

# State of California



## Fair Political Practices Commission

P.O. BOX 807 • SACRAMENTO, 95804 • • • 1100 K STREET BUILDING, SACRAMENTO, 95814

Technical Assistance • • Administration • • Executive/Legal • • Enforcement • • Statements of Economic Interest  
(916) 322-3662 322-3660 322-5901 322-6441 322-6444

February 3, 1984

Thomas J. Harron  
Chula Vista City Attorney  
276 Fourth Avenue  
Chula Vista, CA 92010

Re: Your Request for Advice  
Our File Nos. A-83-283  
and A-84-005

Dear Mr. Harron:

This letter is sent in response to your requests on behalf of Chula Vista Councilmembers Frank Scott and David Malcolm for advice on the financial disclosure and conflict of interest provisions of the Political Reform Act.<sup>1/</sup> You raised a series of questions based on past situations involving Messrs. Scott and Malcolm, and you asked for our opinion on these situations since these questions are likely to come up again. The Act does not authorize our giving of advice as to past conduct; however, we are happy to provide you with general guidance and analysis of the issues. If similar situations arise in the future, we would assist you with specific advice at that time pursuant to Government Code Section 83114(b).<sup>2/</sup>

### Financial Interests

1. Councilmember Frank Scott. Mr. Scott is an account executive for Merrill Lynch, Pierce, Fenner & Smith, Inc. ("MLPF&S"), a large securities firm which conducts its business worldwide.<sup>3/</sup> MLPF&S offers financial services to individuals

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<sup>1/</sup> You sent letters dated December 19, 1983 and January 13, 1984. We agreed that I would respond to both letters by February 3, 1984.

<sup>2/</sup> All statutory references are to the California Government Code.

<sup>3/</sup> All of the facts and figures I cite concerning Merrill Lynch come from its 1982 Annual Report which you provided to me with your letter.

and to corporate and government clients;<sup>4/</sup> account executives for MLPF&S are paid commissions for the brokerage services they provide to their clients.

MLPF&S is the principal subsidiary of Merrill Lynch & Co., Inc. ("ML&Co.") which is a diversified financial services holding company.<sup>5/</sup> Mr. Scott owns stock in ML&Co. valued in excess of \$1,000.

ML&Co. is also engaged in real estate activities through its subsidiary, Merrill Lynch Realty, Inc. ("MLR"). Although Mr. Scott is not personally involved in MLR, he would receive a finders fee for any real estate business that he referred to MLR.

2. Councilmember David L. Malcolm. Mr. Malcolm is a real estate broker, and he has real property interests in Chula Vista.

Analysis:

1. Disclosure of Income from Clients - Mr. Scott

In your letter of January 13, 1984, you asked at what level of income Mr. Scott has to disclose the names of his clients. You sent a copy of the Merrill Lynch policy which makes information about clients confidential. We previously advised Mr. Scott in this regard; see attached letter to George D. Lindberg, dated March 9, 1983. On his Statement of Economic Interests, Mr. Scott should disclose on the Income Schedule the fact that he receives income in excess of \$250 from Merrill, Lynch, Pierce, Fenner & Smith. In addition, he should disclose on Schedule H (Income and Loans to Business Entities) the names of any clients for whose business he received \$10,000 or more in commission or other fees. Section 87207(b) (3).<sup>6/</sup>

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<sup>4/</sup> In 1982, MLPF&S had over 4.2 million individual customer accounts and over 20,000 institutional customer accounts.

<sup>5/</sup> In 1982, ML&Co.'s total gross revenues exceeded \$4.5 billion.

<sup>6/</sup> This section was upheld by the Supreme Court in Hays v. Wood, 25 Cal. 3d 772, 782-785 (1979)..

Thomas J. Harron  
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For purposes of disqualification, however, any client for whose business Mr. Scott has received \$250 or more in commission is a "source of income" to Mr. Scott. Section 87103(c). If there could be a material financial effect on such client as a result of a council decision, Mr. Scott must disqualify himself from that decision. He must disclose on the record that the client is a source of income when he disqualifies himself from participation in the decision; however, he need not disclose the nature or amount of the income. See Commission regulation 2 Cal. Adm. Code Section 18700(b) (5) (copy attached).

## 2. Disqualification

As you know, Section 87100 of the Act prohibits a public official from making, participating in, or attempting to influence governmental decisions in which the official has a financial interest. Financial interest is defined in Section 87103 as a reasonably foreseeable material financial effect of the decision on any business entity in which the official has an investment of \$1,000 or more, on any real property in which the official has an interest of \$1,000 or more, on any source of income to the official of \$250 or more in the preceding 12 months, or on any business entity in which the official holds any position of management.

