



STATE OF CALIFORNIA
FAIR POLITICAL PRACTICES COMMISSION
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December 14, 2015

Thomas B. Brown
Burke Williams & Sorensen, LLP
1901 Harrison Street, Suite 900
Oakland, CA 94612-3501

Re: Your Request for Informal Assistance
Our File No. I-15-179

Dear Mr. Brown:

This letter responds to your request for advice on behalf of Councilmember Greg Pitts regarding the conflict-of-interest provisions of the Political Reform Act (the "Act").¹ Nothing in this letter should be construed to evaluate any conduct that has already taken place. In addition, this letter is based on the facts presented. The Fair Political Practices Commission (the "Commission") does not act as the finder of fact. (*In re Oglesby* (1975) 1 FPPC Ops. 71.) Because your questions are general in nature and not limited to specific governmental decisions, we are treating your request as one for informal assistance.²

Please note that we are only providing advice under the conflict of interest provisions of the Act and not under other general conflict of interest prohibitions such as common law conflict of interest or Section 1090.

QUESTION

As the Co-President of a boutique hospitality advisory firm, does the Act prohibit Councilmember Pitts from taking part in city council decisions involving (1) new revenue sources including becoming a charter city, imposing a real property transfer tax, increasing sales tax, increasing the city's occupancy tax, promoting new hotel developments, and expanding existing hotel entitlements and (2) the development of city owned properties, which may include a hotel?

CONCLUSION

Councilmember Pitts is not prohibited from taking part in decisions limited to enhancing taxation authority by becoming a charter city, imposing a real property transfer tax, or increasing

¹ The Political Reform Act is contained in Government Code Sections 81000 through 91014. All statutory references are to the Government Code, unless otherwise indicated. The regulations of the Fair Political Practices Commission are contained in Sections 18110 through 18997 of Title 2 of the California Code of Regulations. All regulatory references are to Title 2, Division 6 of the California Code of Regulations, unless otherwise indicated.

² Informal assistance does not provide the requestor with the immunity provided by an opinion or formal written advice. (Section 83114; Regulation 18329(c)(3).)

the city's sales tax. He is disqualified, however, from decisions such as increasing the city's occupancy tax, promoting new hotel development, and expanding existing hotel entitlements because of the nexus between the decisions and the income received as the Co-President of the hospitality advisory firm. To the extent that the decisions will be considered as a package, Councilmember Pitts is disqualified from taking part in decisions involving the package unless the decisions are segmented as provided in Regulation 18706.

Barring additional facts, Councilmember Pitts is not prohibited from taking part in the decisions regarding the Adams Street and Main Street Developments merely because the projects may include a hotel.

FACTS

Your office serves as the City Attorney for the City of St. Helena, and you are seeking advice on behalf of St. Helena City Councilmember Greg Pitts regarding decisions that could potentially affect the hospitality industry within the city and, therefore, may affect existing and potential clients of the councilmember's company.

Councilmember Pitts is Co-President of Realty Financial Resources, Inc. (RFR). RFR characterizes itself as "a boutique hospitality advisory firm [that] offers services ranging from project conceptualization and feasibility analysis to project financing. RFR operates in high barrier to entry markets with a focus on luxury resort hotels and mixed-use projects." RFR is primarily retained to raise capital for its clients (equity and debt in various forms) and is paid a "success fee" when such capital has been raised. Councilmember Pitts has no investment in RFR, is not an owner of RFR, has not been issued stock in RFR, and has no obligation to make any investment in RFR. RFR pays Councilmember Pitts through a consulting agreement, under which the councilmember receives commission income as a percentage of what hospitality clients pay RFR.

Councilmember Pitts receives no income directly from hospitality clients. Clients do, however, directly reimburse him for expenses such as travel. Councilmember Pitts, through RFR and not individually, currently represents one hospitality client interested in developing a project in St. Helena. He (again, through RFR) has also previously represented other hotel clients within the city. In the last 12 months, you have stated that RFR has represented one former client that never paid income to RFR because the project was not successful and a second client (commonly known as the Las Alcobas or Grandview Hotel) from which Councilmember Pitts received income, through RFR.

In light of interests arising out of his employment as a consultant for RFR, Councilmember Pitts would like advice regarding the application of the Act's conflict of interest provisions to city council decisions involving the following:

1. **New Revenue Options:** To improve the city's financial circumstances, the St. Helena City Council will consider a variety of options for finding new, and enhancing existing revenue sources. Possible options may include making St. Helena a charter city, with enhanced taxation authority, and imposing a real property transfer tax; increasing the city's sales tax; increasing the existing transient occupancy tax (TOT) rate on existing hotel guests; promoting new hotel development; and expanding existing hotel entitlements.

