



FAIR POLITICAL PRACTICES COMMISSION

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To: Chair Remke, Commissioners Casher, Eskovitz, Wasserman, and Wynne

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Subject: Conflict of Interest Regulations, Public Generally, Regulation 18703

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Summary

A public official is prohibited from making, participating in making, or attempting to influence a governmental decision if it is reasonably foreseeable that the decision will have a material financial effect on the official's financial interest, *distinguishable from its effect on the public generally*. (Gov. Code, §§ 87100 and 87103.)¹ This agenda item involves amendments to the conflict of interest regulations addressing how the term “public generally” is applied.

Conflict of Interest Project

This proposal is part of the ongoing project to revise and streamline the regulations implementing the Act's conflict of interest provisions. To date, the Commission adopted regulatory changes to consolidate the conflict of interest analysis from 8 to 4 steps; amend the meaning of “reasonably foreseeable;” and modify the standards to determine if there is a “material financial effect” on an official's interests.

To determine if a public official has a disqualifying conflict, the 4-steps include:

1. Is it reasonably foreseeable that the governmental decision will have a financial effect on any of the public official's financial interests?
2. Will the reasonably foreseeable financial effect be material?
3. Can the public official demonstrate that the material financial effect on the official's financial interest is indistinguishable from its effect on the public generally?
4. Is public official making, participating in making, or in any way attempting to use his or her official position to influence a governmental decision?

There are two remaining steps to amend to complete the new analysis, public generally, which is presented here, and an official's involvement in the decision making process, which staff hopes to present to the Commission in the near future.

¹ The Political Reform Act (Act) is set forth in Government Code Sections 81000 through 91014, and all further statutory references are to this code. The Commission's regulations are contained in Division 6, Title 2 of the California Code of Regulations, and all regulatory references are to this source.

Problems with Existing Application of “Public Generally”

Currently, there are nine regulations applying the “public generally” provision. (Regs., 18707-18707.10.) The first two regulations establish the general rule, while the remaining seven carve out exceptions and special circumstances. The following summarizes each regulation:

Regulation 18707: This regulation sets up the analysis to apply the two-prong test provided in Regulation 18707.1. In practice, this regulation adds very little substantive value.

Regulation 18707.1: This regulation provides the general rule and the two-prong test to establish if the effect of a decision on an official's financial interest is indistinguishable from the effect on the public generally. The first prong is to determine if a “significant segment” is affected, and the second prong is to ask if those in that significant segment are affected “in substantially the same manner.” If the answer to both questions is yes, the official does not have a conflict.

Regulation 18707.2: This regulation creates a special proportional or across-the-board rule for certain assessments, fees, or tax rate decisions. The general rule in Regulation 18707.1 uses a dollar amount comparison and rejects a proportional basis test for effects on real property. Therefore, this special rule is used, for example, when water districts set uniform rates.

Regulation 18707.4: Because some boards and commissions require the appointment of officials who represent a specific industry or profession, this regulation applies public generally to all decisions that affect the specific interest substantially the same or proportionately the same. In other words, the scope of the significant segment is narrowed to the particular interest that the official was appointed to represent. This exception codifies the decision in *Consumers Union of U.S., Inc. v. California Milk Producers Advisory Board* (1978) 82 Cal.App.3d 434.

Regulation 18707.5: This regulation defines “significant segment” for purposes other than interpreting “public generally.” In particular, it establishes an exception to the definition of “source of income” for customers of an official's retail business. (§ 87103.5.) Since this issue is more appropriately addressed under the sources of income provisions, the definition was moved to new Regulation 18702.3 (Materiality Standard: Financial Interest in a Source of Income).

Regulation 18707.6: This regulation addresses financial effects that result from funds received through disaster relief programs under an official state of emergency declaration.

Regulation 18707.7: This regulation states that the public generally is affected in the same manner as an official's business interest if the business interest is in a business, trade, or profession that constitutes at least 50 percent of the businesses in the jurisdiction.

