PARTNERSHIP FOR PUBLIC SERVICE

Presidential Appointments Vetting Guide

PRECEDENTS, AUTHORITIES AND CASE STUDIES

Partnership for Public Service

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INTRODUCTION

On Jan. 20, 2017, the 45th president of the United States will be inaugurated and become the chief executive of one of the largest and most complex organizations in the world, an enterprise with more than two million civilian employees and a budget of nearly $4 trillion.

Of all the early decisions the new president must make, few will be as important as determining who will have leadership roles in the departments and agencies. The next president will need to fill approximately 4,000 politically-appointed positions, including more than 1,000 top leadership and management jobs that will require Senate confirmation.

Individuals being considered for politically-appointed positions will have to be extensively vetted by the president-elect's legal team and later by the new administration. The attorneys look for potential red flags—financial, ethical or personal issues that might disqualify potential appointees from serving in an administration or require some action to eliminate potential conflicts of interest.

Historically, these vetting teams have operated in a vacuum with very little institutional knowledge of how previous administrations have approached the kinds of problems that emerge during the appointment process.

The law firms of Steptoe & Johnson and Allen & Overy compiled this collection of precedents, authorities and case studies to serve as a reference point for the next president's appointments team as it develops its own rules and guidelines, and as it deals with complex and unexpected issues that inevitably will arise. The guide also can be used by attorneys for potential nominees to better understand the types of issues that should be considered.

This guide represents an important contribution to the work of the Center for Presidential Transition, which is providing guidance to presidential candidates on how to set up and execute a transition, and is working with the outgoing administration to encourage a smooth transfer of power.

Sincerely,

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President and CEO
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I. FINANCIAL DISCLOSURE

Potential financial conflicts of interest, generally governed by 18 USC § 208, are addressed by both disclosure and conflict of interest restrictions. Disclosure of financial interests on OGE Form 278 (and OGE Form 450 for nonpublic filers), is governed by statute, OGE regulations, OGE guidance and informal practice. Disclosure rules are intended to help identify potential conflicts of interest, but are not limited to that goal. Increasingly complex financial products held in the portfolios of filers create a need for different approaches to both disclosure and conflict of interest analysis.

A. Financial Interests and Income: Selected Categories

1.1 Pooled Investment Vehicles

Ownership of passive interests in private equity funds, hedge funds, venture capital funds and other collectively owned investment vehicles, all of which fall into the regulatory category of "pooled investment vehicles," raise significant disclosure and other issues for filers.

1.1.1 Bush II Administration Precedent

If a pooled investment fund does not qualify as an "excepted investment fund" (EIF), the filer must disclose the underlying holdings. A pooled investment fund may qualify as an "excepted investment fund" if: (1) the fund is widely held, typically meaning more than 100 investors; (2) investors do not control and cannot control the financial interests held by the fund; and (3) the fund is publicly available.

Endnote Convention for 278 Disclosures of Portfolio Holdings.

Because of the difficulty of providing information regarding underlying portfolio investments and underlying tiers of investment funds for pooled investment vehicles, convention developed to include relevant information in endnotes attached to the 278 (with references to the endnote on the appropriate line on Schedule A of the 278). The endnote convention was accepted by OGE and the White House beginning in January 2003 and became widely used shortly thereafter, but has never been reflected in formal advisory guidance.

Authority

Cusick, R. I., U.S. Office of Government Ethics - DO-08-022: Financial Disclosure Requirements for Pooled Investment Funds. (July 22, 2008). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20 Documents/AD54F07936C7D6FA85257E96005FBE9B/$FILE/DO-08-022.pdf

1.1.2 **Current Practice Precedent**

Disclosure of underlying assets of pooled investment vehicles continues to depend upon whether the fund qualifies as an EIF. OGE's liberalization of certain tests for qualification as an EIF reduces disclosure requirements but does not affect conflict of interest analysis.

Endnote Convention.

Endnote convention begun in the prior administration for underlying portfolio investments continues to be accepted practice except for disclosure under the Financial Disclosure Management (FDM) online platform. The FDM system does not readily permit endnote attachments and the State Department determined that endnotes could not be used with 278s under State Department jurisdiction. FDM requires the filer to include some information about underlying portfolio investments in a "comment" field. The endnote convention is used to describe intermediate partnership entities (e.g., in a "fund of fund" structure) and has been adapted to a variety of special investment fund disclosures. The new online filing system, Integrity, has its own endnote convention.

Authority

Cusick, R. I., U.S. Office of Government Ethics - DO-08-022: Financial Disclosure Requirements for Pooled Investment Funds. (July 22, 2008). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20 Documents/AD54F07936C7D6FA85257E96005FBE9B/$FILE/DO-08-022.pdf

Precedent: EIFs for Disclosure Purposes.

Beginning in 2009, OGE adopted a more "expansive" definition of EIF. This made it easier for private equity funds and other investment funds to qualify for EIF status. Thus, for example, with respect to the "widely held" test for qualification, OGE adopted the convention that all "ultimate beneficial owners" of interests in a pooled investment vehicle would be counted for purposes of meeting the 100 investors test. As a result, many investment funds with "institutional" (e.g., pension plan) direct investors, or multi-tiered investment fund structures, would meet the widely held test for qualification. In addition, OGE adopted a more expansive interpretation of the "publicly held or available" test for qualification. Under this interpretation, as long as a member of the public who met the objective qualification tests (e.g., qualified investor and net worth test, which are common to many private equity and other investment funds) could invest in the fund or purchase an interest in the fund, this test for qualification as an EIF would be met. As a result of these interpretive changes, many investment funds that previously did not qualify for EIF status began to qualify. Current standards for EIF qualification are now published on the OGE website.

Authority
Office of Government Ethics - Excepted Investment Fund. (2015). Retrieved from https://www2.oge.gov/Web/oge.nsf/Resources/Excepted+Investment+Fund

1.2 Discretionary Trusts

1.2.1 Bush II Administration

Precedent: Discretionary Trust Exemption.
For the first time, in 2008 OGE considered the disclosure and conflict implications of so-called discretionary trusts. In issuing its August 2008 memorandum, DAEOgram 08-024, exempting discretionary trusts from disclosure (as well as conflict of interest) concerns, OGE recognized the unique status of beneficial interests in irrevocable trusts as to which the beneficiary had no legal right to compel a distribution in favor of the beneficiary. The OGE memorandum implicitly recognized that state trust law determined the legal rights of beneficiaries, raising the question of whether a state trust law opinion or other legal authority must be cited to support discretionary trust status of a particular irrevocable trust. In a few cases, changes by filers to the distribution provisions of the particular trust to cause the trust to be discretionary within the meaning of the memorandum were respected. However, the memorandum restricted the application of the discretionary trust rule to those in which the filer was not the settlor of the trust, thus limiting the scope of the rule. Under the 2008 memorandum, the filer must report holdings of a discretionary trust if the filer, filer's spouse or filer's dependent child received income from the discretionary trust during the reporting period. This was later modified.

Authority
Cusick, R. I., U.S. Office of Government Ethics - DO-08-024: Discretionary Trusts.
(August 6, 2008). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20
Documents/94CDD37DC8B2FF5F85257E96005FBE9C/$FILE/DO-08-024.pdf

1.2.2 Current Practice
Precedent: Expansion of Discretionary Trust Exemption.
Filer does not have to report holdings of discretionary trusts even if a payment was received from the discretionary trust during the relevant reporting period. Filers must still report any income received from the discretionary trust to the filer, or the filer's spouse or dependent child.

Authority
Shaub, Jr., W. M., U.S. Office of Government Ethics - LA-13-04: Reporting Requirements for
Discretionary Trusts. (April 9, 2013). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20
Documents/84366EACA265457E85257E96005FBEFC/$FILE/LA-13-04.pdf?open

1.3 Partnership Income

1.3.1 Bush II Administration

Precedent:
During the George W. Bush administration, the convention was developed to report cash distributions, rather than taxable income, for the reporting period. In general, this approach to "cash distributions" permitted filers to provide some more accurate information by denoting "distribution" with the exact amount entered in the "other income" block.

