D.	Income Received	<u>24,554</u>
	Total Due United States Treasury	<u>\$ 58,033</u>



FEDERAL ELECTION COMMISSION  
WASHINGTON, D.C. 20463

RECEIVED  
FEDERAL ELECTION  
COMMISSION  
AUDIT DIVISION

2002 NOV 22 A 11:42

November 21, 2002

**MEMORANDUM**

**TO:** Robert J. Costa  
Assistant Staff Director  
Audit Division

**THROUGH:** James Pehrkon  
Staff Director

**FROM:** Lawrence H. Norton  
General Counsel

Gregory R. Baker  
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**SUBJECT:** Proposed Audit Report on Buchanan/Foster Inc. (LRA #596)

**I. INTRODUCTION**

The Office of the General Counsel reviewed the proposed Audit Report ("Proposed Report") on Buchanan/Foster, Inc. ("General Committee") submitted to this Office on October 23, 2002. The following memorandum summarizes our comments on the Proposed Report.<sup>1</sup> Generally, we concur with the findings in the Proposed Report, and have provided additional legal analysis on three of the findings contained in the Proposed Report. We concur with any finding not specifically discussed in this memorandum. If you have any questions concerning our comments, please contact Kimberly D. Hart, the attorney assigned to this audit.

<sup>1</sup> The Office of the General Counsel recommends that the Commission consider this document in open session since the Proposed Report does not include matters exempt from public disclosure. 11 C.F.R. § 9007.1(e); 11 C.F.R. § 2.4.

## **II. APPARENT NON-QUALIFIED CAMPAIGN EXPENSES (Finding III.A.)**

Monetary bonuses for committee employees and consultants, given in recognition for campaign-related activities and services, are considered as qualified campaign expenses if they are provided for by written contract entered into prior to the date of the election and are paid during the expenditure report period. 11 C.F.R. § 9004.5(a)(5). The General Committee paid six employees a total of \$70,000 prior to the date of the election. However, the General Committee did not demonstrate that it entered into written contracts with the recipients of the bonuses prior to the date of the election.

The General Committee contends that the payments were not bonuses. Rather, the General Committee argues that the \$70,000 actually represents “salary adjustments” granted to those employees once the General Committee became eligible for funds for its general election campaign. The General Committee states that it hired many of the employees who worked for the Buchanan Reform, Inc. Primary Committee (“Primary Committee”). The General Committee made the decision to “continue its six top employees at the salary level they had while working with the Primary Committee because of the General Committee’s uncertainty concerning the availability of federal funds for the general election campaign.” The General Committee contends that these employees had increased responsibilities in working with the Committee and the General Committee “promised to increase their compensation through a lump sum payment if federal funds became available.” The General Committee argues that the internal memorandum, drafted on October 20, 2000, was intended to memorialize the General Committee’s intent to make the salary adjustments. The Committee also takes the position that 11 C.F.R. § 9004.4(a)(5) does not apply to salary adjustments.

We believe that the \$70,000 paid to six General Committee employees constitutes bonuses subject to the requirements of section 9004.5(a)(5). Although the General Committee contends that the payments were salary adjustments, it has not provided any documentation to demonstrate that these payments should be viewed as such, except for the internal memorandum. However, this is the same document that the General Committee argued, at the preliminary audit report stage, demonstrated that there were written contracts for bonuses entered into prior to the date of the election. In fact, the internal memorandum that purports to demonstrate that the payments were salary adjustments specifically designates the payments as bonuses and not salary adjustments. Furthermore, the General Committee did not submit any documentation to demonstrate that the duties and responsibilities of those staff employees increased when they went to work for the General Committee. Therefore, this Office concurs with the Audit staff’s position that the payments constitute bonuses that are subject to the requirements of 11 C.F.R. § 9004.5(a)(5).