A parent corporation and all of its wholly owned subsidiaries are usually considered to be a single entity for the purposes of disqualification under the Act. In the case of Merrill Lynch & Co., which is a financial holding company, it only does business through one of its subsidiaries, and all profits and losses of the subsidiaries flow directly back to the holding company. Accordingly, any effects on a subsidiary are considered to be effects on the parent and vice versa.

Since Mr. Scott owns shares valued at \$1,000 or more in Merrill Lynch & Co., the parent, he must disqualify himself from any council decisions which could materially affect Merrill Lynch & Co., MLPF&S, or MLR. Since Mr. Scott also receives income of \$250 or more from MLPF&S, there is another basis for disqualification from Council decisions which could materially affect MLPF&S. In addition, as noted above, any clients for whose business he has received \$250 or more in the preceding 12 months are sources of income to Mr. Scott.

One of the situations you raised in your letter of December 19, 1983, concerned the Chula Vista Redevelopment Agency, which is composed of the members of the City Council.

Thomas J. Harron  
February 3, 1984  
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Recently, the Agency considered a staff report on the marketing and sale of a Bayfront parcel in the Redevelopment Area of the city. The staff report evaluated proposals made by C. W. Clark, Inc., Grubb & Ellis, and Merrill Lynch Realty to obtain a listing for the exclusive right to sell the parcel, and the staff recommended to the Agency that they authorize the listing between the Agency and Grubb & Ellis. Councilmember Scott abstained from participation in the matter. You asked whether he should disqualify himself in similar situations which arise in the future.

As I stated above, Mr. Scott should disqualify himself from Council decisions which could materially affect Merrill Lynch & Co. or any of its wholly owned subsidiaries including MLR. In situations such as the one you posited, whether Mr. Scott should disqualify himself would depend on an analysis of the foreseeability and materiality issues. Normally where there are proposals to provide goods or services in front of a board or commission, it is reasonably foreseeable that any one of the proposals could be chosen. There may be unusual circumstances which would point to an opposite conclusion,<sup>7/</sup> but normally it may be assumed that a decision on the proposals could affect any of the bidders. Whether the effect would also be material would depend on the amount of the commission and/or other fees that the successful bidder would collect and the relationship of that amount to the size of the bidder. See Commission Regulation, 2 Cal. Adm. Code Section 18702(b). If the exact amount of the commission is not yet known, a reasonable estimate would suffice for this determination. Since ML&CO.'s annualized gross revenues exceed \$1 million, an effect on MLR would have to be \$100,000 or more in order to be considered material.

In your letter of December 19, 1983, you discussed generally two other matters that came before the council. One of the matters concerned the placement of a freeway sign on property adjacent to I-805 at the corner of Bonita Road; the other matter involved questions concerning development in the same area along Bonita Road including the issue of a possible moratorium on development until a study of the effects of further development on traffic volume could be made. Mr. Scott was not sure, but he thought that one of his clients from whom he had received more

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<sup>7/</sup> For example, if a bid were not seriously made with the hope of obtaining the contract, it would not be foreseeable that the decision would affect the bidder. See Opinion requested by Tom Thorner, 1 FPPC Opinions 198 (No. 75-089, December 4, 1975).

Thomas J. Harron  
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Page 5

than \$250 in income owned property in the vicinity of Bonita Road.<sup>8/</sup> Mr. Malcolm owns property in the same vicinity. My understanding is that you told the two councilmembers in both of these situations that it was not foreseeable that the decisions would affect their financial interests and that, therefore, they were not required to disqualify themselves pursuant to Sections 87100 and 87103.

You asked with reference to both of these situations when does a conflict become "ripe." In the freeway sign matter, you indicated that "...any action that they might take on the sign could later have a precedent setting effect which may affect the property value of the property in the vicinity" although, in your opinion, "the decision they were making affected only the property that had applied for the sign." On the moratorium question, the question was whether a council decision to do a study prior to imposing a moratorium created the same potential for conflicts of interest as a decision on the moratorium itself since they were closely related issues. The "ripeness" or foreseeability question can only be answered within the context of all of the relevant circumstances.