1.3.2 Current Practice

Precedent
In general, partnership income should be disclosed in the "other income" Block C of Schedule A of the 278. Disclosure of income from partnerships, other than investment income such as capital gains, dividends and interest that is readily available to filer, is difficult to deal with on OGE Form 278. Such income would include operating income and other similar types of "line 1" income from IRS Form K-1, and for investment partnerships would include the partners' share of management fees and other types of miscellaneous income. According to the Form 278 instructions, the exact amount of other income (as opposed to the amount indicated in brackets in Schedule A) must be reported. For most partnerships that report on a calendar year basis, it is impossible to provide exact amounts of either book or tax income for the partnership for the reporting period. For example, for most investment partnerships, taxable income is reported on a Form K-1 that is issued by September or early October of the following year, permitting the partner to include the income in the partners IRS Form 1040, filed by the extension date of October 15 of the year following the calendar year in which the income is recognized for tax purposes. As a result, compliance with the instructions for partnerships is, as a practical matter, impossible. Problems arise under this "cash distribution" convention in circumstances in which cash distributions and partnership income are substantially different, for example, when real estate partnerships distribute cash from refinancing, but have no taxable income for the tax year. As a practical matter, consistency of treatment has remained of paramount importance in disclosure of partnership items.

Authority
Instructions to OGE Form 278

B. Retirement Plans

1.4 Employee benefit plans exemption and diversified pooled investments

Precedent
A diversified pooled investment fund, if held through an otherwise exempt employee benefit fund, is also exempt from the restrictions of section 208(a): "Where a particular pooled investment fund meets the definition of 'diversified' in part 2640, see 5 C.F.R. § 2640.102(a), an employee may rely on the exemption as to that fund when the employee or other person specified in 18 U.S.C. § 208(a) holds the fund through a qualifying employee benefit plan." This exemption applies only to diversified pooled investment funds: "[When the employee] has specifically designated a non-diversified asset for an allocation of contributions, the employee benefit plan exemption will be unavailable as to that asset. For example, if a plan participant designates that contributions be divided between a diversified pooled investment fund and a non-diversified company stock fund, the employee benefit plan exemption will be available as to the diversified pooled investment fund, but will be unavailable as to the non-diversified company stock fund."

Plans outside of the United States.
The same exemption applies to plans outside of the United States, even though they are generally not covered by ERISA. ERISA coverage is not necessary for the exemption, but the plan must still "satisfy the criteria set forth at section 2640.201(c) (1) (iii) and the definition at section 2640.102(c) to qualify for the exemption."

Authority
Apol, D. J., U.S. Office of Government Ethics - LA-15-06: Employee Benefit Plans Through Which Employees Hold Diversified Pooled Investment Funds and Employee Benefit Plans Established or Maintained Outside of the United States. (May 5, 2015). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/7D7F24A707C3035F85257E96005FBF17/$FILE/839be259811a4b0da33edbf6bdc0e74c2.pdf

II. FINANCIAL CONFLICTS

The holdings disclosed on Form 278 are analyzed to determine whether a filer has potential conflicts. This process involves OGE, the appropriate designated agency ethics official (DAEO) and White House ethics counsel.

2.1 Regulatory Exemption

2.1.1 Current Practice

Precedent
The so-called “regulatory exemption” to disclosure of certain portfolio holdings generally refers to the exemption from financial conflicts for diversified mutual funds provided in OGE regulations. 18 U.S.C. § 208(b) (2) authorizes OGE to issue “regulatory exemptions” for financial disclosure and conflict of interest purposes. On December 18, 1996, OGE published a final rule, later codified as 5 C.F.R. §§ 2640.201-206, that exempted certain financial interests that were too remote to warrant disqualification under section 208. These included specifically diversified mutual funds and certain general categories of exemptions: (1) for pooled investment vehicles; (2) for securities; and (3) for miscellaneous items, which might only apply to certain agency employees.

Authority
5 U.S.C. App. (Ethics in Government Act of 1978); 18 U.S.C. §208; E.O. 12674, 54 FR 15159, 3 CFR, 1989 Comp., p. 215, as modified by E.O. 12731, 55 FR 42547, 1990 Comp., p. 306. (November 18, 2015) http://www.ecfr.gov/cgi-bin/text-idx?c=ecfr&SID=06f812f26e7ed9f364bb87944757b912&rgn=div5&view=text&node=5:3.0.10.10.12&idno=5

2.2 “Blind” EIFs

2.2.1 Bush II Administration

Precedent: Blind EIFs:
In 2009 and 2010, OGE determined that there is no section 208 conflict and therefore no requirement for nominees to divest their pooled investment vehicles if the investments: (1) meet the requirements of an excepted investment fund; and (2) are “blind.” Blind EIFs include hedge funds that do not disclose their holdings to their investors (typical of hedge funds that have “proprietary” or “black box” trading strategies) and other investment funds that are not transparent as to their holdings.

No Knowledge (“Manager”) Letters:
With respect to pooled investment vehicles, especially private equity funds, that decline to disclose their underlying holdings (e.g., because of confidentiality restrictions or because of proprietary trading strategies), OGE began to request a standardized form of documentation from the investment fund management to confirm that they would not provide information concerning underlying portfolio company holdings.

Standardized Letters:
The language of these “no knowledge/manager letters” became standardized during the Bush II administration and has included the following: “I am writing in response to your request for information regarding the individual investment positions of XXX Investment Fund. Please accept this letter as written confirmation that XXX Investment Fund does not disclose these individual investment positions to its investors. We are unable to make an exception for you.” While this language was originally designed to relieve filers of the obligation to provide information concerning underlying portfolio holdings for disclosure purposes, no knowledge/manager letters became a component of the “blind EIF” analysis for conflict of interest relief. See separate discussion of blind EIF development in Section 2.4.

Authority
Cusick, R. I., U.S. Office of Government Ethics - DO-08-022: Financial Disclosure Requirements for Pooled Investment Funds. (July 22, 2008). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/AD54F07936C7D6FA85257E96005FBE9B/$FILE/DO-08-022.pdf

2.2.2 Current Practice

Precedent: EIFs for Conflicts Purposes.
Because EIF status is only relevant for disclosure purposes and does not affect exemptions from potential conflicts of interest, unless some other exemption or special rule applies, underlying portfolio holdings of private equity funds must be provided to ethics officials (although not publicly disclosed) in order to permit conflict of interest analysis.

2.3 Special Categories of Exempted Financial Interests

2.3.1 Bush II Administration

Exchange Traded Funds
The development of new financial products during the administration required analysis of these products under the "regulatory exemption" for widely diversified mutual funds. For instance, most Exchange Traded Funds (ETFs) were determined to meet the exemption.

Authority
Guidance for Reviewers of the OGE Form 450, Part I (Assets & Income), page 18. Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20 Documents/1796AD5F70A6D14E85257E96006B95BD/$FILE/5c5f0f8f99784c17b212c7e4a062e01e3.pdf
OGE Advisory 00x8: Diversified and Sector Mutual Funds (2000). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Advisories/B34550F9C36529A085257E96005FBDEB/$FILE/00x8.pdf

2.3.2 Current Practice

Equity-linked Notes
Equity-linked notes are debt instruments with contingent payment features tied to equity indices and similar securities, such as an S&P index fund or other derivative instrument. Because the notes are not a direct interest in a mutual fund, but instead represent an indirect interest through the contingent payment feature, equity-linked notes do not meet the regulatory exemption for diversified mutual funds, even though they are substantially the same as an investment in a diversified mutual fund. During the Obama transition team period, and early in the Obama administration, investment holdings in "equity linked notes" were added, de facto, to the regulatory exemption category and analyzed for conflict of interest purposes accordingly. OGE and ethics officials, including in White House counsel, developed an "automatic" 208(b)(1) waiver for equity-linked notes, providing the functional equivalent of a regulatory exemption for such securities.

Authority
See OGE Program Advisory PA-15-02, Mar. 23, 2015. Retrieved from https://www.oge.gov/web/oge.nsf/All%20Documents/3AF13B35252607AE85257E96005FBF11/$FILE/PA-15-02.pdf

2.4 "Blind" Investment Funds

2.4.1 Bush II Administration

Precedent: Blind non-EIF Pooled Investment Vehicles:
If the pooled investment fund did not meet the requirements for an "excepted investment fund" and the filer could make full disclosure required by statute, under a 2008 OGE ruling the normal remedy is divestiture of the fund interest. OGE could grant an extension to divest the interest if the terms of the fund only permitted divestiture during a certain period.