Regulation 18707.9: This regulation was adopted to codify *In re Ferraro* (1978) 4 FPPC 62. In this opinion, the Commission decided whether three councilmen who own single-family rental properties could vote on or participate in the consideration of a proposed rental control ordinance. The Commission concluded that the councilmen did not have a disqualifying conflict,

reasoning that the interests of owners of three or fewer rental units will not be affected by rent control decisions in a manner distinguishable from the effect upon a significant segment of the public generally.

Regulation 18707.10: The final regulation adopts a special rule for small jurisdictions when certain conditions apply. In short, this regulation provides an exception that allows an official, otherwise disqualified from a decision involving property within 500 feet of his or her domicile, to take part in the decision under the public generally exception if, among other conditions, the property affected by the decision is 300 feet or more from the official's domicile.

The most problematic issue with the existing public generally rule is that even when a “significant segment” can be identified, it is nearly impossible to show that the significant segment will be affected in “substantially the same manner” because the provision has been interpreted very narrowly. Even the smallest differences between the official’s interests and other interests within the “significant segment” usually will preclude an official from successfully asserting that the effect on his or her interest is indistinguishable from the public generally.

For example, when a decision affects an official’s financial interest in real property, current Regulation 18707.1(b)(2)(A) identifies thirteen factors to consider in determining whether the official’s interests will be affected in “substantially the same manner” as the “significant segment.” These factors range from general considerations such as the “magnitude” of the effect on the neighborhood to more specific considerations such as the lot size or square footage of building space. Since a decision’s financial effect is measured by changes in the value of the property in dollars (as opposed to proportionately), each factor can result in a finding that the effect is not “substantially the same.”

Notwithstanding the general rule, it’s important to note that when the Commission has had the occasion to consider the application of the public generally rule to more specific circumstances, it has typically interpreted the rule much more broadly. This has led to the adoption of multiple “special” public generally rules that are more lenient than the general rule, adding to the complexity of the provision.

Proposed Regulation 18703

Proposed Regulation 18703 will simplify the current regulatory scheme and replace the narrowly interpreted “substantially the same manner” standard with a “unique effect” test. Under the proposed language, once an official determines that a significant segment of the jurisdiction will be affected by the decision, the official is permitted to take part in the decision so long as the decision does not have a unique effect on the official’s interest in comparison to the significant segment. Additionally, proposed Regulation 18703 will simplify and condense the special rules currently provided in Regulations 18707.2 - 18707.10 into one subdivision.

Increasing the Significant Segment Threshold

In adopting a broader “unique effect” test (see below) staff believes that the existing significant segment thresholds need to be increased in order to provide a proper balance. As the public generally provision is intended to permit an otherwise disqualified official to participate in a governmental decision so long as the official can establish that decision’s effect on his or her interest is indistinguishable from the effect on the public as a whole, the existing 10% standards for interest in properties and individuals are considerably low.

Moreover, applying the existing numerical thresholds (5,000 properties or individuals and 2,000 businesses) is problematic. It allows officials in large jurisdictions to participate under the public generally provision despite the fact that only a very small fraction of the jurisdiction is affected by the decision. The overly strict interpretation of the “substantially the same manner” standard has been used to alleviate the concern with applying the public generally provision to decisions affecting only a small percentage of the public.

For these reasons, proposed Regulation 18703 seeks to strike the right balance by increasing the significant segment thresholds, while at the same time providing a less restrictive unique effect test.

Unique Effect Test

Staff is proposing the “unique effect” test to move away from the overly strict interpretation of the “substantially the same manner” standard. So long as a significant segment of the public is affected, the unique effect test is intended to allow officials to take part in more decisions under the public generally provision despite minor differences between the interests affected by the decision.

To provide guidance, the proposed regulation provides scenarios that would constitute a unique effect, focusing on the disproportionate effect of a decision on the official’s interest. The list is not inclusive, but provides examples of how the test will be applied.

