



STATE OF CONNECTICUT

STATE ETHICS COMMISSION

ADVISORY OPINION NO. 87-16

Public Member of the Investment Advisory Council

The advice of the Ethics Commission has been sought regarding the appointment of a person to the Investment Advisory Council as a public member and its chairperson.

The nominee's son is the president of an investment firm. The firm manages portfolios in a dividend recapture strategy, with the objective of providing low volatility of asset values and return, with returns significantly above those available in more traditional short-term assets. The Investment Division, Office of the Treasurer, might hire the firm, or another company of a similar nature, to provide management services for a portion of the investments for which the Treasurer is responsible. The father has no business relationship with, or financial interest in, his son's firm.

The Commission has also been asked whether it would be proper for the Council Chairman, if appointed, to promote the dividend recapture strategy, in view of the fact that his son's firm manages portfolios using that particular strategy.

One of the Treasurer's responsibilities is to invest the funds of a number of the State's trust funds. Section 3-13d, General Statutes. The trust funds are invested in several investment funds created by the Treasurer. Section 3-31b, General Statutes. The Treasurer retains investment firms, such as the nominee's son's, to assist him in managing the investment funds which serve as the investment media for the various trust funds of which he is the trustee. Subsection 3-13a(b), General Statutes.

To give the Treasurer advice and counsel in investment decisions the Investment Advisory Council has been established. Section 3-13b, General Statutes. Its members, who serve four-year terms, include (1) two State officials ex officio, (2) five representatives of persons for whose

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retirement funds the Treasurer is trustee, and (3) five public members, all of whom shall be experienced in matters relating to investments. Subsection 3-13b(a), General Statutes. Four of the public members are appointed by the legislative leadership, one by the Governor. Id. The Governor designates one member to be chairperson. Subsection 3-13b(b), General Statutes. Members receive no compensation for their services, but are reimbursed for their necessary expenses. Id.

The Council reviews all investments by the Treasurer, and recommends investment policies and strategies, consistent with the laws governing the particular investment. Subsection 3-13b(c), General Statutes. When the Council believes it in the best interest of the State, the Governor may direct the Treasurer to change any investment he has made. Id. Annually the Council examines the State's security investments and reports the value of the investments in the custody of the Treasurer to the Governor, the General Assembly, and the beneficiaries of the trust funds of which the Treasurer is trustee. Id.

The only conflict of interests provision specifically applicable to a member of the Investment Advisory Council prohibits a public member, or his business organization or affiliate, from directly or indirectly contracting with or providing any services for the investment of trust funds of the State during his time of service on the Council and for one year thereafter. Subsection 3-13b(a), General Statutes.

It does not appear that the Investment Advisory Council, its chairman, or any member has authority to expend public funds or exercise the power of the State. Members advise and make recommendations to the Treasurer and the Governor. They examine, and appraise the value of, the State's security investments annually, but the report of their evaluation appears to be used for information. It has no direct legal consequence. They receive no compensation, merely reimbursement for necessary expenses incurred in Council duty. Therefore they are members of an advisory board (subsection 1-79(g), General Statutes), not public officials (subsection 1-79(j), General Statutes). Unpaid for their services to the State, they are not State employees (subsection 1-79(k), General Statutes). Neither public officials nor State employees, they are not subject to the Code of Ethics, Chapter 10, Part I, General Statutes.

Consequently, insofar as the Code of Ethics is concerned, if the person were appointed Council Chairman he could advocate a dividend capture strategy, even though his son's investment firm utilizes the strategy, and the Investment Division, Office

of the Treasurer, could engage the services of the son's company.

While observance of the Code of Ethics is mandatory only for those subject to it, the Code also establishes a standard of ethical conduct against which the actions of others can be measured. Actions in the government arena by persons not subject to the Code can affect the confidence of the public in the integrity of government operations. They can also foment undesirable publicity when persons and firms desirous of supplying goods or services to the State lose out to persons or firms which seem to have improper support from within State government.

Assuming utilization of a dividend capture strategy is not unique to the son's firm, the nominee, if made Council Chairman, should be allowed to promote it providing, based on his experience in matters relating to investments, he thinks it desirable for some State investments. On the other hand, if his son's firm were the only one using the strategy (it is understood the strategy is more common than that), there would be questions regarding his motivation for advocating it.

If a Council member were subject to the Code of Ethics and the issue of the Investment Division retaining services which his son's firm was eligible, qualified, and willing to provide came before him as a Council member, he would have to abstain from any action on the matter, in compliance with section 1-86, General Statutes, in order to avoid a violation of subsection 1-84(c), General Statutes. The latter forbids use of State position, or confidential inside information gained in it, for the financial gain of one's son, among others. While having a son in the investment business should not disqualify one from service on the Council, it would avoid casting doubt on the objectivity of Council action if the Council member were to take no part at all should the Council recommend to the Investment Division, Office of the Treasurer what firm or firms like his son's should be hired, should the Council be consulted with regard to investment firms to be hired, etc.

By order of the Commission,



William A. Elrick
Chairman

Dated DEC. 8, 1987

