

October 16, 2014

Gina M, Ratto
Interim General Counsel
California Public Employees' Retirement System
PO Box 942707
Sacramento, CA 94119-2707

**RE: Your Request for Informal Assistance
Our File No. I-14-122**

Dear Ms. Ratto:

This letter responds to your request for advice on behalf of the California Public Employees' Retirement System ("CalPERS") regarding the reporting provisions of Regulation 18950.1 of the Political Reform Act (the "Act").¹ Because you are seeking general guidance, we are providing informal assistance.²

QUESTION

When CalPERS staff travels as a representative of CalPERS to meetings, as described below, and the lodging, meal and transportation costs are paid for by a third party pursuant to a negotiated written agreement between CalPERS and the paying entity, are there any Form 801 or Form 700 reporting obligations?

CONCLUSION

No. A public official is required to report certain gifts and income provided to the official on his or her Form 700. Because CalPERS negotiates the travel, meals, training, etc. under the terms of a contract, it receives the benefit of those terms through the consideration it provides, the same as if it had purchase them. Having, in effect, purchased such benefit, CalPERS then

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).)

provides those benefits to its employee to carry out the duties of the office. The payments do not provide any personal benefit to the employee, so they are not gifts, and Section 82030(b)(2) provides that reimbursement by the agency for travel expenses are not income. The payment received by CalPERS is the equivalent of the up-front travel expenses that are expected to occur as a result of the contract and are therefore treated as a payment made by the agency for travel under Section 82030(b). Even if the payments are not made until after the travel actually occurs, they are incurred pursuant to the prearranged terms of the contract.

Additionally, the provisions of Regulation 18950.1, which establish the Form 801 requirements, are voluntary. No mandatory filing obligations are imposed unless the agency voluntarily chooses to follow the procedures.

FACTS

Your request is a follow-up to the *Ratto* Advice Letter, No. I-14-057. CalPERS is a public pension fund responsible for managing approximately \$296 billion in assets on behalf of more than 1.6 million members. CalPERS contracts with a variety of third parties to enable CalPERS to prudently invest these assets and administer the system.

CalPERS seeks guidance as to whether any gift or income reporting obligations exist when a CalPERS official accepts travel expenses, including lodging, meal and transportation costs, from a third party with whom CalPERS has negotiated a contractual agreement that obligates the third party to pay for such travel expenses. The *Ratto* Advice Letter, No. I-14-057, notes in two places (footnote No. 5 and the sentence beginning at the bottom of page 6) that there has been no gift or income provided with respect to travel payments provided as part of an agreement where equal consideration is provided between the parties. CalPERS seeks confirmation that the following examples of travel expenses, including lodging, meal and transportation costs, provided by a third-party pursuant to a contractual agreement between CalPERS and the third party, are not required to be reported by CalPERS on Form 801 or on a Form 700 filed by the official traveling on CalPERS behalf.

Investment Partnership/Company Travel

CalPERS manages over 60 percent of its assets internally, with the remainder managed by outside investment managers. CalPERS has a fiduciary obligation to manage those managers with whom it entrusts the stewardship of its funds. A large portion of its externally managed assets are invested in private asset classes, such as private equity, real estate, absolute return strategies (hedge funds), and infrastructure, all of which make investments in assets and/or securities.

CalPERS generally invests in these asset classes through investment funds organized as limited partnerships or limited liability companies where CalPERS is often one of many investors (“commingled fund”). In a commingled fund, CalPERS and one or more other limited partners contribute capital to the fund, which is managed by a general partner on behalf of all the limited partners.

At other times, CalPERS is the sole investor in a fund (“separate account”). Separate accounts are also organized as limited partnerships or limited liability companies and managed by a general partner, but with these investments CalPERS’ investment oftentimes amounts to 97% or more of the fund, with the remaining share of the fund borne by the general partner.

Whether investing in a commingled fund or a separate account, these funds are governed by agreements in which the investor often negotiates for certain governance rights allowing the investor to monitor the manager, set the investment parameters of the fund, and participate in certain fund decisions. Many of these governance rights are exercised at meetings of the fund, and a common term in fund agreements requires the fund to pay the reasonable costs of lodging, meals, and transportation for some or all investors attending certain meeting related to the fund. This term is part of an arms-length negotiation between CalPERS, the manager for the fund, and in the case of commingled funds, other limited partners. As a fund expense, the cost of such travel is the responsibility of the investors of the fund, who pay (on a pro-rata share basis) for the expenses of the fund with contributed capital. These expenses are usually accounted for in the calculation of an incentive fees to be earned by the manager. CalPERS’ negotiation of this term may allow travel expenses to count against the manager’s incentive fee where it otherwise would not.

