



STATE OF CALIFORNIA
FAIR POLITICAL PRACTICES COMMISSION
1102 Q Street • Suite 3050 • Sacramento, CA 95811
(916) 322-5660 • Fax (916) 322-0886

August 13, 2024

William Pahland
General Counsel
California State Treasurer's Office
901 P Street, Suite 411B
Sacramento, CA 95814

Re: Your Request for Informal Assistance
Our File No. I-24-088

Dear Mr. Pahland:

This letter responds to your request for advice on behalf of Deputy Treasurer John Sheldon regarding the statement of economic interest reporting provisions of the Political Reform Act (the "Act").¹ Formal advice is prohibited when the request for advice relates to past conduct. (Regulation 18329(b)(6)(A).) Informal assistance is permitted where the request regards past conduct but relates to corrective action to satisfy the requirements of the Act, such as filing an amended statement of economic interests. (Regulation 18329(c)(4)(A).) We are therefore treating your request as one for informal assistance.²

Please note that we are not a finder of fact when rendering advice (*In re Oglesby* (1975) 1 FPPC Ops. 71), and any advice we provide assumes your facts are complete and accurate. If this is not the case or if the facts underlying these decisions should change, you should contact us for additional advice.

QUESTION

Must Deputy Treasurer John Sheldon disclose his interests in individual stocks and securities held in managed accounts on his Statement of Economic Interest ("SEI")?

CONCLUSION

Based on the facts provided, his managed accounts meet the requirements outlined in Regulation 18237 and his interests in the managed accounts are not reportable investments.

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 18104 through 18998 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).)

FACTS AS PRESENTED BY REQUESTER

John Sheldon is currently serving as a Deputy Treasurer with the State Treasurer's Office. Deputy Treasurer Sheldon was formerly employed by Morgan Stanley. During his time at Morgan Stanley, he placed money into managed accounts to relinquish discretion and transfer power of attorney over much of his investment portfolio, which was a solution outlined by Morgan Stanley to remove various regulatory, compliance and legal issues associated with managing his own funds. These accounts are managed by investment professionals, who purchase securities on behalf of their clients. The clients, including Mr. Sheldon, give a power of attorney to the account manager. The account manager has complete discretion over the purchase and sale of investments. The managers populate the accounts with a broad array of securities from many more than 15 issuers. There is a stated policy to manage the accounts in a diversified manner and not hold securities concentrated in the same industry or business; the policy is to hold many diverse securities across many industries. The only influence the investors can possibly assert is to ask the managers to not invest in certain categories of stocks, such as tobacco stocks. There are more than 100 investors in each investment platform Deputy Treasurer Sheldon participates in.

ANALYSIS

An express purpose of the Act is to ensure that the assets and income of public officials that may be materially affected by their official actions be disclosed in order to avoid conflicts of interest. (Section 81001(b).) The Act's conflict of interest provisions ensure that public officials will perform their duties in an impartial manner, free from bias caused by their own financial interests. (Section 81001(b).) To that end, the Act specifically requires that certain officials must file a statement of economic interest disclosing reportable investments, business positions, interests in real property, and source of income upon assuming office, each year thereafter, and upon leaving office. (Sections 87200-87204.)

At issue here is the disclosure of Deputy Treasurer Sheldon's managed accounts, and whether the stocks and securities in these managed accounts meet the definition of the term "investment."³ Relevant to this matter, Section 82034 provides the following definition, in pertinent part:

"Investment" means any financial interest in or security issued by a business entity, including, but not limited to, common stock, preferred stock, rights, warrants, options, debt instruments, and any partnership or other ownership interest owned directly, indirectly, or beneficially by the public official, or other filer, or that person's immediate family, if the business entity or any parent, subsidiary, or otherwise related business entity has an interest in real property in