2. **Adams Street and Main Street Development:** The St. Helena City Council will consider the development of two city-owned properties (the “Adams Street Development” and the “Main Street Development”) The Adams Street Development site is 5.6 acres, and is currently undeveloped. The Main Street Development site is 1.7 acres, and is the location of the City’s current City Hall building. The City Council is expected to consider conducting an open Request for Proposal (RFP) process by which possible developers would present the City with proposals for site development. Such proposals could include hospitality (hotel) components.

Regarding decisions pertaining to the Adam Street Development and the Main Street, neither RFR nor Councilmember Pitts has a current client with an interest in developing either of the sites. RFR and Councilmember Pitts cannot rule out, however, the possibility that, in the future, they might be asked to represent or assist a client interested in developing those sites.

ANALYSIS

Section 87100 prohibits public officials from taking part in governmental decisions in which they have a financial interest. Section 87103 provides that a public official has a financial interest in a decision if it is reasonably foreseeable that the decision will have a material financial effect, distinguishable from its effect on the public generally, on the official, a member of his or her immediate family, or on any of the interests specified in Section 87103. Based upon the facts provided, Councilmember Pitts has the following interests:

RFR: An official has an interest in any business entity in which the official has a direct or indirect investment worth \$2,000 or more (Section 87103(a)) or any business entity in which the official is a director, officer, partner, trustee, or employee, or holds any position of management. (Section 87103(d).) While you have stated that Councilmember Pitts has no investment in RFR and works under a consulting agreement with RFR, Councilmember Pitts has an interest in RFR as a business entity as the Co-President of the company. Additionally, an official has an interest in any source of income aggregating \$500 or more in value received by, or promised to, the official within 12 months prior to the time when the decision is made. (Section 87103(c).) Accordingly, Councilmember Pitts also appears to have an interest in RFR as a source of income.

Clients of RFR: As stated above, an official has an interest in any source of income aggregating \$500 or more in value received by, or promised to, the official within 12 months prior to the time when the decision is made. (Section 87103(c).) You have stated that Councilmember Pitts receives income directly from RFR based upon the “success fees” paid to RFR by its clients. Pursuant to Regulation 18700.1, an official who receives commission income as a broker, agent, or salesperson for a specific sale or similar transaction may have interests in both the direct source of the income as well as the actual source of the income if the income from the source aggregates to \$500 or more in the previous 12 months. (Regulation 18700.1(c).)³ In this case, Councilmember

³ Officials may also have interests in sources of incentive compensation defined as an employee’s income “over above salary ... as sales or purchases of goods or services accumulate.” (Regulation 18700.1(d).) As the Co-President of RFR, to the extent Councilmember Pitt’s receives or is promised a “success fee” from any client purchasing RFR’s services, Councilmember Pitt’s may also have a source of income from the clients as sources of incentive compensation.

Pitts has an interest in any client of RFR if his commission income based upon the fees paid or promised by the client to RFR aggregate to \$500 or more prior to the decision.⁴

1. New Revenue Options:

Generally, a financial effect is presumed to be reasonably foreseeable if the interest is a named party in, or the subject of, a governmental decision before the official or the official's agency. (Regulation 18701(a).) If the interest is "not explicitly involved" in the decision, a financial effect is reasonably foreseeable if the effect can be recognized as a realistic possibility and more than hypothetical or theoretical. A financial effect need not be likely to be considered reasonably foreseeable. (Regulation 18701(b).) Different standards apply to determine whether a reasonably foreseeable financial effect on an interest will be material depending on the nature of the interest. (Regulation 18702.) The materiality standards for any particular interest are provided in Regulations 18702.1 through 18702.5.

You have identified multiple options for increasing revenue. For decisions limited to enhancing taxation authority by becoming a charter city, imposing a real property transfer tax, or increasing the city's sales tax, Councilmember Pitt's interests are not explicitly involved in the decisions. For decisions specific to the hospitality industry such as increasing the existing TOT, promoting new hotel development, and expanding existing hotel entitlements, we also find that Councilmember's interests in RFR are not explicitly involved in the decisions.⁵

Generally, a reasonably foreseeable financial effect on an official's interests in a business entity not explicitly involved in a decision, including a source of income from the sale of services, is material:

"[I]f 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 businesses entity's publicly traded stock, or the value of a privately held business entity." (Regulations 18702.1(b) and 18702.3(a)(4).)