The statute does not require that the financial effect be certain; a substantial likelihood or probability is sufficient. See Opinion requested by Tom Thorner, 1 FPPC Opinions 198 (No. 75-089, December 4, 1975). "What is reasonably foreseeable must depend on the facts and circumstances of each specific situation." 1 FPPC Opinions at 205. All possible effects of the decision, not just the intended effects must be analyzed, although effects remote in time or speculative in nature are not reasonably foreseeable. It is also necessary to examine whether a decision in a matter will require or dictate a particular decision in another matter; if this is the case, the effects of the second decision are also foreseeable.

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<sup>8/</sup> Section 87100 provides that an official should not participate in a governmental decision if he knows or has reason to know that he has a financial interest in the outcome of the decision. Mr. Scott is not required to investigate his clients' financial affairs. If he has no indication that a client has a financial interest in a governmental decision, he is under no obligation to inquire further. However, if he becomes aware that a client has a potential financial interest in a City Council decision, he should make his determination on disqualification on the basis of what he knows and any information generally available.

Thomas J. Harron  
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As I noted in my introduction, I cannot advise you regarding the specific situations you raised since the actions have already been taken, and, in any event, I do not have enough facts to make a determination. However, I can discuss some of the questions which would need answers before I could make such a determination; these should indicate a direction for future analysis.

Freeway sign situation: To determine whether effects on the financial interest of either Mr. Malcolm or Mr. Scott would be foreseeable, I would ask:

1. What effect does the placing of the freeway sign have on the applicant's property?
2. What rules apply to the placement of freeway signs?
3. Have any other properties in the area applied for freeway signs? Disposition of these matters?
4. Has Mr. Malcolm applied for a freeway sign for his property? If not, is he contemplating doing so?
5. Same question as #4 for Mr. Scott's client.
6. What is the Assessor's opinion of effects on property value from the placement of a freeway sign? Effects on adjacent or nearby property?
7. What is the history of council decisions on the placement of freeway signs?

Moratorium situation:

1. Even though there had been no formal notice or motion on the matter, had the Council been seriously considering placing a moratorium on development? (E.g., had there been meetings, hearings, other studies, etc.?)
2. Is a traffic study required before the Council can impose a moratorium?

The answers to these and related questions should suggest the proper conclusion on the issue of foreseeability.

Examples of the analysis of foreseeability in specific situations can be helpful. Accordingly, I have enclosed copies

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of several staff advice letters which have detailed discussions of foreseeability in the context of land use matters.

I hope this letter is helpful to you and your clients. I look forward to the seminar on February 23. In the meantime, if I can be of further assistance, please feel free to contact me at (916) 322-6444.

Sincerely,

A handwritten signature in cursive script, reading "Diane Maura Fishburn", followed by a horizontal line extending to the right.

Diane Maura Fishburn  
Counsel  
Legal Division

DMF:pln  
Enclosures



# The City of Chula Vista

Office of the City Attorney (619) 691-5037

January 13, 1984

F P P C  
JAN 17 10 00 AM '84

Barbara A. Milman  
General Counsel  
Fair Political Practices Commission  
P.O. Box 807  
Sacramento, CA 95804

Dear Barbara:

This letter is a follow up to our telephone conversation on January 12, 1984 in which I asked you the question whether Chula Vista City Councilman Frank Scott, a stockbroker, is required to disclose the names of clients from whom he has received \$250 or more in commissions.

Frank Scott is a stockbroker for Merrill Lynch and has some Merrill Lynch stock, but an insignificant amount. It is not 10% of the company. Mr. Scott works on a commission basis. When he sells stock to a client he knows a certain percentage of the transaction will come to him. It has been our advice in the past that he need only disclose those clients from whom his pro rata share of fees was equal to or greater than \$10,000.

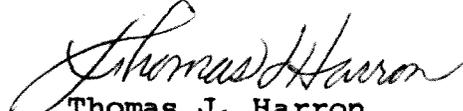
I have enclosed a copy of a Merrill Lynch policy which makes information about clients confidential. This policy would cause Mr. Scott no problems if the \$10,000 figure is used, but if he were required to disclose clients from whom he received \$250 in commissions, he would in all likelihood have to resign from the City Council in order to continue his employment with Merrill Lynch. In our telephone conversation you indicated to me that it was your understanding he need only disclose those clients from whom he has received more than \$10,000 in commissions. You also suggested that I follow this up with a request for a letter opinion.

In addition, I would again like to express my appreciation of the FPPC's agreement to participate in the workshop we are having on the Political Reform Act on February 23, 1984. I will be contacting City Attorneys and public officials throughout the area in the interim period to invite them to the workshop. I will send them a copy of your letter and encourage them to forward to you any questions they might have prior to the workshop.