## **III. DETERMINATION OF NET OUTSTANDING QUALIFIED CAMPAIGN EXPENSES (Finding III.B.1.)**

The Proposed Report recommends that the General Committee make a pro-rata repayment of \$218,059 for surplus funds. The surplus repayment is based on the Statement of



Net Outstanding Qualified Campaign Expenses (“NOQCE statement”). The NOQCE Statement includes an accounts receivable of \$147,496 from the Primary Committee. The Audit staff contends that the General Committee overpaid the Primary Committee \$147,496 when it purchased a mailing list from the Primary Committee. The Proposed Report concludes that the General Committee paid more than fair market value for the mailing list. The auditors believe the value of the list is \$50,000.

The General Committee states that its treasurer estimates that the “Committee raised a net of almost \$400,000 from direct mail, more than defraying the cost of the list and further supporting the Committee’s estimate of the list’s value to the Committee.” The General Committee argues that it submitted two valuations from direct mail vendors to support its contention that the price paid for the mailing list was fair market value. The first valuation, dated May 10, 2002, valued the mailing list of 71,784 names at \$2.75 per name.<sup>2</sup> The second appraisal valuation, dated January 5, 2001, addresses the potential rental income that could be derived from the use of the mailing list and estimates that income of \$156,780 could be earned over a period of 12 months by the General Committee.

The Audit staff compared the General Committee’s mailing list to another 2000 Presidential campaign mailing list of comparable size purchased from a political action committee.<sup>3</sup> The Audit staff noted that the Quayle Committee obtained two independent valuations, valuing the mailing list respectively at \$40,000 and \$50,000. The Quayle Committee subsequently purchased the mailing list for \$45,000, the apparent average of the two valuations. Based on the General Committee’s second appraisal, the Audit staff calculated the present value of the mailing list based on an anticipated stream of rental income payments for a 12 month time period.<sup>4</sup> This rental calculation is relevant if the General Committee attempted to rent the list to recover the purchase price. The auditors use this information to conclude that a reasonable value for the General Committee’s mailing list was \$50,000. Therefore, the Audit staff concluded that the General Committee paid more than fair market value for the mailing list. It is our

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<sup>2</sup> The \$2.75 per name valuation was based on the 1996 Buchanan Committee’s sale of its mailing list at \$3.00 per name. The vendor discounted the \$3.00 per name value to \$2.75 based on the differences in the time period. The General Committee also provided a valuation that was based on rental income from the mailing list.

<sup>3</sup> The Proposed Report notes that the Audit staff compared the General Committee’s mailing list to another 2000 Presidential campaign mailing list. However, the name of the committee is not specified. It is our understanding that a mailing list from the Quayle 2000 Primary Committee (“Quayle Committee”) was used for comparison purposes. The Office of General Counsel recommends that the Audit staff specify the Quayle Committee mailing list as the mailing list used by the Audit staff for comparison purposes in its cover memorandum. This will ensure that the Commission is fully informed of the specific mailing list used for comparison purposes.

<sup>4</sup> The Proposed Report states that “reference materials are readily available to determine the market value for the use of a mailing list by another entity. For example, the Buchanan list is available for \$135 per thousand names.” It is our understanding that the source of this information, SRDS Street Marketing List Source, contains several mailing lists and the one referred to in the Proposed Report is titled “Buchanan Campaign 2000 Donors.” However, the Audit staff cannot state with certainty that this is the same mailing list as the one at issue in the Proposed Report without comparing the names on both lists. Therefore, the Office of General Counsel recommends that the Proposed Report be revised to include clarifying language on this point.

understanding that the Audit staff believes that the \$400,000 raised by the General Committee from direct mail solicitations at a later date is not necessarily indicative of the value of the mailing list at the time of purchase. The Proposed Report notes that the General Committee's two appraisal valuations do not demonstrate that fair market value was paid by the General Committee for the mailing list because of the Audit staff's inability to assess the reasonableness of the May 10, 2002 valuation and the lack of independence of the January 5, 2001 appraisal valuation.<sup>5</sup>

We agree that there are some problems with the General Committee's valuation. However, in the alternative, the auditors provide their own valuation of the list based on a suggestion that the General Committee's list is comparable to the Quayle Committee's list and based on the rental value supported by the assumption that the General Committee would market the list to recover the purchase price. We have some concerns with the Audit Division's valuation. It is our understanding that the Quayle Committee list is similar in size. However, the Audit Division's comparison assumes that the value for each name on the Committee's list is the same as the Quayle Committee list. Furthermore, there is no indication that the General Committee intended to market the list to recover the purchase price.