Special Rules under Subdivision (e)

Proposed Regulation 18703(e) sets out the specific rules for special circumstances when the effect on an official’s financial interest will be deemed indistinguishable from that of the public generally and permit the official to participate.

Under the proposal, the current regulations that apply special rules (Regulations 18707.2, 18707.4, and 18707.6) are edited and incorporated into subdivision (e). And two additional rules are added to this subdivision. The first clarifies that the public generally provision will permit officials to participate in decisions regarding general fees that apply to the entire jurisdiction (subdivision (e)(2)). The second rule extends the public generally provision to limited neighborhood decisions affecting residential real property (subdivision (e)(3)).

Finally, other special rules will be repealed or substantively amended as follows:

Regulation 18707.5: This regulation will be deleted. It defines “significant segment” for purposes other than interpreting “public generally.” Since it establishes an exception to the definition of “source of income” for customers of an official’s retail business, as stated above, the definition was moved to new Regulation 18702.3 (Materiality Standard: Financial Interest in a Source of Income).

Regulation 18707.7: Under proposed Regulation 18703, an official can satisfy the public generally provision if the decision affects a single industry, trade, or profession, so long as significant segment threshold is met. Accordingly, staff finds no reason to continue to have a special rule for decisions affecting a single industry, trade, or profession; the public generally provision will apply only when the decision reaches the same broad segment of the public required for any other decision. Under this approach, Regulation 18707.7 is no longer necessary and will be deleted.

Regulation 18707.9: The residential property exception applicable to rental decisions by officials with three or fewer rental units will be deleted and replaced with a broader exception that applies equally to all interests in business entities or real properties that meet the new test. Proposed Regulation 18703(c)(3) provides that the cumulative effect on multiple interests is a unique effect only if the effect is substantially greater than the effect on a single interest. Under this new standard, multiple interests will no longer result in automatic disqualification. Therefore, the special rule for multiple rental units is no longer necessary; requiring officials with multiple rental units to meet the significant segment thresholds applied to other decisions.

However, because it is unlikely that a residential lessee would act to enrich his or her landlord, proposed Regulation 18707(e)(4) provides a special rule allowing officials to take part in decisions that affect all renters of residential property in their jurisdiction when the decision will only effect interests related to the official’s leasehold interest in his or her residence.

Regulation 18707.10: Prior to the conflict of interest project, officials were disqualified from any decision affecting the official's property if the property was within 500 feet of the property subject to the decision regardless of the scope of the effect on the official's property. Under this strict disqualification rule, there was concern that too many officials could be disqualified from a decision merely because officials in small jurisdictions reside in a limited geographical area. However, with earlier amendments to the materiality standards for real property now provided in new Regulation 18702.2, officials are no longer disqualified from decisions with an insignificant effect on their property merely because the property is within 500 of feet of the property subject of the decision. Accordingly, there is no longer a concern that disqualification rules are too strict as applied in small jurisdictions and Regulation 18707.10 should be deleted.

Technical Clean Up

In addition to the proposed amendments to the public generally provisions, staff is also proposing that the Commission delete current Regulations 18703.2, 18703.4, and 18703.5. While providing definitions for economic interests under the Act, these definitions merely restate statutory definitions and do not add anything substantively.

Conclusion and Recommendation

Staff submits that this proposal will improve the identification of potential conflicts of interest and promote compliance, while moving away from the overly strict “substantially the same manner” standard. Staff recommends that the Commission adopt the proposed amendments.

Attachments:

Amended Regulation 18703
Repealed Regulation 18703.2
Repealed Regulation 18703.4
Repealed Regulation 18703.5
Repealed Regulation 18707
Repealed Regulation 18707.1
Repealed Regulation 18707.2
Repealed Regulation 18707.4
Repealed Regulation 18707.5
Repealed Regulation 18707.6
Repealed Regulation 18707.7
Repealed Regulation 18707.9
Repealed Regulation 18707.10