Barbara Milman  
Fair Political Practices Commission  
January 13, 1984  
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Thank you very much for your courtesy and cooperation in this matter.

Very truly yours,

  
Thomas J. Harron  
City Attorney

TJH:clb  
enc.

**BLUE SKY**

Blue Sky considerations are essential whenever we are recommending securities to our customers. Since the laws in each state vary, it is the responsibility of the account executive and manager to be familiar with local requirements.

(Policy Manual, Section 03.63)

**CONFIDENTIAL NATURE OF ACCOUNTS**

Customer's accounts shall be handled in a highly confidential manner. Managers and account executives shall not discuss or convey, even by implication, the affairs of any customer with anyone else. Any transactions of customers shall not be discussed among employees who are not concerned with the matter.

It is Corporate policy that no information or records concerning the affairs of Merrill Lynch and/or its customers be released except to persons legally entitled to receive such, and then only in the appropriate manner. This includes confidential information requested during routine regulatory visits.

(Policy Manual, Section 09.3)  
(Policy Manual, Section 05.25.6)  
(Policy Manual, Section 05.25.6.1)

**Penny Stocks**

For the purposes of Corporate policy, any listed or unlisted stock or warrant which sells for under \$3.00 per share is classified as a penny stock. Accordingly, your actions should be governed by the following:

- a) there shall be absolutely no solicitation to buy securities in the penny stock category unless the Research Division has a favorable QRQ;
- b) new accounts may not be opened for the sole purpose of either buying or selling highly speculative securities generally described as penny stocks;
- c) sell orders for penny stock securities are acceptable provided the following two conditions are met:
  - 1. the securities to be sold are long in the account; and
  - 2. the order is related to the existing market.

Unsolicited buy orders for penny stocks for which the Research Division does not have a favorable QRQ may be accepted if the customer is a good customer, understands and is willing to accept the risks involved and is advised in advance that Merrill Lynch charges its standard commission rate.

(Policy Manual, Section 09.1.9)



# The City of Chula Vista

Office of the City Attorney (619) 691-5037

December 19, 1983

DEC 21 9 24 AM '83

Fair Political Practices Commission  
Legal Division  
P. O. Box 807  
Sacramento, California 95804

Re: Duty to Abstain Under Section 87103

Dear Sir or Madam:

On Thursday, December 15, 1983, the Chula Vista Redevelopment Agency, which is composed of the members of the City Council, considered a report on the marketing and sale of a Bayfront parcel in the Redevelopment area of the City of Chula Vista. Redevelopment staff had sent out a Request for Proposals (RFP) and the only respondents were C. W. Clark, Inc., the previous developer of the site under an expired agreement, Grubb & Ellis and Merrill Lynch Real Estate Division. Staff recommended to the Agency that they approve the selection of a review panel and authorize an exclusive right to sell listing between the Agency and Grubb & Ellis.

One of the members of the Redevelopment Agency is Councilman Frank Scott who is an account executive for Merrill Lynch. Mr. Scott abstained from participation in this matter, but at the same time he requested that I seek a letter opinion from the FPPC to guide him in future actions that raise the same issue.

Merrill Lynch is a holding company which wholly owns numerous subsidiaries. There is a separate corporate entity known as Merrill Lynch, Pierce, Fenner & Smith which is a brokerage for securities, option contracts, etc.. There is a second subsidiary corporation known as Merrill Lynch Real Estate Division that deals in land. Mr. Scott tells me that he does not know who the members of the Real Estate Division are and they would not know who he is. On the other hand, if Mr. Scott were to become aware of a potential real estate commission that could be earned, he would be able to refer this to the Real Estate Division and would be entitled to a finder's fee. That was not the case in this instance.

FPPC

December 19, 1983

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The question Mr. Scott posed was whether he, as a member of the brokerage firm, is required to abstain in matters that may affect the Real Estate Division or other divisions that may be affected by some action of the City. If he is required to abstain, he would also like to know the reason for this. Is it based on the provision that requires a person to abstain when he has received \$250 in income from a source and could the Real Estate Division be considered a source of income for him? If there is some other basis, he would like to know exactly what that basis is. Mr. Scott submitted a portfolio on Merrill Lynch to me and I have enclosed it for your consideration.