Authority
DAEOgram DO-08-022 (2008). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/AD54F07936C7D6FA85257E96005FBE9B/$FILE/DO-08-022.pdf

2.4.2 Current Practice

Precedent: Blind non-EIFs:
In September 2014, OGE announced at the Annual Ethics Summit that it was considering modification of its 2008 blind non-EIF ruling to eliminate, under certain circumstances, the per se requirement that blind non-EIFs be divested. OGE no longer requires divestiture for blind non-EIFs. Instead, "the question of divestiture should turn primarily on whether a PAS nominee is unable to disclose a fund's holdings due to a lack of knowledge regarding those holdings." However, "when a PAS nominee has access to information about a fund's holdings but is unwilling to disclose those holdings because disclosure would violate a preexisting confidentiality agreement," divestiture remains appropriate.

Authority
Apol, D.J., OGE LA-14-05: Financial Disclosure Requirements for Pooled Investment

Funds. (September 30, 2014). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20 Documents/6796AE932D86D26E85257E96005FBF0B/$FILE/b1aa4ca489f74ef3b5bafc0af37fa2253.pdf

2.5 Qualified Blind Trusts

2.5.1 Bush II Administration

Precedent
OGE focused attention on the "independence" of trustees for purposes of qualified blind trust status. Under OGE guidance, "[a]n independent trustee cannot be affiliated with, associated with, related to or subject to the control or influence of anyone who has a beneficial interest in the trust." Non-institutional trustees were, for all practical purposes, unable to satisfy OGE requirements of independence. At least two trusts that satisfied congressional requirements for blind trust classification (congressional rules do not have the same "independence" requirements as does the executive branch rule) were deemed not to comply with the Independence requirement. Testing independence of trustees includes inquiry into the relationship between the trustee and the filer (and potentially an obligation to execute a "relationship" declaration or letter that includes representations regarding the relationship between the prospective trustee and the filer, to police the independence requirement).

Authority
5 CFR § 2634.405

2.5.2 Current Practice

Precedent
One can establish either a qualified blind trust or a qualified diversified trust in order avoid a section 208(b) conflict. The trust must be certified by OGE, and the employee must turn over "management of the trust assets to a trustee who is approved by OGE." In the case of a qualified blind trust, the independent trustee may not disclose any new assets purchased by the trust to the government employee in order to avoid creating a conflict. No qualified blind trusts were established in the Obama administration.

Authority
https://www.law.cornell.edu/cfr/text/5/part-2634/subpart-D
U.S. Office of Government Ethics - Resolving Conflicts of Interest. (2015). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/34F1CF2FAF392D7D85257E96006364EB

2.6 Qualified Diversified Trusts

Precedent
A qualified diversified trust must be "widely diversified," meaning that the value of assets concentrated in a particular economic or geographic sector is no more than 20 percent of the total and that no single entity other than the U.S. government makes up more than 5 percent of total value. 5 C.F.R. 2634.406(b)(2). Unlike a blind trust, the initial assets in a qualified diversified trust do not create a conflict "because the portfolio is so diversified that an official action taken by the employee would not have a direct and predictable effect on the value of the portfolio." A qualified trust may contain both blind and diversified portfolios as a "hybrid qualified trust." 5 C.F.R. § 2634.406(c) (2015).

Authority
See Generally Subpart D of 5 C.F.R. § 2634.

III. SPOUSAL CONFLICTS

3.1 Financial Conflicts

3.1.1 Current Practice

Precedent
OGE's website explains that a nominee "who is divorced or permanently separated need not report a

spouse's interests for the period before or after the divorce or permanent separation."
Otherwise, there are four criteria that a filer must be able to certify in order to avoid having to disclose their spouse's assets: (1) the assets are solely their spouse's, (2) they have no knowledge of the assets, (3) the assets have not been derived in any way from their income, assets, or activities, and (4) they neither derive, nor expect to derive, any financial or economic benefit from the assets.

As a practical matter, the requirements for the "innocent spouse" rule are almost never satisfied. For example, if the filer and the spouse are co-signatories on a mortgage or jointly hold significant amounts of property, separation of assets is not sufficient to avoid disclosure. Additionally, in situations in which there is no reporting requirement, 18 U.S.C. § 208 will still apply to particular matters in which an employee knows his or her separated spouse has a financial interest.

Authority
5 C.F.R. 2634.309
U.S. Office of Government Ethics. (2015). Public Financial Disclosure Guide, Section 2.02: Spouses and Dependent Children. Retrieved from https://www2.oge.gov/Web/278eGuide.nsf/2cf9ac792bc0654a85257ea1005f838a/6956138088b7033b85257f45007529ae?OpenDocument
U.S. Office of Government Ethics. (2015). Filing Requirements Related to Spouses and Children. Retrieved from https://www2.oge.gov/Web/OGE.nsf/110ba2529ebf517185257e9e004ff8ae/e1a4a7da3b934b3b85257e96006b95ca

3.2 Spousal Employment Conflicts

3.2.1 Bush II Administration

Case Study
The Department of Defense withdrew Rear Adm. Elizabeth Hight's appointment to head the Defense Information Systems Agency because her husband was the vice president of business development and sales for the mission systems sector, defense mission systems division at Northrop Grumman. The DOD withdrew the nomination after a member of the Senate Armed Services Committee blocked the nomination because of the potential conflict of interest with these two jobs.

Authority
Brewin, B., Defense plans to withdraw Hight's nomination to head DISA. Nextgov.com. (June 20, 2008). Retrieved from http://www.nextgov.com/defense/2008/06/defense-plans-to-withdraw-hights-nomination-to-head-disa/42165/

3.2.2 Current Practice

A. General Issue

Precedent
While the disclosure and conflicts rules concerning assets owned by spouses (and dependent children) are well-established, potential conflicts raised by spouses' careers are not, aside from "appearance of conflict" restrictions under 5 U.S.C. § 2634.502. Restrictions on employment activities of a filer's spouse are sometimes included in the filer's ethics agreement, and the form of these restrictions varies widely depending upon the filer's position and the spouse's career.

Case Study
Thomas Nides's ethics agreement for the position of deputy secretary of state for management and resources included restrictions on his interaction with his wife, who is a journalist. The agreement stated: "I will seek a waiver to participate in certain particular matters related to media strategy. However, I understand that any such waiver will not cover particular matters involving specific parties in which the American Broadcasting Company is the sole party."

Authority
Thomas Nides ethics agreement.
But see William Schultz ethics agreement (containing no "media strategy" provision for spouse's position as a reporter at the Washington Post).
But see Susan Rice ethics agreement (containing no "media strategy" provision for spouse's position as a

producer at ABC News).

Case Study
David Ogden, Deputy Attorney General in the Justice Department, received an ethics pledge waiver for work involving his former employer and his spouse's current employer, WilmerHale. As part of the waiver, Ogden's spouse agreed to a screening arrangement wherein she would not receive any portion of the fees from WilmerHale's involvement in the matter.

Authority
Lofthus, L. Certificate of Public Interest Waiver for David Ogden. (May 6, 2009). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/D5A3829B3E87715085257EBC00669521/$FILE/8c33143bfb3b49cdbb06ad700898b3c23.pdf

B. Performance-Based Bonuses

Precedent
When there is little likelihood that the nominee will be involved in any matters affecting the spouse's employer, and the spouse receives a performance-based bonus and does not have an equity interest in their employer, the ethics agreement only contains a section 2635.502 recusal.

Authority
Samantha Power ethics agreement (containing only a section 2635.502 recusal with respect to spouse's position as tenured faculty member at Harvard Law School).
Christina Romer ethics agreement (containing only a section 2635.502 recusal with respect to spouse's position as unpaid scholar at the International Monetary Fund).
Tim Broas ethics agreement (containing only a section 2635.502 recusal with respect to spouse's position as an attorney for the Washington Legal Clinic for the Homeless).

