



## FAIR POLITICAL PRACTICES COMMISSION

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May 24, 2011

John T. Unger, Senior Vice President  
and General Counsel  
600 Travis, Suite 5800  
Houston, Texas 77002

Re: Your Request for Advice  
**Our file No. A-11-081**

Dear Mr. Unger:

This letter responds to your request for advice regarding the lobbying provisions of the Political Reform Act (the "Act").<sup>1</sup> The Fair Political Practices Commission ("the Commission") will not advise with respect to past conduct. (Regulation 18329(b)(8)(A).) Therefore, nothing in this letter should be construed to evaluate any conduct that may have already taken place.

### QUESTION

Does the Act prohibit a placement agent from accepting compensation from an external manager that was based on a percentage of the amount that the external manager will be managing for a state public retirement system?

### CONCLUSION

Yes. You have described a contingency fee arrangement that the Act expressly prohibits in Section 86205(f).

### FACTS

You represent SMH Capital Advisors, Inc. ("SMHCA"), a Texas Corporation that is a registered investment advisor providing advice to, among others, public pension and retirement boards. SMHCA has engaged an affiliated entity, Sanders Morris Harris, Inc. (SMHI), a registered broker dealer and investment advisor, to act as a solicitor and locate individuals and institutions interested in obtained SMHCA's services. Both of these entities are wholly-owned subsidiaries of Sanders Morris Harris Group, Inc.

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<sup>1</sup> 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.

SMHI intends to solicit California public retirement systems on behalf of SMHCA. Typically such arrangements between SMHCA and a public retirement system involves a fee based on the amount of assets under management. SMHCA charges a percentage of the assets under management on an annual basis. SMHCA (as external manager) then has an arrangement with SMHI (as placement agent) to pay a portion of the management fee from the California public retirement system. Of that amount, SMHI pays its employee who was responsible for bringing in the client (the public retirement system, in this case). SMHCA pays neither SMHI nor its employees a flat fee for their solicitation services.

As we understand your facts, SMHI would register as a lobbying firm using Form 601 (listing SMHCA as a lobbyist employer). The solicitors would register as lobbyists, as you indicated. SMHCA would file a Form 602 as a lobbyist employer.

### ANALYSIS

The legislature passed, and the governor signed, Assembly Bill 1743 (“the Bill”), a series of laws adding to the Government Code. The Bill makes a key change to the Act that includes “placement agent” in the Act’s definition of “lobbyist.” The rules and regulations regarding lobbyists therefore now apply to placement agents, per the Bill. The Bill codifies the policy of requiring certain disclosures of individuals who will solicit the business of California Public Retirement Systems.

The Bill makes several amendments and additions to the Act to effectuate the overall goal of including placement agents under the definition of lobbyists and providing Californians with more information about their public retirement systems. Specifically, the Bill:

- Amends the definition of “administrative action” to include decisions by a state agency to enter into a contract to invest state public retirement system assets on behalf of a state public retirement system. (Section 82002(a)(2).)
- Adds a definition of “external manager” as either “a person who is seeking to be, or is, retained by a state public retirement system in California to manage a portfolio of securities or other assets for compensation” or “a person who is engaged, or proposes to be engaged in the business of investing, reinvesting, owning, holding, or trading securities to a state public retirement system in California.” (Section 82025.3.)
- Adds “placement agent” to the definition of “lobbyist.” (Section 82039(a)(2).)

Section 86205(f) states that “no lobbyists or lobbying firm may accept or agree to accept any payment in any way contingent on the defeat, enactment, or outcome of any proposed legislative or administrative action.”<sup>2</sup> There are no exceptions to this ban on contingency fees. The contingency fee ban applies to lobbyists and lobbying firms – that is, SMHI and its lobbyist

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<sup>2</sup> As stated above, administrative action includes entering into a contract to invest state retirement system assets on behalf of a California public retirement system.

employees may not accept any payment that is tied to the success of the lobbyists at a California public retirement system.

To the extent that any lobbying firm or lobbyist is paid on a contingency-basis, the Act prohibits the practice. As of the passage of AB 1743, contingency fees are banned for placement agents (including lobbyist employers). SMHI could not receive any payment that was made on a contingency basis, nor could its employees who gained the business of a California public retirement system. We realize that this is a change in the way these contracts have historically been structured. To comply with the law, the contract and fee arrangement must be in place before the lobbyist approaches the public retirement system and the amount cannot be contingent on the lobbyist's success.

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

Sincerely,

John W. Wallace  
Assistant General Counsel

A handwritten signature in black ink, appearing to read "Heather M. Rowan", with a long horizontal flourish extending to the right.

By: Heather M. Rowan  
Counsel, Legal Division

HMR:jgl