When CalPERS staff travels as a representative of CalPERS to these meetings, and the lodging, meal and transportation costs are paid for by a third party pursuant to a written agreement, are there any Form 801 or Form 700 reporting obligations?

User Conferences and Training

CalPERS also occasionally contracts with third parties for various goods and services. In some of these contracts, CalPERS has negotiated for the right to send one or more employees to attend user conferences and related training provided by the contractor. These conferences and training are designed to enhance CalPERS ability to utilize the underlying goods or services (e.g., specialized training in the use of a piece of software) and their purpose mirrors the intent of knowledge transfer requirements typically found in state contracts. Meals are often included at these conferences or training, and are paid for by the contractor pursuant to the contract.

When CalPERS staff attend these user conferences and training and meals are provided, are there any Form 801 or Form 700 reporting obligations?

ANALYSIS & CONCLUSIONS

Section 82028(a) defines a gift as:

“Gift means, except as provided in subdivision (b),³ any payment that confers a personal benefit on the recipient, to the extent that consideration of equal or greater value is not received and includes a rebate or discount in the price of anything of value unless the rebate or discount is made in the regular course of business to members of the public without regard to official status.”

Section 82030 defines income in part to include:

“a payment received, including . . . any salary, wage, advance, dividend, interest, rent, proceeds from any sale, gift, including any gift of food or beverage, loan, forgiveness, or payment of indebtedness received by the file, reimbursement for expenses, per diem . . .”

Section 87200 identifies certain officials, including “public officials who manage public investments.” Section 87203 requires “[e]very person who holds an office specified in Section 87200” to file annual statements (Form 700) disclosing his [or her] investments, his [or her] interests in real property and his [or her] income.” Income includes gifts.⁴ Additionally, Section 87203 requires each agency to adopt a conflict of interest code that identifies all positions within the agency that engage in the making or participating in the making of governmental decisions and requires persons holding those positions to disclose, also on a Form 700, any interest in real property, investments, and income that may reasonably foreseeably be materially financially affected by any decisions in which the employee makes or participates. These employees, referred to as designated employees or code filers, are required to disclose gifts from sources as identified in the conflict of interest code, while those positions identified in Section 87200, referred to as statutory filers, are required to disclose gifts from any source.

Your questions are directed to these reporting requirements and the alternate reporting requirements adopted last year under Regulation 18950.1. In order to fully understand these requirements, perhaps some background would be helpful.

Last year, in an effort to provide some guidance as to what does, or more accurately does not constitute a personal benefit, the Commission adopted Regulation 18950 et seq. to identify certain payments made in the course of conducting agency business that are not reportable on an employee’s Form 700 when they meet certain specified qualifications, and when the agency identifies these payments and reports them alternatively on a Form 801. The purpose of this disclosure is to resolve any question as to whether or not the employee would be required to report such payments as either gifts or as income.

³ Additional exceptions to the definition of gift are provided in Regulation 18942.

⁴ Section 82030.

The travel regulations under Regulation 18950.1 were the last portion of what began as a complete revision to the Act's gift and travel regulations. The project was conceived, in part, in recognition that certain restrictions had become overly burdensome and had crept into areas that were simply beyond the original intent of the Act. This realization was the impetus for our recognizing the "considerations that argue for caution in imposing more restraints on officials in the name of morality." (See "*The Purity Potlach: An Essay on Conflicts of Interest, American Government, and Moral Escalation*" Bayless Manning, 24 Fed. B. J. 239 1964.)

Regulation 18950.1 does not impose any reporting requirements unless an agency chooses to avail itself of the "safe harbor" it provides for the agency and the agency employee when travel payments are covered by an outside party through an arrangement with the agency in conducting authorized business. Its intent was to give meaning to the Act's full definition of "gift" to counteract previous misinterpretations, and to provide a vehicle for clearly identifying these payments.

In the case of CalPERS, the payments you ask about are payments specifically negotiated through contractual arrangements directly between CalPERS and the individual provider. The purpose is to save CalPERS expenses and thereby increase their profits, a goal consistent with good business practices and not different than any agency negotiating a better deal for itself in a contractual arrangement, whether it be to provide training on a certain product purchased or for other obligations incurred by way of the contract. These payments are incurred by way of the contract, and the payee's obligation to CalPERS. When necessary, CalPERS then chooses the employee who actually makes the travel and he or she does so at the direction of his or her agency to carry out his or her job assignment. These payments are equivalent to payments for reimbursement of expenses under Regulation 82030(b)(2), which are not income.

Accordingly, it is not necessary to apply the safe harbor provisions of Regulation 18950.1 as the payments are already exempt as provided above.

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

Sincerely,

Zackery P. Morazzini
General Counsel

By: William J. Lenkeit
Senior Counsel, Legal Division

WJL:jgl