Precedent
When there is a substantial likelihood that the nominee will be involved in some matters that affect a spouse's employer, and the spouse receives a performance-based bonus and does not have an equity interest in the employer, the ethics agreement contains a section 2635.502 recusal and a "limited" section 208 recusal.

Case Study
Deputy Secretary of the Treasury Sarah Raskin, whose spouse is a Maryland state senator, agreed to "not participate personally and substantially in any particular matter involving specific parties in which the State of Maryland is a party or represents a party, unless [she is] first authorized to participate, pursuant to 5 C.F.R. § 2635.502(d)." In addition, she agreed to a "limited" section 208 recusal in which she would "not participate personally and substantially in any particular matter that has a direct and predictable effect on [her] spouse's compensation or employment with the State of Maryland, unless [she] first obtain[s] a written waiver pursuant to 18 U.S.C. § 208(b)(1)." A "limited" section 208 recusal requires the nominee to recuse herself only from matters affecting her spouse's compensation and employment, as opposed to a "full" section 208 recusal that requires the nominee to recuse herself from any matter affecting the financial interests of her spouse's employer.

Authority
Sarah Raskin ethics agreement .
See also Lisa Jackson ethics agreement (containing a limited section 208 recusal with respect to spouse's position as a computer analyst for Merrill Lynch).

See also William Schultz ethics agreement (containing a limited section 208 recusal with respect to spouse's position as a reporter for the Washington Post).

C. Profit-Sharing Agreements

Precedent
When the spouse has an equity interest in their employer, a profit-sharing agreement with the employer, or receives compensation based on their employer's profitability, the nominee's ethics agreement contains a "full" section 208 recusal.

Case Study
Former Secretary of Labor Hilda Solis, whose spouse owned an auto body shop in southern California, agreed to a "full" section 208 recusal in which she would "not participate personally and substantially in any particular matter that has a direct and predictable effect on the financial interests of [Sam's Foreign and Domestic Auto Center] unless [she] first obtain[s] a written waiver, pursuant to 18 U.S.C. § 208(b)(1)...." Despite the "likelihood that [her] duties will involve a matter affecting this entity is remote," the Department of Labor nonetheless incorporated a "full" section 208 recusal into her ethics agreement.

Authority
Hilda Solis ethics agreement.
See also Charles Rivkin ethics agreement (containing a full section 208 recusal with respect to spouse's position at Capital Research & Management Company).
See also Susan Rice ethics agreement (containing a full section 208 recusal with respect to spouse's position at Disney).
See also Margaret Hamburg ethics agreement (containing a full section 208 recusal with respect to spouse's position at an investment fund).

D. Spouse is Equity Partner at Law Firm

Precedent
When the spouse is an equity partner in a law firm, the nominee's ethics requirement typically contains a "full" section 208 recusal, a section 2635.502 recusal for matters affecting clients of the law firm, and a communications limitation. But see Mary Jo White case study below in which a spouse transitioned from equity partnership to non-equity position upon nominee's confirmation.

Case Study
SEC Commissioner Daniel Gallagher, whose spouse was an equity partner at Levin & Gallagher, agreed to a full section 208 recusal in which he would not "participate personally and substantially in any particular matter that has a direct and predictable effect on the financial interests of the firm, unless [he] receives a written waiver, pursuant to 18 U.S.C. § 208(b)(1)." He also agreed to a section 2635.502 recusal provision for issues involving clients of Levin & Gallagher: "I also will not participate personally and substantially in any particular matter involving specific parties in which a client of my spouse is a party or represents a party, unless I have been authorized pursuant to 5 C.F.R. § 2635.502(d)." Finally, the ethics agreement contains a commitment on the part of Commissioner Gallagher's spouse to not communicate with the SEC: "[M]y spouse has agreed not to communicate with the Securities & Exchange Commission on behalf of the firm or any client."

Authority
Gallagher ethics agreement.
See also Denise Bauer ethics agreement (containing a full section 208 recusal, a section 2635.502 recusal and a communications limitation with respect to spouse's position as an equity partner at Latham & Watkins, LLP).
U.S. Office of Government Ethics. Legal Advisory 95x1: Conflict of Interest Issues Raised by Spouse's Position as Partner in Law Firm. (February 13, 1995). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/8260B300B06CEDDF85257E96005FBCDC/$FILE/f65a75777639422eae4927637009319d3.pdf.

Case Study
SEC Chairwoman Mary Jo White's spouse had been an equity partner at Cravath, Swaine, and Moore LLP, but converted to a non-equity partner status upon White's confirmation. Currently, her spouse receives a fixed salary and annual performance bonus, and consequently the ethics agreement contains only a "limited" section 208 recusal in which White agrees to "not participate personally and substantially in any particular matter that has a direct and predictable effect on my spouse's compensation or employment at the firm, unless [she] first obtain[s] a written waiver, pursuant to 18 U.S.C. § 208(b) (1)." The ethics agreement also contains unique section 2635.502 recusal language in which White agrees to "not participate personally and substantially in any particular matter involving specific parties in which" Cravath or her husband's clients are "a party or represent[] a party, unless [she is] first authorized to participate, pursuant to § 2635.502(d)." However, if White "know[s] that [her] spouse has consulted for fewer than 16 hours on a matter involving a client, [she] will consult [the SEC ethics office] for a determination under 5 C.F.R. § 2635.502(c) as to the appropriateness of participating personally and substantially in any particular matter

involving specific parties in which that client is a party or represents a party." Finally, the ethics agreement contains a communications limitation: "[M]y spouse has agreed that he will not communicate directly with the SEC on behalf of the firm or any client in connecting with a rulemaking proposed by the SEC and that he will not sign any such comment letters that the law firm submits to the SEC."

Authority
Macy Jo White ethics agreement.

E. Restrictions on Communication

Precedent
Although an ethics agreement is only executed by the nominee, several agreements contain promises that the spouse not communicate directly with the nominee's agency. The OGE Ethics Agreement Guide states that this language is needed when the nominee's agency "occasionally receives communications from the spouse's employer."

Case Study
NIH Director Francis Collins, whose wife is an officer of the Genetic Alliance and an active participant in the National Society of Genetic Counselors, signed an ethics agreement that limited his spouse's ability to communicate with the NIH. In addition to standard "limited" section 208 and section 2635.502 recusals, Director Collins's ethics agreement states that his "spouse has agreed not to communicate with NIH on behalf of either of these entities or other organizations during [his] appointment as director."

Authority
Francis Collins ethics agreement.

Case Study
Former Ambassador to Hungary Eleni Tsakopoulos-Koulanakis, whose spouse is an employee of California-based AKT Development Corporation, entered into an ethics agreement that stated her "spouse has agreed not to communicate with the U.S. Department of State on behalf of AKT Development Corporation during [her] appointment to the position of Ambassador to the Republic of Hungary."

Authority
Eleni Tsakopoulos-Koulanakis ethics agreement.

Case Study
Anne Richard, the Assistant Secretary of State for the Bureau of Population, Refugees and Migration, is married to a United Nations employee, and signed an ethics agreement with a number of unique communications limitations, in addition to a typical section 2635.502 recusal. Richard agreed to "not participate in any meeting in which [her] spouse is participating as a UN employee," to "not communicate with [her] spouse in his capacity as a UN employee," and to "not communicate individually with [her] spouse's employing UN organization, unless [she is] first authorized to participate pursuant to 5 C.F.R. § 2635.502(d)."

Authority
Anne Richard ethics agreement.

F. Miscellaneous

Precedent
If the spouse is a salaried employee of an agency contractor, then the nominee must sign an ethics agreement that contains a "limited" section 208 recusal (nominee will not participate in matters affecting her spouse's compensation and employment) and a section 2635.502 recusal (to avoid the "appearance of loss of impartiality").

