



STATE OF CALIFORNIA
FAIR POLITICAL PRACTICES COMMISSION
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September 6, 2016

Daniel G. Sodergren, City Attorney
City of Pleasanton
City Attorney's Office
P.O. Box 520
Pleasanton, CA 94566

Re: Your Request for Advice
Our File No. A-16-155

Dear Mr. Sodergren:

This letter responds to your request for advice on behalf of Mayor Jerry Thorne regarding the conflict of interest provisions of the Political Reform Act (the "Act")¹ and Section 1090, *et seq.*² Please note that we do not advise on any other area of law, including Public Contract Code or common law conflicts of interest. We are also 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.

As required by statute, we have forwarded your request to the Attorney General's Office and the Alameda County District Attorney's Office and we did not receive a written response from either entity. (See Section 1097.1(c)(3) and (4).) Finally, we are required to advise you that the following advice is not admissible in a criminal proceeding against any individual other than the requestor. (See Section 1097.1(c)(5).)

QUESTIONS

1. Under the Act, may Mayor Thorne participate in decisions related to the City of Pleasanton's Johnson Drive Economic Development Zone ("JDEDZ") which allow for a club retail business, where he owns stock in Costco Wholesale Corporation ("Costco")?
2. Does Section 1090 prohibit Mayor Thorne from participating in permit and land use applications; and possible development-related agreements between the City and Costco?

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 Government Code Sections 1090 through 1097.5.

CONCLUSIONS

1. No. Mayor Thorne has a prohibited financial interest in the JDEDZ approvals and any permit or land use applications related to Costco. He may not participate in these decisions.

2. Section 1090 does not bar Mayor Thorne's participation, as his financial interest is a non-interest pursuant to Section 1091.5(a)(1).

FACTS

Mayor Thorne has an ownership interest in 24 shares of Costco stock with a value exceeding \$2,000. The shares are in a separately managed account ("SMA"), part of a trust, handled through a financial advisor, and are part of an investment in the Davis Large Cap Value Portfolio.³

Costco is an international club retail business, with a total of 705 warehouses worldwide and 493 in the United States, as of July 2016.⁴ Costco has annual revenues of \$116.2 billion and is a publicly traded company.⁵ Costco's recent "shares outstanding" is calculated at 438 million.⁶ Costco is one of two club retail businesses operating in California, and one of three such businesses in the United States.⁷

The City is considering an Economic Development Zone along Johnson Drive ("JDEDZ") comprising 12 parcels with approximately 40 total acres. The current General Plan designates these parcels as "Business Park." Phase I development within the JDEDZ includes club retail use, a hotel, and other general retail uses. City approvals ("JDEDZ approvals") required to adopt the JDEDZ include the following:

- General Plan Amendment designating the parcels as "Retail/Highway/Service Commercial; Business and Professional Offices;" and
- Rezoning of the project site to "Planned Unit Development-Commercial."

The City states that the JDEDZ approvals refer to "club retail" and do not refer to Costco by name. The City also states that Costco is the only club retail business that has expressed interest in the development. The City's August 2016 report, "Johnson Drive Economic Development Zone, Supplemental Comparative Analysis" ("Report") reflects this.⁸ In this document, City references to

³ The Davis Large Cap Value Portfolio is not a fund as described in Regulation 18237(a); and meets the definition of "investment" under Section 82034.

⁴ <https://en.wikipedia.org/wiki/Costco>

⁵ <http://phx.corporate-ir.net/phoenix.zhtml?c=83830&p=irol-homeprofile>

⁶ <http://finance.yahoo.com/quote/COST/key-statistics?ltr=1>

⁷ https://en.wikipedia.org/wiki/Warehouse_club

⁸ The Report reviews an initiative measure, which has been placed on the upcoming November ballot, to prohibit retail uses (including club retail) 50,000 square feet or greater in the JDEDZ. (Report, Appendix A, page 2.)

“club retail” are accompanied by references to Costco. For example, the Report contains the following statements:

. . . although developers representing club retail [Costco] and hotel enterprises have expressed interest . . .

. . .

The City’s public process for the Zone includes the study of potential General Plan amendments . . . and other actions to allow retail, including a possible Costco club retail . . .

. . .

If Council provides direction to proceed with consideration of the Zone . . . with club retail / Costco will continue to be evaluated by staff . . .

(See Report, page 7; and Appendix A, pages 2 and 6)

The City states it has no record of any agreements between a JDEDZ-related property owner and Costco. City staff has heard that Nearon Enterprises, the current owner of the majority of the parcels in the JDEDZ, may have an option agreement with Costco to locate a Costco warehouse store on Nearon Enterprises property. The City is not a party to any agreements between Nearon Enterprises and Costco. However, the City is currently meeting with Costco in relation to the JDEDZ. The Report states that City staff, Nearon Enterprises, and “potential future business owners (hotels and Costco)” have been in discussions as to funding sources for transportation mitigations. (See Report, page 20.)

The City anticipates that, in the event of the JDEDZ approvals, Costco will apply for a conditional use permit, land entitlements (use permit); and may request development and/or improvement agreements from the City.

ANALYSIS

Political Reform Act

Section 87100 prohibits any public official from making, participating in making, or using his or her official position to influence a governmental decision in which the official has a financial interest. Section 87103 provides that a public official has a “financial interest” in a governmental decision if it is reasonably foreseeable that the decision will have a material financial effect on one or more of the public official’s interests.

Section 87103(a) defines financial interests to include “any business entity in which the public official has a direct or indirect investment worth \$2,000 or more.” (Sections 87103(a).) Mayor Thorne has a financial interest in his investment in Costco.