A second question which has occurred on numerous occasions involves the time which a conflict becomes "ripe". The Chula Vista City Council recently had before it a question as to whether a freeway sign would be permitted on property adjacent to I-805 at the corner of Bonita Road. Mr. Scott was not sure but he felt that there was a good possibility that a client of his from whom he had received more than \$250 in income owned property in the vicinity of the property in question. In addition, another Councilman, David Malcolm, who is a real estate broker, had an ownership interest in property in the vicinity. Neither of them had any interest in the property that was applying for the sign. Their concern was that any action that they might take on the sign could later have a precedent setting effect which may affect the property value of the property in the vicinity. It was my opinion at that time that the decision they were making affected only the property that had applied for the sign. It was too speculative to say whether their action would have an effect on any further applications in the future or whether the properties in which they were interested would even be interested in a similar application. That being that case, I felt that it was not "foreseeable" that their decision would have a material effect on any financial interest.

A similar question arose involving the same general area. Council was requested to impose a moratorium on any development along Bonita Road until a study could be made with regard to increasing volumes of traffic and how it would be handled. The same financial interests existed for Mr. Scott and Mr. Malcolm. This question was brought up by a member of the public at oral communications and there was no advance notice. One of the Councilmen made a follow-up motion that a study should be undertaken. The question of whether a moratorium should be imposed was put off

FPPC

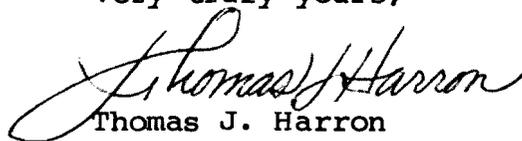
December 19, 1983

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until such time as that study would be completed. I called the FPPC with regard to this and discussed the question with one of the attorneys. I was advised that it would be proper for Mr. Malcolm and Mr. Scott to participate in the question as to whether a study should be undertaken and that if a moratorium was suggested as a result of that study, that they could abstain at that later date. The problem is that if they in fact do have a conflict of interest with regard to the moratorium and they would have to abstain on the question on whether a moratorium would be imposed, wouldn't they also be able to serve that interest by voting against the study in the hope that if no study is undertaken, the question of the moratorium would never arise? I would characterize these questions as questions about "conflict of interest--one step removed". While I want to make sure that Councilmembers do not participate in any decision where they may have a conflict of interest, I don't want to disenfranchise members of the Council by going overboard in this regard.

Any direction that you might give would be greatly appreciated.

Very truly yours,



Thomas J. Harron  
City Attorney

TJH:lgk  
Enc.

# State of California



## Fair Political Practices Commission

P.O. BOX 807 • SACRAMENTO, 95804 • • • 1100 K STREET BUILDING, SACRAMENTO, 95814

Technical Assistance • • Administration • • Executive/Legal • • Enforcement • • Statements of Economic Interest  
(916) 322-5662 322-5660 322-5901 322-6441 322-6444

January 18, 1984

Thomas J. Harron  
City Attorney  
276 Fourth Avenue  
Chula Vista, CA 92010

Re: A-84-005

Dear Mr. Harron:

Your letter requesting advice under the Political Reform Act has been referred to me. If you have any questions about your advice request, please contact me directly at (916) 322-5901.

We try to answer all advice requests promptly. Therefore, unless your request poses particularly complex legal questions, or unless more information is needed to answer your request, you should expect a response within 21 working days.

Very truly yours,

*Barbara A. Milman*  
Barbara A. Milman  
General Counsel

BAM:plh

# State of California



## Fair Political Practices Commission

P.O. BOX 807 • SACRAMENTO, 95804 • • • 1100 K STREET BUILDING, SACRAMENTO, 95814

Technical Assistance • • Administration • • Executive/Legal • • Enforcement • • Statements of Economic Interest  
(916) 322-5662                      322-5660                      322-5901                      322-6441                      322-6444

December 22, 1983

Thomas J. Harron  
City Attorney  
276 Fourth Avenue  
Chula Vista, CA 92010

Re: A-83-283

Dear Mr. Harron:

Your letter requesting advice under the Political Reform Act has been referred to Diane Maura Fishburn, an attorney in the Legal Division of the Fair Political Practices Commission. If you have any questions about your advice request, you may contact this attorney directly at (916) 322-5901.

We try to answer all advice requests promptly. Therefore, unless your request poses particularly complex legal questions, or unless more information is needed to answer your request, you should expect a response within 21 working days.

Very truly yours,

Barbara A. Milman  
Chief, Legal Division

BAM:plh