Authority
OGE Legal Advisory 85x10: Conflict of Interest Issues Raised by Spouse's Employment at Government Contractor (July 15, 1985)
(U.S. Office of Government Ethics. 85x10: Conflict of Interest Issues Raised by Spouse's Employment with Government Contractor. (July 15, 1985). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20 Documents/36030E88C0F4EC3A85257E96005FBC0F/$FILE/9ee1d961f3d744439bfa08925cd37aa32.

pdf);
OGE Legal Advisory 84x6: Conflict of Interest Issues Raised by Spouse's Employment on Retainer with a Government Contractor (May 1, 1984)
(U.S. Office of Government Ethics. 84x6: Conflict of Interest Issues Raised by Spouse's Employment on Retainer with a Government Contractor. (1984, May 1). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/0A017F8E497197BE85257E96005FBC00/$FILE/b590f7160965476f9ac4889ae9853a032.pdf).

Precedent
When a spouse receives royalties from a publication, the nominee must agree to recuse herself from participating in matters that would affect the "ability or willingness" of the publisher to honor its contract.
Case Study
Christina Romer, former chairperson of the Council of Economic Advisers, is married to an economics professor who receives royalties from McGraw-Hill Companies and Authors Registry for sales of his textbook, Advanced Macroeconomics. Romer's ethics agreement states: "I will not participate personally and substantially in any particular matter that has a direct and predictable effect on the ability or willingness of McGraw-Hill Companies and Authors Registry to honor their contractual obligations regarding these royalties, unless I first obtain a written waiver, pursuant to 18 U.S.C. § 208(b)(1)."

Authority
Cristina Romer ethics agreement.
See also Francis Collins ethics agreement (containing an ability and willingness recusal with respect to spouse's book publisher).
See also Sarah Raskin ethics agreement (containing an ability and willingness recusal with respect to spouse's book publisher).

Case Study
Maria Contreras-Sweet agreed to remove her name from her and her spouse's executive search consulting business, the Contreras Sweet Company, upon her confirmation as Small Business Administration administrator. As her spouse remained sole proprietor of the firm, Contreras-Sweet agreed in her ethics agreement that she "will not participate personally or substantially in any particular matter that has a direct and predictable effect on the financial interests of the Contreras Sweet Company, or its successors, unless [she] first obtain[s] a written waiver pursuant to 18 U.S.C. § 208(b) (1)."

Authority
Maria Contreras-Sweet ethics agreement.
See also Lael Brainard ethics agreement (containing an agreement to remove her name from consulting firm shared with her spouse).

IV. REMEDIES FOR CONFLICTS

4.1 Recusal

4.1.1 Clinton Administration

Precedent
An employee may be recused from working on a matter under 18 U.S.C. § 208, 5 C.F.R. § 2635.502, or 5 C.F.R. § 2635.503. Often documents containing recusal requirements are included with the employee's ethics agreement. A recusal document typically outlines the topic of recusal, the gatekeeper who will screen the employee's communications to make sure they are not involved with the covered matter, and the agency person who will handle the topic in the recused employee's place.

Authority
U.S. Office of Government Ethics - 99x8: Recusal Obligation and Screening Arrangements.
(2015). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/FC5E4250FAED2F8085257E96005FBCFD/$FILE/99x8.pdf

4.1.2 Bush II Administration

Precedent
Treasury Secretary Henry Paulson's ethics agreement required him to recuse himself from matters involving his (small) pension plan at Goldman Sachs for his tenure as secretary of the Treasury. During the 2008 financial crisis, Paulson received a 208(b) (1) waiver in order to communicate with Goldman.

Authority
Henry Paulson ethics agreement
See also During Crisis, Paulson's Calls to Goldman Posed Ethics Test. "The New York Times." (2015). Retrieved from http://www.nytimes.com/2009/08/09/business/09paulson.html?pagewanted=all&_r=0

4.1.3 Current Practice

Precedent
Secretary of State John Kerry was recused from participating in matters in which the H.J. Heinz Company or its subsidiaries are a party or represent a party because of his wife's large financial holdings in the Heinz Company.

Authority
John F. Kerry ethics agreement.

Precedent
Ethics officials have discretion to determine when a recusal arrangement is appropriate and how PAS officials should demonstrate compliance. A screening arrangement may be unnecessary for stocks that will be quickly divested, for an inactive company that exists only for administrative reasons, or for an entity that has little chance of coming before the PAS official's agency. If a screening arrangement is not used, the official must issue a written recusal statement "reaffirming his or her agreement to not engage in matters implicating the ethics agreement signed in connection with the PAS official's nomination." OGE considers this "acceptable evidence of compliance with recusal obligations."

Authority
Apol, D. J., U.S. Office of Government Ethics - LA-14-06: Flexibility in Ensuring and Documenting Compliance with Ethics Agreements. (November 4, 2014). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/ECDADA000D6612BF85257E96005FBF0C/$FILE/eecbe744513c40b7a3c049def23f2fdd3.pdf

4.2 Section 208(b) (1) Waiver

4.2.1 Clinton Administration

Precedent
18 U.S.C. § 208(b) (1) is the authorizing statute, which permits a waiver for financial conflicts. On Dec.18, 1996, OGE promulgated a final rule, codified as 5 C.F.R. § 2640.301, which provides guidance on issuing a section 208(b) (1) waiver. Under Executive Order 12674, agencies must consult with OGE "when practicable" before issuing this waiver. Agencies decide whether to grant a waiver but they must send copies to OGE. Typically waivers are not granted unless the other curing mechanisms, exemptions, recusal, and divestiture, are unavailable or impracticable. The waiver must: (1) be issued in writing by the person responsible for the employee's appointment (often the DAEO); (2) be issued prior to the employee's participation in a particular matter covered by the waiver; (3) disclose the disqualifying financial interest and nature of the matter the employee will work on; and (4) conclude that the disqualifying financial interest is not so substantial as to be deemed likely to affect the employee's integrity. OGE lists other factors to consider before granting a waiver in the case study linked below.

Authority
Cusick, R. I. U.S. Office of Government Ethics - DO-07-006: Waivers under 18 U.S.C. §§ 208(b) (1) and (b) (3). (February 23, 2007). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/328CE4B5A300EAEB85257E96005FBDE5/$FILE/do-07-006.pdf

4.2.2 Bush II Administration

Precedent
Henry Paulson retained his Goldman Sachs defined benefit pension plan, which met the definition of a disqualifying financial interest under 18 U.S.C. § 208. During the 2008 financial crisis, Paulson received a waiver, which allowed him to communicate with Goldman Sachs.

Authority
The Paulson Ethics Waiver | Bear Market Investments. (August 11, 2009). Retrieved from http://www.bearmarketinvestments.com/the-paulson-ethics-waiver

4.2.3 Current Practice

Precedent
Various rules of thumb have been developed in connection with section 208(b) (1) waiver requests, primarily relating to the size of the conflicted financial interest as to which the waiver is requested relative to the filer's total net worth. Thus, in general, if the conflicted interest is a small fraction of the filer's wealth, a waiver request could be granted by the agency and supported by OGE. Several variables impact this analysis. For example, the denominator of the fraction is generally limited to the filer's investable net worth, excluding residential real estate and other non-investment type assets. Establishing support for the denominator, especially where the filer's investments include illiquid investment funds, is necessary. In the case of an investment fund, since the waiver is granted with respect to the interest in the fund itself, rather than with respect to the individual portfolio holdings of the fund, analysis may be required as to the relative value of both the interest in the fund, and the proportionate interest in the underlying portfolio holdings that have created potential conflicts of interest.

Case Study
Cheryl Mills, former counselor and chief of staff, U.S. Department of State, received a waiver in order to serve as the U.S. government's representative on the Board of the Interim Haiti Recovery Commission (IHRC). Mills began her position at the State Department in 2009 and requested the waiver in 2011 after the IHRC was set-up. The waiver was approved on the grounds that Mills had no financial interest in the activities of the IHRC and that the goals of the IHRC and the State Department did not conflict and, in fact, were somewhat coextensive. See Cheryl Mills 208(b) (1) Waiver, pages 12-13.

4.3 Section 208(b) (3) Waiver

4.3.1 Clinton Administration

Precedent
Waiver under section 208(b) (3) is available for Special Government Employees (SGEs) serving on advisory committees established under the Federal Advisory Committee Act. On Dec.18, 1996, OGE published a final rule giving guidance on section 208(b) (3) waivers. Agencies and not OGE decide whether to grant a waiver. The link below to a 2007 OGE document explains the suggested factors considered.