³ We note that Deputy Treasurer Sheldon previously contacted FPPC email advice when filing his assuming office SEI and was advised that these interests were not reportable as investments under the Act. He now seeks further clarification as to future disclosure or possible amendments in light of the conclusion in the *Watson* Advice Letter, No. A-22-088, which stated that an "index-tracking, tax-loss harvesting strategy" did not meet the criteria to qualify for the exception to the definition of "investment" found in Section 82034 and Regulation 18237, as was not a "bona fide investment fund that pools money from more than 100 investors" and, therefore, would be reportable.

the jurisdiction, or does business or plans to do business in the jurisdiction, or has done business within the jurisdiction at any time during the two years prior to the time any statement or other action is required under this title. An asset shall not be deemed an investment unless its fair market value equals or exceeds two thousand dollars (\$2,000).

Section 82034 excludes the following types of interests, including as relevant here, certain “diversified mutual funds,” from the definition:

[A] time or demand deposit in a financial institution, shares in a credit union, any insurance policy, interest in a diversified mutual fund registered with the Securities and Exchange Commission under the Investment Company Act of 1940 or in a common trust fund created pursuant to Section 1564 of the Financial Code, interest in a government defined-benefit pension plan, or any bond or other debt instrument issued by any government or government agency.

In adopting Regulation 18237 “Definition of Investments” in 2011 to interpret and clarify the “mutual fund exception” in Section 82034, the Commission recognized there are types of funds that share key characteristics with mutual funds and may also fall under the exception. Regulation 18237 states:

(a) For purposes of Section 82034, the term “investment” does not include a fund, including an exchange traded fund (ETF), closed-end fund or fund held in a plan qualified under Sections 401(k), 403(b), 457 or similar provision of the Internal Revenue Code (qualified plan), that is substantially similar to a “diversified mutual fund registered with the Securities and Exchange Commission under the Investment Company Act of 1940” if all the following are met:

(1) The fund is a bona fide investment fund that pools money from more than 100 investors and invests the money in stocks, bonds, or other securities.

(2) The fund holds securities of more than 15 issuers.

(3) The public official did not influence or control the decision to purchase or sell the specific fund on behalf of the official’s agency during the applicable reporting period.

(4) The public official does not influence or control the selection of any specific investment purchased and sold on behalf of the fund.

(5) The fund does not have a stated policy of concentrating its holdings in the same industry or business.

As you note in your request, there are more than 100 investors in each of the managed accounts in which Deputy Treasurer Sheldon participates. The managed accounts hold a broad array of securities from more than 15 issuers. The clients of the managed accounts grant a power of attorney to the account manager, who has complete discretion over the purchase and sale of securities. The only influence the investors can assert is to ask the managers not to invest in certain

general categories of stocks, such as tobacco stocks. Regulation 18237(a)(4) requires that the public official not influence or control the selection of any specific investment for the exception to the Act's definition of "investment" to apply. However, we note that typical investment portfolio exclusions, applicable to mutual funds and ETFs, include categories such as tobacco, controversial weapons, small arms, gambling, and alcohol.⁴ As such, the ability to request that investments do not include certain categories⁵ would not amount to the "selection of any specific investment." There is a stated policy "to manage the accounts in a diversified manner and not hold securities concentrated in the same industry or business; the policy is to hold many diverse securities across many industries." Based on the facts provided, Deputy Treasurer Sheldon's managed accounts meet the requirements outlined in Regulation 18237, and his interests in the managed accounts are not reportable investments.

If you have other questions on this matter, please contact me by email at norton@fppc.ca.gov.

Sincerely,

Dave Bainbridge
General Counsel

Zachary W. Norton

By: Zachary W. Norton
Senior Counsel, Legal Division

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⁴ Overview of Environmental, Social, and Governance (ESG) ETFs.
<https://www.schwab.com/etfs/types/socially-responsible-etfs>

⁵ To the extent that the ability to request exclusions of investments from certain categories becomes overbroad or extensive, so as to significantly limit or influence the selection of specific investments purchased on behalf of the managed accounts, or concentrating holdings in the same industry or business, this conclusion will not apply.