The value of the mailing list drives the surplus repayment determination. However, this repayment determination is subject to judicial review. 26 U.S.C. § 9011(a). Therefore, it is imperative that the Audit Division's valuation is not arbitrary and capricious. We believe that an opinion from a professional independent appraiser in the mailing list industry would show that the valuation is not arbitrary and capricious.<sup>6</sup> As a condition to receiving public financing, the General Committee agreed to provide all documentation relating to receipts and disbursements and *other* information that the Commission may request. 11 C.F.R § 9003.1(b)(3)(emphasis added). Therefore, upon the Commission's request, the General Committee is obligated to provide the information.

In the Preliminary Audit Report, the Commission requested an independent appraisal, and the General Committee failed to provide this information. However, since this is a repayment matter, the General Committee could still submit the information as a part of its written materials at the administrative review stage. 11 C.F.R § 9007.2(c)(2)(i). Nevertheless, this approach requires the Commission to first use a specific amount on the NOQCE Statement for the value of the mailing list to actually notify the General Committee that there is a repayment. Given the limited options at this point, we believe that the Commission may use the Audit Division's valuation.

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<sup>5</sup> The Audit staff also questioned the independence of the appraisal valuation due to the fact that the General Committee and the Primary Committee had previously utilized services of the vendor and the General Committee later entered into an agreement with this vendor to market this particular mailing list.

<sup>6</sup> The auditors attempted to obtain an independent appraisal prior to the issuance of the Preliminary Audit Report. However, the auditors were unsuccessful in obtaining the appraisal.

When a committee does not submit documentation in support of its expenditures, the Audit Division may estimate the expenditures. *See John Glenn Presidential Committee v. FEC*, 822 F.2d 1097, 1103 (D.C. Cir. 1987) (Commission may estimate allocation of expenses to state expenditure limitations in the absence of documentation of the exact allocation). However, the committee must have the burden of producing the documentation.<sup>7</sup> A publicly-financed committee has the burden of demonstrating, with supporting documentation, that its disbursements are qualified campaign expenses. 11 C.F.R. § 9003.5(a).

The General Committee's disbursement for the mailing list is not addressed in the Proposed Report as an issue of whether it is a qualified campaign expense. The Proposed Report addresses the issue as a reimbursement from the Primary Committee to the General Committee. However, this issue is about a disbursement for a qualified campaign expense. Any amount that a committee overpays for goods and services is non-qualified campaign expense. *See Fulani v. FEC*, 147 F.3d 924 (D.C. Cir. 1998). The auditors contend that the General Committee overpaid the Primary Committee for the mailing list. Therefore, we recommend that the Audit Division revise the Proposed Report to address the mailing list payment as a General Committee's non-qualified campaign expense. If the Proposed Report is revised in this manner, the General Committee will have the burden of demonstrating that its disbursement to the Primary Committee for the mailing list was a qualified campaign expense.<sup>8</sup> If the General Committee fails to submit documentation (independent appraisal) supporting this disbursement as a qualified campaign expense during the administrative review, then the Commission is justified in using the Audit Division's valuation. *See John Glenn Presidential Committee v. FEC*, 822 F.2d 1097, 1103 (D.C. Cir. 1987).

#### **IV. INCOME RECEIVED (Finding III.B.2.)**

The Preliminary Audit Report identified \$41,638 in interest earned by the General Committee from funds deposited into its bank and investment accounts. The General Committee provided documentation indicating that federal and state taxes of \$16,332 had been paid leaving a net income of \$25,306 (\$41,638 - \$16,332). The Preliminary Audit Report recommended that the Commission make a determination that the General Committee should make a pro-rata repayment of \$24,389 to the United States Treasury.