Authority
Cusick, R. I. U.S. Office of Government Ethics - DO-07-006: Waivers under 18 U.S.C. §§ 208(b) (1) and (b) (3). (February 23, 2007). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20 Documents/328CE4B5A300EAEB85257E96005FBDE5/$FILE/do-07-006.pdf

4.3.2 Current Practice

Precedent
Waivers for certain special government employees are authorized under 18 U.S.C. § 208(b) (3). Under OGE regulations, waivers issued under section 208(b) (3) must be issued "prior to the individual taking any action in the matter or matters" for which the waiver is sought. 5 C.F.R. § 2640.302(a) (6). The "agency official first must review the special government employee's financial disclosure form before determining that a waiver is appropriate in light of the information disclosed by the employee."

Authority
Fox, D. W. U.S. Office of Government Ethics - DO-10-005: Guidance on Waivers under 18 U.S.C. § 208(b), Authorizations under Agency Supplemental Regulations. (April 22, 2010). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/

F0D8053747931EAD85257E96005FBB7A/$FILE/438cb0a3fe89437e877ef22c26c6fada4.pdf

Case Study

In 2009, the Food and Drug Administration granted a waiver to Dr. Richard Mann, a transplant nephrologist, to serve as a temporary voting member to the Cardiovascular and Renal Drugs Advisory Committee in the matter of a new drug application for a drug to be used in kidney transplants. His employer, Robert Wood Johnson Medical School, had received a research contract for a competing drug. The committee needed the "input of physicians who [had been] responsible for the day-to-day management of kidney transplant patients." Because of Dr. Mann's extensive experience conducting kidney transplants, the need for his input outweighed the concerns over a potential for a conflict of interest. Out of the 16 transplant nephrologists who were invited, Dr. Mann was the only one who could attend the meeting.

Authority

Peterson, J. E. 18 U.S.C. 208(b) (3) Waiver to Allow Participation in a Food and Drug Administration Advisory Committee. (November 4, 2009). Retrieved from http://www.fda.gov/downloads/AdvisoryCommittees/CommitteesMeetingMaterils/Drugs/CardiovascularandRenalDrugsAdvisoryCommittee/UCM191574.pdf

4.4 Divestiture

4.4.1 Bush I Administration

Precedent

In order to comply with 18 U.S.C. § 208, nominees may have to divest certain financial holdings that pose a conflict of interest. Since 1989, section 1043 of the Internal Revenue Code allows the director of OGE to issue a certificate of divestiture, which allows the employee to sell the property and reinvest the proceeds into permitted property. Any capital gains tax owed on the sale of the conflicting property is deferred until the replacement permitted property is sold.

Authority

26 U.S.C. § 1043 - Internal Revenue Code. (2009). Retrieved from http://www.gpo.gov/fdsys/pkg/USCODE-2009-title26/html/USCODE-2009-title26-subtitleA-chap1-subchapO-partIII-sec1043.htm

4.4.2 Current Practice

Precedent

By the administration of President George W. Bush, divestiture had become the "default remedy" for many potential conflicts of interest, eclipsing the use of recusals and waivers in many situations in which such alternative remedies might have been viable but were viewed as less effective or less politically palatable. This continues to be the case.

V. EXECUTIVE COMPENSATION ARRANGEMENTS

5.1 General Issues Relating to Executive Compensation Arrangements

Executive compensation arrangements constitute one of the most complicated areas for government ethics compliance. These arrangements pose disclosure, conflict of interest, and remedial issues. Executive compensation arrangements, as individualized contractual arrangements between employers and executives, take a range of forms. Treatment of executive compensation arrangements in ethics agreements is subject to a considerable degree of flexibility and extended negotiations concerning the treatment of such plans was common in the Obama and Bush II administrations.

Significant amounts of time are dedicated to resolving potential conflicts related to executive compensation arrangements. Little standardization of treatment has developed. No administration has utilized a template to handle all executive compensation arrangements in a consistent manner.

Disclosure and related technical issues are addressed in Public Financial Disclosure: A Reviewer's Reference (Second Edition) section 6 (Nov. 2004). OGE's new electronic 278 highlights executor compensation issues, moving disclosure

of such arrangements to the front of the on-line reporting system.
Some elements of executive compensation arrangements in private industry exacerbate the complexity and lack of standardization for purposes of government ethics, including the absence of clear definitions, frequent lack of clarity, and even misunderstandings on the part of the filers as to the relevant features of their own executive compensation arrangements. Filers themselves often confuse different categories and features of executive compensation arrangements, e.g., stock options, restricted stock units and phantom stock, even if they understand the economics of their arrangements.

Direct discussions with human resources and other components of the employer are often necessary in order to address disclosure and conflict issues adequately. However, such contacts raise confidentiality concerns, exacerbating some of the practical problems of dealing with such arrangements in the vetting process. For example, certain executive compensation arrangements may raise potential 208 issues that could be resolved by amendments to such arrangements, but such changes require compensation committee or board action, or raise issues under ERISA rules and tax rules, especially IRC § 409A.

5.2 Bonus Payments

5.2.1 Current Practice

Precedent
To an extent not evident in vetting during prior administrations, the Obama administration focused extensively on bonus payments paid to filers by their employers, especially bonus payments made for the portion of the current calendar year prior to the start of government service and any other bonus payments made in connection with termination of employment. This focus was in part tied to the financial crisis in late 2008, and the emphasis in the press concerning large bonuses paid to executives in private industry.

These bonus payments were necessarily made prior to the beginning of government service, in order to avoid "supplementation" issues under 18 U.S.C. § 209. Under Crandon v. United States, 494 U.S. 152 (1990), as long as the payments are received prior to the beginning of government service, a "safe harbor" precluded the application of section 209. Thus, regardless of whether the bonus evidences an intent to "make up" for reduced compensation while in government, as long as the payment is received under the terms of the Crandon decision, no section 209 issue can arise. (Issues under the extraordinary payment restructures in 5 CFR § 2634.203 are separate and less significant because of the Obama pledge.) Acceptance of this safe harbor preclusion of section 209 by ethics officials with respect to all payments to individuals entering government service has been uneven, notwithstanding the clear instruction of the Supreme Court on this issue.

In a number of vetting cases in the Obama administration, questions were raised concerning how the employer determined the amount of the bonus, and whether the determination was based upon "objective" factors (viewed as a positive). These questions may reflect ethics officials' limited familiarity with how such bonuses are actually determined in the private sector, especially for senior executives. Because such bonuses are generally determined by a compensation committee or other subset of the Board of Directors and because such bonus payments necessarily involve business judgments, rather than the use of a simple mathematical formula, in many cases it was not possible to show that the determination was based exclusively upon objective factors. Often, an explanation that bonus determinations are not purely discretionary could satisfy these concerns.

5.3 Deferred Compensation Arrangements

General Issues.
Deferred compensation arrangements, sometimes also referred to as "nonqualified" retirement plans, involve the agreement by the employee to forgo receipt of current salary in exchange for an unsecured and unfunded promises by the employer to pay an amount in the future that reflects the foregone salary plus some return or "yield." The total amount, including yield, is tracked in a "deferred compensation account." The employee does not have any security interest in the account, which remains subject to the claims of general creditors of the employer, and therefore the amount is at risk of the solvency of the employer.

A contractual obligation of the employer to pay the deferred compensation account to the employee or former employee represents a "financial interest" by the employee in the employer for purposes of section 208.

Deferred compensation arrangements take a number of forms. Some deferred compensation arrangements involve establishment of a contractual obligation by the employer to pay the employee the amount of the compensation that has been deferred, plus some fixed yield, and therefore raise only the "ability or willingness" issue described below. Other deferred compensation arrangements replicate investment accounts, because the deferred compensation account is "invested" in securities, or a basket of securities, selected by the employee, much like a qualified defined contribution plan. The amount paid out in the future is increased by the investment return of those selected securities. (These arrangements, in which the yield tracks selected securities, do not involve actual investments in the securities; the yield is simply adjusted by an amount calculated based upon the investment performance of the securities.)