For decisions limited to enhancing taxation authority by becoming a charter city, imposing a real property transfer tax, or increasing the city's sales tax, any effect on the value of specific businesses within the hospitality industry including RFR and clients of RFR is purely speculative and unmeasurable because the decisions apply broadly and are not specific to the hospitality industry. Accordingly, Councilmember Pitts is not prohibited from taking part in decisions limited to enhancing taxation authority by becoming a charter city, imposing a real property transfer tax, or increasing the city's sales tax.

⁴ We note that Councilmember Pitts also has an interest in his or her immediate family's personal finances. (Section 87103.) However, where a decision affects an interest in a business entity or real property, an effect on the official's personal finances need not be considered under Regulation 18702.5(c). Accordingly, we do not address the potential effect on the councilmember's personal finances further.

⁵ We are unable to determine whether Councilmember Pitt's interests in clients of RFR are explicitly involved in decisions to increase the existing TOT, promote new hotel development, or expand existing hotel entitlements based upon the facts provided. Nonetheless, because we find a reasonably foreseeable material effect resulting from his interest in RFR in these decisions, it is unnecessary to consider whether the councilmember's interest in clients of RFR are potentially disqualifying.

Turning to decisions specific to the hospitality industry such as increasing the existing TOT, promoting new hotel development, and expanding existing hotel entitlements, we must consider the “nexus test” as applied to Councilmember Pitt’s interests in RFR and clients of RFR as sources of income. As provided in Regulation 18702.3(c):

“Any reasonably foreseeable financial effect on a person who is a source of income to a public official is deemed material if the public official receives or is promised income the income to achieve a goal or purpose which would be achieved, defeated, aided, or hindered by the decision.”

The rationale for the nexus test is that when an employee earns salary or income to accomplish a purpose that may be advanced by what he or she does as a public official, we presume that the employer is benefiting from the actions of the employee in his or her official capacity. (*Furtek* Advice Letter, No. A-14-074; *Yarnell* Advice Letter, No. A-00-161.) Typically, a “nexus” is found in situations where the official is also a high-level employee with direct influence and control over his or her employer’s management or policy decisions. (*Furtek* Advice Letter, *supra*; *Moser* Advice Letter, No. A-03-147; *Low* Advice Letter, No. A-99-304.)

In interpreting the nexus test, we are also guided by the purposes the Act serves:

“Public officials should perform their duties in an impartial manner free from the pressures and bias caused by their own financial interests. (Section 81001, subds. (a) and (b).) To implement those goals, the assets and income of public officials which may be materially affected by their official actions must be disclosed. In appropriate circumstances the officials should be disqualified to avoid conflicts of interest. (Section 81002, subd. (d).) To this end the PRA should be liberally construed to accomplish its purposes. (Section 81003.) The PRA seeks to bring a degree of credibility to government by providing that those who hold a public trust must act, and appear to act, ethically. Erosion of confidence in public officials is detrimental to democracy. The election and appointment of ethical public officials depends upon an informed, interested and involved electorate. To maintain confidence and to avoid public skepticism, conflicts of interest must be shunned.” (*Consumers Union of U.S., Inc. v. California Milk Producers Advisory Bd.* (1978) 82 Cal. App. 3d 433, 443.)

Councilmember Pitts is one of two “Co-Presidents” of RFR. Based upon the facts provided, the councilmember has a consulting agreement with a boutique hospitality advisory firm that specializes in luxury hotels and mixed-use projects. Under this consulting agreement, Councilmember Pitts provides advice to the firm’s clients ranging from project conceptualization and feasibility analysis to project financing, and receives a commission based upon success fees paid by the firm’s clients.

While Councilmember Pitts may not have a financial investment in the business, the councilmember appears to hold a high-level position with the company sharing responsibilities with just one other Co-President. Moreover, RFR specializes in the development of hotels and Councilmember Pitts stands to receive commission income based upon the success of any projects

by RFR's clients within the city. Under these facts, at least some portion of Councilmember Pitt's income from RFR is received to achieve a goal or purpose that would be aided or hindered by decisions such as increasing the TOT, promoting new hotel development, and expanding existing hotel entitlements. For purposes of these decisions, we find a reasonably foreseeable effect on RFR and a nexus between the decisions and Councilmember Pitt's income. Accordingly, Councilmember Pitts is disqualified from taking part in the decisions such as increasing the TOT, promoting new hotel development, and expanding existing hotel entitlements.

