

September 22, 2020, Agenda - Open Meeting Matter

To: The Board

From: Christopher M. Hammer *cmh*

Date: July 20, 2020

Re: Proposed Amendments to Board Rules § 1-04: Investments in Publicly Traded Securities

As part of its review of the Board's rules, practices, and advisory opinions pursuant to City Charter § 2603(c)(4),¹ Staff brings to the Board proposed amendments to Board Rules § 1-04. Board Rules § 1-04 defines "a firm whose shares are publicly traded" for purposes of the provisions of Chapter 68 relating to a public servant's ownership interest. Staff proposes that the Board amend Board Rules § 1-04 to address three additional types of ownership interests that have been the subject of advisory opinions: (1) mutual funds; (2) investments held in individual retirement accounts ("IRAs"); and (3) investments in bonds issued by government and quasi-government entities.

The proposed amendments are discussed in greater detail in the draft Notice of Public Hearing and Opportunity to Comment (**Exhibit 1**), but Staff here highlights the proposed amendments regarding mutual funds. The term "mutual fund" is not defined in Chapter 68 or in the Board's advisory opinions; in researching how to define this term for purposes of Chapter 68, Staff found the regulations of federal government employees' ownership of mutual funds to be instructive. These regulations, relevant provisions of which are attached as **Exhibit 2**, distinguish "diversified" mutual funds from "sector" mutual funds, the latter of which "concentrate[] ...

¹ City Charter § 2603(c)(4) requires the Board to "initiate a rulemaking to adopt, as interpretive of the provisions of [Chapter 68] any advisory opinion of the board issued after the year 1990 and before [October 27, 2018] which the board determines to be consistent with and have interpretive value in construing the provisions of this chapter and which either (a) establishes a test, standard, or criterion; or (b) is anticipated by the board to be the subject of future advisory opinion requests from multiple persons."

investments in an industry, business, single country other than the United States, or bonds of a single State within the United States.” 5 C.F.R. § 2640.102(q) (defining “sector mutual funds”). A federal employee’s ownership of diversified mutual funds does not pose a conflict of interest, while ownership of sector mutual funds would require the federal employee to examine the contents of the mutual fund’s portfolio before determining whether a conflict exists because federal employees may use sector funds to concentrate their investments in a firm affected by their government work or decisions. See 5 C.F.R. § 2640.201(a) (involving diversified mutual funds and § 2604.201(b) (involving sector mutual funds). Staff thus proposes that the Board adopt a similar distinction to exclude diversified mutual funds from the definition of “ownership interests” in Charter § 2601(16).

The proposed amendments have been informally reviewed by the New York City Law Department; with the Board’s approval, Staff will formally submit these proposed amendments to the Law Department and the Mayor’s Office of Operations, as required by the City Administrative Procedure Act. See Charter Section 1043(d).

1 **New York City Conflicts of Interest Board**

2 **Notice of Public Hearing and Opportunity to Comment on Proposed Rules Regarding**
3 **Investments in Publicly Traded Securities**

4 **What are we proposing?** The Conflicts of Interest Board proposes to amend its rules regarding
5 investments in publicly traded securities.

6 **When and where is the Hearing?** The Conflicts of Interest Board will hold a public hearing on
7 the proposed rule. The public hearing will take place by video conference at [] on [] and is
8 accessible by:

- 9 • **Internet Video and Audio.** To access the hearing by Zoom, use the following URL: [].
10
11 • **Telephone.** To access the hearing by telephone, dial []. When prompted, use the following
12 access code [] and password [].

13 **How do I comment on the proposed rules?** Anyone can comment on the proposed rules by:

- 14 • **Website.** You can submit comments to the Conflicts of Interest Board through the NYC
15 rules website at <http://rules.cityofnewyork.us>.
16
17 • **Email.** You can email comments to Rules@COIB.nyc.gov.
18
19 • **By Speaking at the Hearing.** Anyone who wants to comment on the proposed rule at the
20 public hearing may speak for up to three minutes. Please access the public hearing by
21 Internet Video and Audio or by Telephone using the instructions above. It is
22 recommended, but not required, that commenters sign up prior to the hearing by contacting
the Conflicts of Interest Board by phone at (212) 437-0730 or by email at
lee@coib.nyc.gov.

23 **Is there a deadline to submit comments?** Yes, you must submit written comments by [].

24 **This hearing has the following accessibility option(s) available:** The Zoom platform
25 accommodates screen reader software. Simultaneous transcription or a sign-language interpreter
26 are available upon request.