5.3.1 Clinton Administration

Precedent
A financial interest represented by deferred compensation account in favor of a filer gives rise to potential conflicts of interest under section 208 as a "financial interest" with respect to the obligor (the employer or former employer). Such conflict of interest could be mitigated by purchasing a surety bond or other insurance product from a third-party insurance company. The surety bond covered the risk that the employer could not or would not pay the deferred compensation obligation in the future, and therefore in effect ensured the solvency of the employer under the deferred compensation arrangement. This insurance the deferred compensation obligation and therefore eliminated the conflict of interest with respect to the employer.

5.3.2 Bush II Administration

Precedent
During the George W. Bush administration, the cost of surety bond premiums, as used in the Clinton administration, increased, and their availability decreased (only a few insurers, including Lloyds and Chubb were willing to issue such policies). Therefore the ability to mitigate conflicts of interest represented by deferred compensation arrangements was threatened.

Faced with this concern, the treatment of deferred compensation arrangements for purposes of potential conflicts of interest was changed during the Bush II administration. Under the revised policy, no surety bond or other insurance was required to defease the obligation represented by the deferred compensation arrangement. Instead, the potential section 208 conflict is limited to the ability of the filer to impact the employer's "ability or willingness to pay" the amount due on the deferred compensation arrangement. Based on this limited scope of potential conflict, the filer's ethics agreement included a commitment that the filer would recuse herself from any "particular matters" that could affect the "ability or willingness to pay" of the employer, that is, the ability of the filer to engage in particular matters that could affect the solvency of the employer. Since such particular matters are rare (although not unheard of, especially in connection with the financial collapse in 2008), the ability or willingness provision of the ethics agreement has become the norm.

Authority
DAEOgram 99x6 (Apr. 14, 1999) (concerning only qualified pension plans, not deferred compensation arrangements). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20 Documents/72A887D63D64192185257E96005FBCFB/$FILE/bf65b709bbb841598a91b1f52db4c9be3.pdf

5.3.3 Current Practice

Precedent
A "straight" deferred compensation arrangement, involving an obligation to pay foregone salary plus a fixed yield can be addressed through the "ability or willingness" recusal mechanism developed in the George W. Bush administration. Deferred compensation arrangements that included a "tracking" mechanism that permitted the deferred compensation account to be adjusted based upon the investment results of selected securities or a basket of securities in which the deferred compensation balance was "invested" gives rise to potential section 208 conflicts.

5.4 Special Categories of Executive Equity Compensations Interests

As noted, executive compensation arrangements take a wide array of forms, ranging from special bonus payments to interests that resemble stock. Each of these forms raises separate issues in the vetting process.

5.4.1 Current Practice

Precedent

Stock options. Compensatory stock options, for section 208 purposes, represent financial interests in the issuer of the options, identical to the financial interest represented by outright ownership of shares. Compensatory stock options are often issued with vesting restrictions, which provide that the filer as holder of the stock option will forfeit the option under certain circumstances, generally including termination of employment before "vesting dates" (sometimes conditioned upon termination without good cause, or other contractual complexities).

Compensatory stock options issued by public companies are almost always issued at "fair market value," that is, the exercise price that must be paid in order to receive the underlying stock is generally equal to the fair market value of the stock at the time the options were issued, and therefore the "spread" representing net fair market value to the holder is initially zero. In addition, fair market value of the underlying stock may decline below the exercise price, in which case the options are "underwater," and therefore the options themselves may have little or no current value. However, this nominal value for compensatory stock options does not reduce the attention paid to such options in the vetting process.

OGE's Public Financial Disclosure: A Reviewer's Reference (Second Edition) details the way in which compensatory stock options should be reported on the 278, generally on Schedule A and often as part of the employer arrangements on Schedule C Part II. In the Obama administration, additional details concerning compensatory stock options were required as part of 278 disclosure. Detailed exhibits are often attached to the 278 to sufficiently describe compensatory stock options. These attachments included details concerning the number of options, the forfeiture conditions (that is, the dates on which the forfeiture conditions would be satisfied or would lapse), the strike price and whether the stock options were "underwater." This detail was believed to be necessary by OGE and ethics officials in order to provide sufficient information to the public concerning compensatory options, and reflected a suspicion that such options might have little current fair market value (which ordinarily would be reflected on Schedule A) but could represent substantial "optionality" value in the future, for example for issuing companies in the technology sector.

The complexity of and concerns regarding various compensation option arrangements contributed to an expanded amount of disclosure concerning options (as well as other executive compensation arrangements), and led during the Obama administration to extraordinary attention to the details of disclosure concerning such arrangements on the various parts of the 278, including Schedule C Part II. During the Obama administration, such disclosure often required several iterations and negotiation among various stakeholders in order to satisfy all constituencies that the arrangements had been adequately disclosed on various parts of the 278, and there was no standardized approach developed for such disclosure. Filers often omitted supplying text for such disclosure, deferring to OGE and ethics officials as to their preferred format on initial drafts of the 278.

Restricted stock.

Unlike compensatory options, stock issued in connection with services represents outright ownership of shares, and does not require payment of an exercise price to receive the shares. Forfeiture conditions cause compensatory stock to be "restricted stock," and those "vesting" restrictions would be included in the details disclosed in the 278, including in an attachment to the 278. Ordinarily, compensatory stock is issued without payment, or at a steep discount. Any discount is taxable as compensation income, as soon as the forfeiture conditions end, or "lapse." Such lapse can occur as a result of "accelerated vesting." Some executive compensation plans involving grants of restricted stock permit acceleration of vesting upon taking a portion in a university, a nongovernmental organization, or the government.

Restricted stock units.

Restricted stock units, or RSUs, represent a right, in the hands of an employee, to receive a certain number of employer shares upon certain events, and are generally granted for no consideration to be paid by the employee. RSUs constitute a contractual right, not a direct interest in the employer shares themselves. In practice, the value represented by RSUs is converted into cash based on the fair market value of the shares represented by the units at some designated vesting or other maturity date, although occasionally employees convert RSUs into shares and hold the compensatory shares.

The interest in employer equity represented by RSUs is often confused with stock options.

Phantom stock.
As in the case of RSUs, phantom stock, or "phantom stock rights," represents at best an indirect interest in employer shares. Phantom shares are converted into cash upon certain events, based upon the appreciation in the index shares, and unlike RSUs are never convertible into actual shares. For purposes of section 208, phantom stock is a financial interest identical to employer stock.

Phantom stock or phantom stock rights are often confused with stock options and RSUs.

Carried interests.
Carried interests, also sometimes referred to as "promoted interests," are a creature of partnership tax law, where the technical term for such partnership equity interests is "profits interests." Profits interests represent an interest in a partnership (including a limited liability company treated as a partnership for U.S. tax purposes) other than a capital interest (which is a partnership interest that reflects an interest in capital, often in the form of a capital account; a profits interest has a zero capital account). Carried interests permit holders to receive allocations of capital gain in connection with services to the partnership, in effect as a substitute for compensation for services (which would be taxed at the maximum rate applicable to ordinary income), and are generally issued to the managers of such funds. Carried interests are common in real estate partnerships and are practically universal in investment partnerships, including private equity and, to a limited degree, hedge fund arrangements. As the holder or "owner" of a carried interest, a filer is treated as a full owner of an equity interest in a partnership, including in the profits and losses of the partnership, and not simply as right to get cash compensation.

Carried interests carry with them both a political and a conflict of interest dimension. Politically, carried interests have been the subject of tax reform efforts. The reform proposals would charge holders income taxed at ordinary income rates. These reform efforts have been ongoing for many years, and have been blocked during the Obama administration.

From a conflict point of view, the holder of a carried interest is a partner for all relevant purposes, and therefore the holder of the carried interest has a conflict with respect to each of the portfolio companies or other investments held in the fund.

