



California Fair Political Practices Commission

April 7, 1987

John K. Gillies
P.O. Box 506
Del Mar, CA 92014

Re: Your Request for Advice
Our File No. A-87-81

Dear Mr. Gillies:

You have requested advice concerning your disclosure responsibilities under the conflict of interest provisions of the Political Reform Act (the "Act").^{1/}

QUESTIONS

1. Is income from transactions on a regulated commodity futures market exempt from the disclosure requirements of the Political Reform Act?
2. Does trading on a national commodity futures market, through an out-of-state brokerage firm, result in receipt of income from a source which is doing business within the jurisdiction for disclosure purposes?
3. Is interest from the cash balance in a trading account income which must be reported under the Act?

CONCLUSIONS

1. Exemption from the income disclosure requirements is specifically limited to a security which is registered with the Securities and Exchange Commission. This provision does not include the commodity futures market, and therefore, sales from commodity futures do produce income within the meaning of the Act.
2. Although the proceeds from sales of commodity futures are reportable as income, the income is not from a business entity source doing business in your jurisdiction (the City of Del Mar).

^{1/}Government Code Sections 81000-91015. All statutory references are to the Government Code unless otherwise indicated. Commission regulations appear at 2 California Administrative Code Section 18000, et seq. All references to regulations are to Title 2, Division 6 of the California Administrative Code.

Therefore, the income from your transactions in commodity futures is not reportable income.

3. Interest earned on the cash balance of your trading account is paid by your broker, who is doing business in your jurisdiction, and must be reported as income.

FACTS

You are a city council member who is required to file a statement of economic interests, Form 721. (Sections 87200, 87203.) Part of your income is derived from trading in commodity futures and from interest on the cash balance of the trading account you have established with your brokerage firm. Your brokerage firm is headquartered out-of-state and does not have an office in your jurisdiction.

Commodity futures are transactions in "contracts for future delivery" which are traded on "contract markets" registered with and regulated by the Commodity Futures Trading Commission, an independent agency of the United States Government. (7 U.S.C.A. Sections 1-24.) Commodities include agricultural products such as wheat, cotton, fats and oils, and livestock products. (7 U.S.C.A. Section 2.)

Usually investors do not know, or have reason to know, from whom futures interests are bought or sold. Only registered brokers are permitted to conduct the transaction, and trading is accomplished in an open national market which has a large number of individual transactions each day. The commodity futures market is similar to the nationally listed securities market in that those who buy and those who sell commodity futures ordinarily do not know to each other.

ANALYSIS

As a member of a city council, you are required to disclose sources of income of \$250 or more on your statement of economic interests, Form 721, Schedule D. (Sections 87200, 87207.) For purposes of disclosure, income is defined as "... a payment received, including but not limited to any salary, wage, advance, dividend, interest, rent, proceeds from any sale..." (Section 82030(a), emphasis added.) However, there are specific exceptions to the definition of income. Among these are: "Dividends, interest and any other return on a security which is registered with the Securities and Exchange Commission of the United States government." (Section 82030(b)(5).)

In your letter, you point out similarities between the stock market and the commodity futures market. Both types of

investments are traded on national markets which are regulated by agencies of the United States government, and each are registered with their respective regulatory agencies.

These similarities, no matter how appealing, cannot overcome the express wording of the statute. The statutory exception to the income disclosure requirements for securities is limited to those registered with the SEC. It does not include unregistered securities, nor does it include similar types of income-earning investments. Under these circumstances, only a change in the specific language of the statute would permit us to exempt income from the sales of commodity futures from the Act's reporting requirements.^{2/}

The definition of income in the Act does exclude income received "... from any source outside the jurisdiction and not doing business within the jurisdiction..." (Section 82030(a).) Commodity futures are traded on a large and anonymous market. Individual buyers and sellers transact business through a brokerage firm and never come in contact with each other. Furthermore, interests which are traded are not shares in an identifiable business entity, as is usually the case in the stock market, but are "contracts for future delivery" of a specific quantity of an agricultural commodity. It is unlikely that buying and selling interests in contracts for future delivery of an agricultural product will involve an entity which is doing business within the jurisdictional boundaries of the City of Del Mar, California. For that reason, your income from sales of interests in commodity futures is not reportable on your statement of economic interests.

Interest which the brokerage firm pays on the cash balance of your commodity trading account is a different question. It does not matter that the firm has out-of-state headquarters and that it does not have an office in Del Mar. Since the firm is doing business with you in the jurisdiction, the firm is doing business in the jurisdiction.

The interest which the firm pays you, as long as the money is from the firm's own funds, is reportable income if it amounts to \$250 or more during the reporting period. If the firm is simply "passing through" interest earnings which are not reportable

^{2/}We anticipate that the Commission will consider the merits of proposing legislature to exempt registered commodity futures from reporting at its April meeting.

John Gillies
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income, such as interest earned on a demand deposit from a financial institution (Section 82030(b)(4)), then you would not have to disclose the interest income on your statement of economic interest.

I trust that this information is helpful to you. If you have additional questions, I may be contacted at (916) 322-5662.

Sincerely

Diane M. Griffiths
General Counsel



By: Bruce Robeck
Political Reform Consultant

DMG:BR:kmt



John Gillies
Councilman

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March 6, 1987

Fair Political Practices Commission
428 J Street
Sacramento, CA 95814

Gentlemen:

I am preparing to file a Form 721, Statement of Economic interest, for last year. Schedule D requires a list of sources of income, but specifically excludes "Dividends, interest or other return on a security which is registered with the SEC." I assume the reasoning is that stocks and bonds traded nationally, would not exert an undue influence on local decision making.

I receive income from a commodity account with a brokerage firm that has no office within the jurisdiction of Del Mar. The income is comprised of interest on the cash balance, and is paid in New York, as well as capital gains. Although commodities are not registered with the SEC, they bear many relevant similarities to stocks and bonds.

Commodity futures are registered with the Commodity Futures Trading Commission (CFTC). Commodity futures are traded on national markets, primarily in Chicago and New York, as are stocks and bonds. Similarly, prices of commodity futures for wheat, platinum or hog bellies could not possibly be affected by decisions made in Del Mar.

I feel that income from my commodity account should be exempt from reporting on Form 721, just as are stock and bond accounts, but I would like to receive a written opinion from your office.

I must file my forms by March 31, 1987, and would appreciate it if you could respond to my inquiry in the next week or so. I would like to thank you in advance for your assistance.

Sincerely,


John K. Gillies