27 **Do you need assistance to participate in the hearing?** You must tell the Conflicts of Interest
28 Board if you need a reasonable accommodation of a disability at the hearing, including if you need
29 a sign language interpreter or simultaneous transcription. You can advise us by email at
30 lee@coib.nyc.gov or by telephone at (212) 437-0730. You must tell us by [].

31 **Can I review the comments made on the proposed rules?** You can review the comments made
32 online on the proposed rules by going to the website at <http://rules.cityofnewyork.us/>. Copies of
33 all comments submitted online, copies of all written comments, and a summary of oral comments
34 concerning the proposed rule will be available to the public on the Conflicts of Interest Board's

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1 website ([https://www1.nyc.gov/site/coib/public-documents/open-meetings-and-public-](https://www1.nyc.gov/site/coib/public-documents/open-meetings-and-public-hearings.page)
2 [hearings.page](https://www1.nyc.gov/site/coib/public-documents/open-meetings-and-public-hearings.page)) as soon as practicable.

3 **What authorizes the Conflicts of Interest Board to make this rule?** Sections 1043, 2603(a),
4 and 2603(c)(4) of the City Charter authorize the Conflicts of Interest Board to make this proposed
5 rule. This proposed rule was not included in the Conflicts of Interest Board’s regulatory agenda
6 for this Fiscal Year because it was not anticipated to be a subject of rulemaking at that time.

7 **Where can I find the Conflicts of Interest Board’s rules?** The Conflicts of Interest Board’s
8 rules are in Title 53 of the Rules of the City of New York.

9 **What rules govern the rulemaking process?** The Conflicts of Interest Board must meet the
10 requirements of Section 1043 of the City Charter when creating or changing rules. This notice is
11 made according to the requirements of Section 1043 of the City Charter.

12 **Statement of Basis and Purpose of the Proposed Rule**

13 City Charter § 2604(a)(1)(b) prohibits a regular employee of the City from having an
14 ownership interest in a firm “engaged in business dealings with the city, except if such interest is
15 in a firm whose shares are publicly traded, as defined by rule of the board.” The Board accordingly
16 adopted Board Rules § 1-04 in 1990, defining a publicly traded firm as one that “offers or sells its
17 shares to the public and is listed and registered with the Securities and Exchange Commission for
18 public trading on national securities exchanges or over-the-counter markets.”

19 In the intervening thirty years, the Board has advised many public servants about the impact
20 of the conflicts of interest provisions of Chapter 68 on their ownership interests in publicly traded
21 securities, including six advisory opinions: A.O. Nos. 1994-10, 1994-13, 2002-1, 2007-4, 2009-7,
22 and 2012-1. The proposed amendments to Board Rules § 1-04 would retain the definition of
23 “publicly traded firm” as paragraph (a) and add new paragraphs (b), (c), and (d) dealing,
24 respectively, with the ownership of mutual funds, investments held in individual retirement
25 accounts (“IRAs”), and the ownership of bonds.

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1 1. *Ownership of Mutual Funds*

2 City Charter § 2601(16) excludes from the definition of ownership interest a mutual fund
3 comprised of investments that “are not controlled by the public servant [or] the public servant’s
4 spouse, domestic partner, or unemancipated child,” but does not define “mutual fund.” Proposed
5 Board Rules § 1-04(b) would define “mutual fund” for the purposes of this exclusion to include “a
6 management company, exchange-traded fund, or unit investment trust registered with the
7 Securities and Exchange Commission, provided that the company, fund, or trust does not have a
8 stated policy of concentrating its investments in any particular business sector,” such as
9 pharmaceuticals or financial services. This proposed definition would mirror the distinction
10 contained in the rule for federal employees. See 5 Code of Federal Regulations § 2640.201. Thus,
11 as the proposed rule indicates, investments in diversified funds are not ownership interests for
12 purposes of Chapter 68, while in contrast investments in sector funds are treated like any other
13 ownership interest under Chapter 68.

14 2. *Investments Held in IRAs*

15 City Charter § 2601(16) establishes a definition of “ownership interest” in a firm but
16 excludes “interests held in any pension plan, deferred compensation plan or mutual fund, the
17 investments of which are not controlled by the public servant, the public servant’s spouse,
18 domestic partner, or unemancipated child.” For purposes of this definition, proposed Board Rules
19 § 1-04(c) would treat investments contained in an IRA, Roth IRA, Simplified Employee Pension
20 IRA, or Keogh plan just like any other investments. Thus, for example, shares in a publicly-traded
21 firm that are chosen by the public servant and held in their IRA are considered “ownership
22 interests” within the meaning of City Charter § 2601(16).