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<sup>7</sup> In *John Glenn Presidential Committee v. FEC*, the John Glenn Presidential Committee exceeded two state expenditure limitations. The court noted that the amount in excess of the state expenditure limitation was a non-qualified campaign expense. *John Glenn Presidential Committee* at 1099. Therefore, the John Glenn Presidential Committee had the burden of demonstrating that it had not incurred non-qualified campaign expenses in excess of the state expenditure limitations. 11 C.F.R. § 9033.11(a)(1984).

<sup>8</sup> As a non-qualified campaign expense, the remedy is not necessarily a repayment to the United States Treasury. The Audit Division may maintain the Primary Committee's reimbursement to the General Committee as the General Committee's cure for its payment of a non-qualified campaign expense. *See Bush-Quayle '92 Primary Committee v. FEC*, 104 F.3d 448, 451 (D.C. Cir. 1997)(General election committee and compliance fund have standing with primary election committee to challenge repayment determination although compliance fund could reimburse the general election committee to eliminate a repayment).

In its response to the Preliminary Audit Report, the General Committee argues that:

the requirement that the net interest earned on deposits be refunded to the Treasury was intended to apply, however, only to the campaigns of the major parties which are prohibited by the Presidential Election Campaign Fund Act from spending more money than they receive from the Presidential Election Campaign Fund. ... As a candidate of a minor party, however, Mr. Buchanan did not receive full federal payment and, consequently, he had the right to raise funds from other sources, and should have the right to retain interest on funds deposited in financial institutions.

The Proposed Report concludes that 11 C.F.R. §§ 9004.5, 9007.2(b)(4), and 9007.2(b)(2)(iii) does not distinguish between fully funded and partially funded general election campaigns. The Office of General Counsel concurs with the Audit staff's conclusion that the applicable regulatory provisions on repayment of interest income received by committees does not distinguish between fully funded and partially funded general election campaigns. Furthermore, as a minor party candidate, Buchanan could accept contributions to defray qualified campaign expenses. 26 U.S.C. § 9003(c)(2). However, Buchanan's receipt of contributions as a minor party candidate does not entitle the candidate to the gains from the use of public funds. Requiring a repayment of gains on the investment of public funds "ensure that any income received through the use of public funds benefits the public financing system." Explanation and Justification for 11 C.F.R. § 9007.2 at 60 Fed. Reg. 31864 (June 16, 1995).



FEDERAL ELECTION COMMISSION  
WASHINGTON, D.C. 20463

December 26, 2002

Angela Buchanan, Treasurer  
Buchanan Foster, Inc.  
115 Rowell Court  
Falls Church, VA 22046

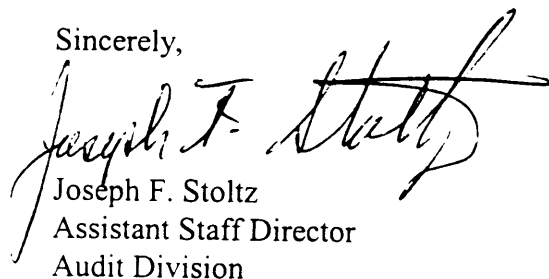
Dear Ms. Buchanan:

Attached please find the Report of the Audit Division on Buchanan Foster, Inc. The Commission approved the report on December 23, 2002. As noted in the report, the Commission may pursue any of the matters discussed in an enforcement action.

The Commission approved report will be placed on the public record on December 31, 2002. Should you have any questions regarding the public release of the report, please contact the Commission's Press Office at (202) 694-1220.

Any questions you have related to matters covered during the audit or in the report should be directed to Paula King or Alex Boniewicz of the Audit Division at (202) 694-1200 or toll free at (800) 424-9530.

Sincerely,



Joseph F. Stoltz  
Assistant Staff Director  
Audit Division

Attachment as stated

cc: John J. Duffy, Esq.



## CHRONOLOGY

### BUCHANAN FOSTER, INC.

Audit Fieldwork	07/15/01 – 4/19/02
Exit Conference	4/23/02
Preliminary Audit Report to the Committee	7/17/02
Response Received to the Preliminary Audit Report	9/19/02
Final Audit Report Approved	12/23/02

