



November 19, 2014

Members of the Commission  
Fair Political Practices Commission  
428 J Street, Suite 800  
Sacramento, CA 95814

RE: Agenda Item 53: Regulations 18704, 18704.1 and 18705.1

Dear Chair Remke and Commissioners:

On behalf of the League of California Cities City Attorneys FPPC Committee, I submit this letter for comment on the above-referenced agenda item.

Last April, the Commission adopted amendments to the regulations describing the financial impacts to real property that would be considered "material" for the purposes of conflicts of interest analysis. Staff now presents for your consideration amendments to the regulations describing the degree of impact to business entities that will be considered "material." At the Commission hearing on the real property materiality regulation, our committee expressed concern about the degree to which the proposed amendments moved away from more quantifiable, bright line standards to less concrete, "you know it when you see it" tests. The proposed amendments to the business entity materiality standards are very similar to the changes to the real property standards, and our committee continues to be concerned about this approach.

### **The Current Regulatory Scheme**

The current regulations address business entity conflicts in a two-step process. The first step is to determine if the business entity is "directly" or "indirectly" involved in the decision. Regulation 18704.1 provides that a business entity is directly involved in a governmental decision if it initiated the proceedings that will lead to the decision, or is otherwise the subject of the proceedings. If the business entity is not the subject of, or did not initiate, the proceedings, the business entity is considered to be "indirectly" involved in the decision.

The second step in the process is described in section 18705.1. If the business entity is directly involved in the decision, the effects of the decision are presumed to be material. The regulation provides that this presumption may be rebutted by proof that the decision will have no financial effect on the entity. If the entity is indirectly involved in the

decision, the official must apply a sliding scale of financial impact that relates to the size of the entity involved.

### **Staff's Proposed Regulation**

The proposed regulation seeks to simplify and clarify this scheme by removing the "direct/indirect" step, and establishing two new sets of criteria. Proposed subsection (a) sets forth a number of circumstances where the entity can be said to be directly involved in the decision. If one of these circumstances is present, the effects of the decision would be deemed material. There would be no opportunity to rebut this presumption. The proposed regulation would add an exception for agency purchases when the amount of the purchases would not equal or exceed \$1,000 within any 12-month period. The proposed regulation would also add a new exception that would apply to travel payments. This exception would permit an official to purchase fuel, meals, lodging, and transportation from an entity in which they have an interest, unless the purchase would be deemed "material" under the standards found in proposed subdivision (b).

Subdivision (b) contains the most significant changes to the existing regulatory scheme. This provision would eliminate the sliding scale approach, and replace it with a new, qualitative standard. Instead of asking the official to determine the dollar impact on the entity that could foreseeably result from the decision, the new regulation would ask the official to determine whether "...a prudent person with sufficient information would find it is reasonably foreseeable that the decision's financial effect would contribute to a change in the price of the business entity's publicly traded stock, or the value of a privately-held business entity." The proposed regulation goes on to list a number of decisions by reference to their effects that may result in the impact on the entity's value described above.

### **The Committee's Concerns**

#### *General Concern*

As an overarching, general comment, our committee believes the sliding scale approach contained in the existing regulation is better than the proposed "prudent person" standard. We believe the sliding scale provides a more concrete standard for measuring those financial impacts that are considered "material," and that this approach reflects that not all impacts on value are material. While the Committee supports the Commission's goal of simplifying and clarifying the business entity conflict regulation, we would prefer efforts to update and improve the sliding scale approach, instead of the adoption of the proposed "prudent person" standard.

#### *Specific Recommendations*

Recognizing that the Commission may prefer staff's approach, our committee also discussed ways in which the proposed language might be made more clear. For example, existing regulation 18904.1(a)(2) describes the circumstances under which an entity will

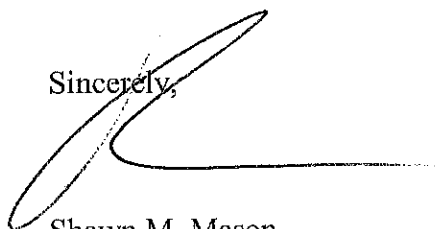
be considered to be “directly” involved in a decision, even though the entity did not initiate the proceedings. Staff’s proposal replaces this language with a number of different types of decisions described in proposed subdivisions (a)(2) through (a)(7). We find these subdivisions to be duplicative and confusing. For example, subdivisions (a)(2) and (a)(3) appear to describe the same thing (the purchase of goods or services), as, at least in part, do subdivisions (a)(5) and (a)(6) (which both describe regulatory proceedings involving the entity). We would recommend simply carrying over the language from existing regulation 18904.1(a)(2). This language sufficiently describes all of the decisions described in the proposed subdivisions. If the Commission concurs with this recommendation, our committee does support the proposed exception for smaller purchases described in proposed subdivision (a)(4). This would have to be redrafted as an exception to new subdivision (a)(2).

Another specific recommendation relates to the elimination of an existing exception relating to the financial impacts on very large companies. Existing regulation 189705.1(b)(2) provides an exception for decisions in which the entity is directly involved when the official’s interest in the entity is merely an investment interest valued at no more than \$25,000. Under these circumstances, the presumption of material effect would not apply, and instead, one would apply the sliding scale standard applicable to Fortune 500 companies, or companies with net income of no less than \$2.5 million. Staff’s proposal would eliminate this exception. As a result, if an official owned \$2,000 worth of Apple stock, they would not be able to participate in a decision to purchase \$1,000 worth of Apple equipment or software. Our committee believes this exception serves a useful purpose and should not be eliminated.

Before closing, I would like to thank Commission staff for the opportunity to provide feedback during the development of the proposed regulation. As city attorneys, we are frequently called upon to provide advice on business entity conflicts to local elected officials, appointed officials, and city staff. Recognizing this, staff reached out to our committee to discuss its ideas for improving regulation, and solicited our input on the proposed regulation as it was being drafted. As always, we appreciate being given the opportunity to participate in this effort.

Thank you for your consideration of these comments.

Sincerely,



Shawn M. Mason  
City Attorney of San Mateo  
Chair, League of Cities FPPC Committee