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1 3. *Ownership of Bonds*

2 Proposed Board Rules § 1-04(d)(1) would codify the general advice the Board provided in
3 A.O. No. 1994-10, and reiterated in A.O. Nos. 1994-13, 2002-1, and 2009-7, that a public servant’s
4 ownership of bonds issued by public entities is not a prohibited ownership interest in a “firm.”
5 Specifically, City Charter § 2601(11) and Board Rules § 1-08, which codified A.O. No. 1994-10
6 pursuant to City Charter § 2603(c)(4), exclude certain public and quasi-public entities, including
7 the City of New York and its agencies, from the definition of “firm.” Nevertheless, the Board
8 recognized in A.O. 2009-7 that a small group of public servants has personal and substantial
9 responsibility in the issuance and management of City debt obligations. For these public servants,
10 the purchase, ownership, or sale of City-issued bonds implicates City Charter § 2604(b)(2)
11 prohibiting private interests that conflict with their official City duties, § 2604(b)(3) prohibiting a
12 public servant’s use of their position to benefit themselves or any of their “associated” persons or
13 firms, and § 2604(b)(4) prohibiting the use or disclosure of confidential information obtained as
14 part of their City job. Proposed Board Rules § 1-04(d)(2) would codify this holding.

15
16 New material is underlined. [Deleted material is bracketed.]

17 **§ 1-04 Investments in Publicly Traded Securities [Definition of a Firm Whose Shares are**
18 **Publicly Traded].**

19 **(a) Definition of a Firm Whose Shares are Publicly Traded.** For purposes of Charter §
20 2604(a)(1)(b), “a firm whose shares are publicly traded” means a firm [which] that offers
21 or sells its shares to the public and is listed and registered with the Securities and Exchange
22 Commission for public trading on national securities exchanges or over-the-counter
23 markets.

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1 **(b) Mutual Funds.** For purposes of the definition of “ownership interest” in Charter §
2 2601(16), the term “mutual fund” means a management company, exchange-traded fund,
3 or unit investment trust registered with the Securities and Exchange Commission, provided
4 that the company, fund, or trust does not have a stated policy of concentrating its
5 investments in any particular business sector. Accordingly, investments in companies,
6 funds, or trusts that do not have a stated policy of concentrating its investments in any
7 particular business sector are not “ownership interests,” while investments in companies,
8 funds, or trusts that have a stated policy of concentrating its investments in any particular
9 business sector are ownership interests.

10 **(c) Investments held in IRAs.** For purposes of Charter § 2601(16), an “ownership interest”
11 includes investments in firms held in an individual retirement account (“IRA”), Roth IRA,
12 Simplified Employee Pension IRA, or Keogh plan, provided that the investment is not
13 otherwise excluded from the definition of “ownership interest.”

14 **(d) Public Debt Obligations.**

15 (1) Except as provided in paragraph (d)(2), for purposes of Charter § 2604(a)(1) and §
16 2601(11), a public servant is not prohibited from owning debt obligations issued by the
17 City or “other similar entities” as defined in Board Rules § 1-08.

18 (2) For purposes of Charter § 2604(b)(2), § 2604(b)(3), and § 2604(b)(4), a public servant,
19 prior to becoming personally and substantially involved in the issuance and/or
20 management of City debt obligations must divest their ownership in such debt
21 obligations, and for the duration of such involvement may not buy or hold such City
22 debt obligations on behalf of the public servant or an associated person or firm. For
23 purposes of Charter § 2604(b)(3), a public servant who is personally and substantially

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1 involved in the issuance and/or management of City debt obligations may not trade, or
2 participate in trading, City debt obligations on behalf of, or for the account of, an
3 associated person or firm.

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Federal Regulations Involving Ownership of Mutual Funds

5 CFR § 2640.102 – Definitions

- (a) **Diversified** means that the fund, trust or plan does not have a stated policy of concentrating its investments in any industry, business, single country other than the United States, or bonds of a single State within the United States and, in the case of an employee benefit plan, means that the plan's trustee has a written policy of varying plan investments.