Segmentation: As analyzed above, Councilmember Pitts is not disqualified from decisions limited to enhancing taxation authority by becoming a charter city, imposing a real property transfer tax, or increasing the city's sales tax, but is prohibited from decisions such as increasing the TOT, promoting new hotel development, and expanding existing hotel entitlements. To the extent that the decisions will be considered as a package, Councilmember Pitts is disqualified from taking part in decisions involving the package unless the decisions are segmented as provided in Regulation 18706.

The segmentation rule recognizes that the conflict of interest rules of the Act are applied on a decision-by-decision basis. Thus, even related decisions can be analyzed separately so long as they are not inextricably interrelated. For purposes of this regulation, decisions are "inextricably interrelated" when the result of one decision will effectively determine, affirm, nullify, or alter the result of another decision.

Regulation 18706 provides the method for segmentation of a governmental decision:

"(a) An agency may segment a decision in which a public official has a financial interest, to allow participation by the official, provided all of the following conditions apply:

"(1) The decision in which the official has a financial interest can be broken down into separate decisions that are not inextricably interrelated to the decision in which the official has a disqualifying financial interest;

"(2) The decision in which the official has a financial interest is segmented from the other decisions;

"(3) The decision in which the official has a financial interest is considered first and a final decision is reached by the agency without the disqualified official's participation in any way; and

"(4) Once the decision in which the official has a financial interest has been made, the disqualified public official's participation does not result in a reopening of, or otherwise financially affect, the decision from which the official was disqualified.

In this case, decisions limited to enhancing taxation authority by becoming a charter city, imposing a real property transfer tax, or increasing the city's sales tax do not appear to be inextricably interrelated to decisions such as increasing the TOT, promoting new hotel

development, and expanding existing hotel entitlements. To the extent that the decisions will be considered as a package, Councilmember Pitts is not prohibited from taking part in decisions limited to enhancing taxation authority by becoming a charter city, imposing a real property transfer tax, or increasing the city's sales tax so long as those decisions in which he may not take part in are considered first.

Public Generally Exception: The public generally exception permits an otherwise disqualified official to take part in a decision where the effect on the official's interest is indistinguishable from the effect on the public generally. (Regulation 18703.) Because we have found no reasonably foreseeable material effect on RFR or clients of RFR from decisions limited to enhancing taxation authority by becoming a charter city, imposing a real property transfer tax, or increasing the city's sales tax, it is unnecessary for us to consider the public generally exception as applied to these decisions. Moreover, for decisions such as increasing the TOT, promoting new hotel development, and expanding existing hotel entitlements, there is no indication from the facts presented that the public generally exception may apply.

2. Adams Street and Main Street Developments:

Based upon the facts provided, RFR is not explicitly involved in decisions regarding the Adams Street and Main Street Developments. You have also stated that neither Councilmember Pitts nor RFR has a client interested in either development. Provided that any source of income or promised income to Councilmember Pitts (RFR's clients) are not explicitly involved in the decision, the financial effect of the decision on Councilmember Pitt's interests in RFR and clients of RFR is foreseeable only if the effect can be recognized as a realistic possibility and more than hypothetical or theoretical. (Regulation 18701(b).) Additionally, the effect is material only "if a prudent person ... would find it is reasonably foreseeable that the decision's financial effect would contribute to a change in the price of the businesses entity's publicly traded stock, or the value of a privately held business entity." (Regulations 18702.1(b) and 18702.3(a)(4).)

In this case, the mere fact that the Adams Street and Main Street Developments may contain a hotel does not result in a foreseeable material effect on RFR or clients of RFR not explicitly involved in the decision. Accordingly, Councilmember Pitts is not prohibited from taking part in the decisions regarding the Adams Street and Main Street Developments barring additional facts. We caution, however, that should a company or individual explicitly involved in either development hire or indicate any interest in hiring Councilmember Pitts or RFR for any reason whatsoever, Councilmember Pitts may be disqualified from decisions involving the developments and should seek additional assistance providing the relevant facts.⁶

⁶ In light of this conclusion, it is unnecessary to consider segmenting decisions regarding the developments or the application of the public generally exception.

If you have other questions on this matter, please contact me at (916) 322-5660.

Sincerely,

Hyla P. Wagner
General Counsel

A handwritten signature in black ink, appearing to read "B. Lau", with a large, stylized flourish extending to the right.

By: Brian G. Lau
Senior Counsel, Legal Division

BGL:jgl