Foreseeability and Materiality:

To determine if Mayor Thorne will have a prohibited conflict of interest under the Act, we determine if it is reasonably foreseeable that the governmental decisions will have a material financial effect on his financial interest in Costco. (Regulation 18700(d).)

The standard for foreseeability differs depending on whether an interest is explicitly involved in the decisions at issue. (Regulation 18701.) A financial interest that is explicitly involved is presumed to be reasonably foreseeable. (*Id.*) A financial interest is explicitly involved where it is a named party or the subject of a decision. (Regulation 18701(a).) The financial interest is the “subject” of a decision where the government decision “involves the issuance, renewal, approval, denial or revocation of any license, permit, or other entitlement to, or contract with, the financial interest.” (*Id.*)

The applicable standard for materiality is set forth in Regulation 18702.1(a) (in pertinent part):

(a) The reasonably foreseeably financial effect of a government decision on a business entity in which an official has a financial interest . . . is material whenever the business entity:

(1) Initiates the proceeding in which the governmental decision will be made by filing an application, claim, appeal, or request for other government action concerning the business entity;

...

(5) Applies for a permit, license, grant, tax credit, exception, variance, or other entitlement that the official’s agency is authorized to issue;

...

(7) Is otherwise subject to an action taken by the official’s agency, the effect of which is directed solely at the business entity in which the official has an interest.

Preliminary JDEDZ Approvals: General Plan Amendments and Rezoning Decisions

Here, the JDEDZ approvals involve Costco; and Costco is the subject of the decisions. (Regulation 18701(a).) The City’s JDEDZ land use approvals will allow or deny club retail use in this area. Costco is the sole club retail business entity interested and related to the JDEDZ approvals. Costco is therefore explicitly involved and the financial effect is presumed reasonably foreseeable. (*Id.*)

The financial effect is material under Regulation 18702.1(a)(7), in that the JDEDZ approvals are directed solely at Costco in terms of changing the General Plan and zoning to allow a

club retail business.⁹ Under the Act, Mayor Thorne has a financial interest in these decisions, where it is reasonably foreseeable that the decisions will have material financial effect on his financial interest, and must recuse himself pursuant to Regulation 18707.

JDEDZ Costco Permit and Land Use Applications; Agreements between the City and Costco:

Here, with Costco as the applicant, Costco is explicitly involved as the named party of any JDEDZ-related permit and land use application decisions; and the financial effect is presumed reasonably foreseeable. (Regulation 18701(a).)

This financial effect is material under Regulation 18702.1(a)(1) and (a)(5), as Costco is the applicant. Under the Act, the decisions will have a reasonably foreseeable and material financial effect on his financial interest, and Mayor Thorne must recuse himself pursuant to Regulation 18707.

Section 1090

As to Costco's anticipated applications and agreements related to the JDEDZ, you wish to know if Section 1090 prohibits the Mayor's participation.

Section 1090 generally prohibits public officers, while acting in their official capacities, from making contracts in which they are financially interested. The prohibition applies regardless of whether the terms of the contract are fair and equitable to all parties.¹⁰ Section 1090 is concerned with financial interests, other than remote or minimal interests, that prevent public officials from exercising absolute loyalty and undivided allegiance in furthering the best interests of their agencies. A contract that violates Section 1090 is void.¹¹

As a general rule, when Section 1090 is applicable to one member of a governing body of a public entity, the prohibition cannot be avoided by having the interested board member abstain; the entire governing body is precluded from entering into the contract. However, the Legislature has created various statutory exceptions to Section 1090's prohibition where the financial interest involved is deemed a "remote interest," as defined in Section 1091, or a "noninterest," as defined in Section 1091.5.

Where a remote interest is present, the contract may be lawfully executed provided: (1) the officer discloses his or her financial interest in the contract to the public agency; (2) the interest is noted in the public body's official records; and (3) the officer completely abstains from any participation in the making of the contract. (Section 1091.)

⁹ In addition, we note that the JDEDZ decision is inextricably interrelated to the future Costco application because the proposed amendments are a necessary prerequisite to the approval of the Costco's future application and will effectively determine, affirm, nullify, or alter the Costco's effort to build a store at that location. (See Regulation 18706. *Quinn* Advice Letter, No. A-14-106(b).)

¹⁰ *Thomson v. Call* (1985) 38 Cal.3d 633, 646.

¹¹ *Stigall v. Taft* (1962) 58 Cal.2d 565, 569.

We employ a six-step analysis to determine whether an official has a disqualifying conflict of interest under Section 1090. These steps are: (1) does the matter involve a public officer or employee; (2) involve a contract; (3) is the official making or participating in making a contract; (4) does the official have a financial interest in the contract; (5) does a remote or non-interest exception apply.

Steps one through four are not at issue here. We focus on whether the Mayor's Costco shares fall under a remote or non-interest exception.

Step Five: Does either a remote interest or a non-interest exception apply?

Section 1091.5, subdivisions (a), provides that a public officer shall not be deemed to be interested in a contract if his or her interest meets the following criteria:

(1) The ownership of less than 3 percent of the shares of a corporation for profit, provided that the total annual income to him or her from dividends, including the value of stock dividends, from the corporation does not exceed 5 percent of his or her total annual income, and any other payments made to him or her by the corporation do not exceed 5 percent of his or her total annual income.

Mayor Thorne owns 24 shares of Costco, which meets the less than 3 percent threshold. If the total annual income to Mayor Thorne from Costco dividends, or other payments, does not exceed 5 percent of his total annual income, then his financial interest in the Costco stock is a non-interest under Section 1091.5(1).

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

Sincerely,

Hyla P. Wagner
General Counsel

/s/

By: L. Karen Harrison
Counsel, Legal Division

LKH: jgl