Note to paragraph (a): A mutual fund is diversified for purposes of this part if it does not have a policy of concentrating its investments in an industry, business, country other than the United States, or single State within the United States. Whether a mutual fund meets this standard may be determined by checking the fund's prospectus or by calling a broker or the manager of the fund. An employee benefit plan is diversified if the plan manager has a written policy of varying assets. This policy might be found in materials describing the plan or may be obtained in a written statement from the plan manager. It is important to note that a mutual fund or employee benefit plan that is diversified for purposes of this part may not necessarily be an excepted investment fund (EIF) for purposes of reporting financial interests pursuant to 5 CFR 2634.310(c) and 2634.907(i)(3). In some cases, an employee may have to report the underlying assets of a fund or plan on his financial disclosure statement even though an exemption set forth in this part would permit the employee to participate in a matter affecting the underlying assets of the fund or plan. Conversely, there may be situations in which no exemption in this part is applicable to the assets of a fund or plan which is properly reported as an EIF on the employee's financial disclosure statement.

* * *

- (k) **Mutual fund** means an entity which is registered as a management company under the Investment Company Act of 1940, as amended (15 U.S.C. 80a-1 et seq.). For purposes of this part, the term mutual fund includes open-end and closed-end mutual funds and registered money market funds.
- (q) **Sector mutual fund or sector unit investment trust** means a mutual fund or unit investment trust that concentrates its investments in an industry, business, single country other than the United States, or bonds of a single State within the United States.

5 CFR § 2640.201 – Exemptions for Interests in Mutual Funds, Unit Investment Trusts, and Employee Benefit Plans

- (a) **Diversified mutual funds and unit investment trusts.** An employee may participate in any particular matter affecting one or more holdings of a diversified mutual fund or a diversified unit investment trust where the disqualifying financial interest in the matter arises because of the ownership of an interest in the fund or trust.

Example 1 to paragraph (a): An employee owns shares worth \$100,000 in several mutual funds whose portfolios contain stock in a small computer company. Each mutual fund prospectus describes the fund as a “management company,” but does not characterize the fund as having a policy of concentrating its investments in any particular industry, business, single country (other than the U.S.) or bonds of a single State. The employee may participate in agency matters affecting the computer company.

Example 2 to paragraph (a): A nonsupervisory employee of the Department of Energy owns shares valued at \$75,000 in a mutual fund that expressly concentrates its holdings in the stock of utility companies. The employee may not rely on the exemption in paragraph (a) of this section to act in matters affecting a utility company whose stock is a part of the mutual fund’s portfolio because the fund is not a diversified fund as defined in § 2640.102(a). The employee may, however, seek an individual waiver under 18 U.S.C. 208(b)(1) permitting him to act.

(b) Sector mutual funds.

- (1) An employee may participate in any particular matter affecting one or more holdings of a sector mutual fund or a sector unit investment trust where the affected holding is not invested in the sector in which the fund or trust concentrates, and where the disqualifying financial interest in the matter arises because of ownership of an interest in the fund or unit investment trust.
- (2)(i) An employee may participate in a particular matter affecting one or more holdings of a sector mutual fund or a sector unit investment trust where the disqualifying financial interest in the matter arises because of ownership of an interest in the fund or the unit investment trust and the aggregate market value of interests in any sector fund or funds and any sector unit investment trust or trusts does not exceed \$50,000.
- (ii) For purposes of calculating the \$50,000 de minimis amount in paragraph (b)(2)(i) of this section, an employee must aggregate the market value of all sector mutual funds and sector unit investment trusts in which he has a disqualifying financial interest and that concentrate in the same sector and have one or more holdings that may be affected by the particular matter.

Example 1 to paragraph (b): An employee of the Federal Reserve owns shares in the mutual fund described in the preceding example. In addition to holdings in utility companies, the mutual fund contains stock in certain regional banks and bank holding companies whose financial interests would be affected by an investigation in which the Federal Reserve employee would participate. The employee is not disqualified from participating in the investigation because the banks that would be affected are not part of the sector in which the fund concentrates.

Example 2 to paragraph (b): A health scientist administrator employed in the Public Health Service at the Department of Health and Human Services is assigned to serve on a Departmentwide task force that will recommend changes in how Medicare reimbursements will be made to health care providers. The employee owns \$35,000 worth of shares in the XYZ Health Sciences Fund, a sector mutual fund invested primarily in health-related companies such as pharmaceuticals, developers of medical instruments and devices, managed care health organizations, and acute care hospitals. The health scientist administrator may participate in the recommendations.

Example 3 to paragraph (b): The spouse of the employee in the previous Example owns \$40,000 worth of shares in ABC Specialized Portfolios: Healthcare, a sector mutual fund that also concentrates its investments in health-related companies. The two funds focus on the same sector and both contain holdings that may be affected by the particular matter. Because the aggregated value of the two funds exceeds \$50,000, the employee may not rely on the exemption.