Analysis of carried interests during the vetting of appointees during the Obama administration confronted the increasing complexity of carried interest arrangements. For example, multitier private equity funds might issue a single carried interest that would represent an indirect interest in the profits of numerous lower-tier partnerships and therefore in each of the portfolio companies of those partnerships. Although in substance a performance bonus related to the performance of the investment funds, carried interests transformed such bonus arrangements into an analysis similar to the analysis required with respect to EIF type investments. For carried interests, disclosure of the financial interest on Schedule A and more detailed disclosure in attachments to Schedule C Part II is often required.
From a political point of view, in the Obama administration, the holding of a carried interest creates vetting concerns.
Qualified plans. Filers have often failed to take into account assets held in 401(k) or other ERISA qualified plans or in section 529 plans established for purposes of paying for children's tuition. Each of these qualified plans, to the extent that it holds interests in underlying securities, is treated as holding financial interest on behalf of filers and all holdings must be disclosed. Qualified plans raise a number of disclosure issues that are exacerbated by the fact that filers fail to focus on these plans, because they do not generate K-1's or 1099s to report their income for tax purposes, and therefore can be overlooked if financial information is being compiled using tax returns.

Section 529 plans pose unique issues, because of the "asset mix" of such plans. Generally, each state plan provides for a limited menu of investment options. As the maturity of the plan evolves closer to the date on which the funds will be used for college expenses, the mix of investment options tends towards fixed income and away from equity investments (in order to reduce the risk profile of the investments), and therefore section 529 plan investments will change and the conflict profile may also change.

5.5 Treatment of Payments That Raise “Emolument” Issues

Under Article I, Section 9, Clause 8 of the Constitution, the “Emoluments Clause,” certain federal employees are prevented from receiving payments from foreign governments. For these purposes, foreign governments can include investment funds owned by such governments (including “sovereign wealth funds”), and therefore to the extent certain federal employees receive payments the source of which is a sovereign wealth fund, the payments can be subject to the Emoluments Clause.

Application of the Emoluments Clause to categories of appointees, e.g., part-time employees who retain an interest in law partnerships, is subject to considerable uncertainty, in part because of changes in advice received from the Office of Legal Counsel in the Department of Justice during different administrations.

5.5.1 Current Practice

Authority
Yoder, E. Federal Employees Warned to Watch Out for Emoluments, “The Washington Post.” (April 2, 2013). Retrieved from https://www.washingtonpost.com/news/federal-eye/wp/2013/04/02/federal-employees-warned-to-watch-out-for-emoluments/

OLC Opinion, “Application of the Emoluments Clause to a Member of the FBI Director’s Advisory Board” (Jan. 15, 2007). Retrieved from https://www.oge.gov/web/oge.nsf/Legal%20Interpretation/6FB719825F20112885257EF2004DFF4D/$FILE/fbi_advisory_board_opinion_061507_0.pdf

OLC Opinion, “Applicability of the Emoluments Clause to Nongovernmental Members of ACUS” (Jun. 3, 2010). Retrieved from https://www.justice.gov/sites/default/files/olc/opinions/2010/06/31/acus-emoluments-clause_0.pdf

VI. ORM 86 SUPPLEMENT

Supplement to Standard Form 86 (SF-86) is technically associated with the National Security Questionnaire (Standard Form 86), but is only tangentially related to that form. The “86 Supp” was generated, modified and reformatted by White House officials in several administrations, and is designed to provide vetting officials with information about topics that, in the past, have led to scandals. As a prophylactic screening mechanism, the 86 Supp provides somewhat fragmented information, and the requested information overlaps with other disclosure forms, therefore requiring extra care to make sure information is consistently reported across forms. Moreover, the questions in the 86 Supp are, in some cases, not well-drafted, with undefined terms and unstated assumptions. These questions should be read in the context of past scandals that are reflected in the particular section of the 86 Supp. See Appendix A for the most current version of the 86 Supplement.

6.1 Positions and Former Positions

6.1.1 Current Practice

Precedent
The 86 Supp (Question 1S. [for “Supplement]” Part a) asks for detailed information about positions and former positions with organizations and companies, and therefore overlaps with the disclosure required in other documents, including in the 278, Schedule C, Part I. Therefore, this question should be completed at the same time, with the same information.

6.2 Positions with Potential Conflicts

6.2.1 Current Practice

Precedent
Question 1S. Part b) in the 86 Supp asks (among other things) if the filer now holds any positions that will create a conflict in a future executive branch position. Because all presidential appointees must terminate their outside positions before government service begins, “position conflicts” will be resolved prior to

federal service. As with a number of the responses, the filer might be able to use standardized language for the response to this question. For example, a response that states: “I do not believe that any of my current positions will present a conflict or an appearance of conflict, and any such potential conflicts will be resolved in connection with my ethics agreement” may be appropriate.

6.3 Violation of Laws

6.3.1 Current Practice

Precedent

The violation-of-laws question (Question 3S) is an example of drafting problems in the 86 Supp. For purposes of responding to this question, it should be noted that the literal language of the question means that any criminal investigation targeting any business with which the filer “has been associated” would be responsive. For filers who have been employed by large companies, there will often be some violation of law in the history of the company (for example, an OSHA violation). If the filer knows of such a violation, of course, it should be disclosed. If not, an answer with standard language along the following lines has been accepted: “I have not been convicted of a violation of law. However, in the course of my career, businesses with which I have been associated may have been convicted of such violations. I am not, however, aware of any such specific violation.”

6.4 Investigations

6.4.1 Current Practice

Precedent

As with the immediately prior question, Question 4S is worded broadly, and could encompass any “investigation” (an undefined term) of any business or organization with which the filer “has been associated,” presumably because such investigation might cause embarrassment by association. If the filer has direct knowledge of any such investigation that might be publicly or otherwise known, of course, it should be specifically disclosed. However, in order to address the possibility of an investigation that is tangentially related to the filer, a standardized response to this question along the following lines has been accepted: “In the course of my career, I have been associated with a large number of companies or organizations, and some of these companies may have been subject to an investigation for possible violation of law. However, I have not been personally subject to any such investigation [and I do not know of any such investigation of any of the businesses with which I have been directly associated].”

6.5 Litigation

6.5.1 Current Practice

Precedent

A thorough search of public litigation databases should be conducted in connection with Question 5S.

6.6 Political Committees and Issues

6.6.1 Bush I Administration

Precedent

The breadth of Question 7S. Part a) has been expanded to include the following clause: “or have been identified in a public way with a particular organization, candidate or issue.” Although the origin of this question is unclear, it may encompass a wide range of political issues.

6.6.2 Current Practice

Case Study

The Senate voted 47-52 to reject President Obama’s nomination of Debo Adegbile to head the Justice Department’s Civil Rights Division. During his time as litigation director of the NAACP Legal Defense Fund, Adegbile was involved in filing an amicus brief for controversial figure Mumia Abu-Jamal. Abu-Jamal had been convicted of murdering a Philadelphia police officer in 1981.

Authority
Weisman, J., & Shear, M. D. Democrats in Senate Reject Pick by Obama. "The New York Times." (March 5, 2015). Retrieved from http://www.nytimes.com/2014/03/06/us/politics/senate-rejects-obama-nominee-linked-to-abu-jamal-case.html?_r=0

6.7 Lobbyist Activities

6.7.1 Current Practice

Precedent
Question 7S. Part b) seeks information not only with respect to LDA-type registration by the filer, but also whether the filer has "acted" as a lobbyist, asking the filer to indicate whether he has been carrying on lobbying-type activities, which could raise risks to the filer, if the filer has not registered.

6.8 Discriminatory Social Clubs

6.8.1 Carter Administration

Precedent
Following the controversy over Griffin Bell's nomination as attorney general, the 86 Supp included a question about a nominee's membership (or past membership) in a social club that discriminates on racial, religious, or other grounds. Bell had been a member of at least one such club and faced heavy questioning about it during his Senate confirmation.

Authority
Lyons, Patrick J. Griffen Bell, Ex-Attorney General, Dies at 90. "The New York Times" (January 5, 2009). Retrieved from http://www.nytimes.com/2009/01/06/washington/06bell.html?_r=0

6.8.2 Clinton Administration

Case Study
Webster Hubbell's nomination for associate attorney general, the number three position in the Department of Justice, sparked controversy because of his membership in a previously whites-only country club.

Authority
ackett, M. Clinton Nominee In The Rough Over Golf Club. "Chicago Tribune." (May 13, 1993). Retrieved from http://articles.chicagotribune.com/1993-05-13/news/9305130234_1_webster-hubbell-howard-reed-private-social-club

6.8.3 Current Practice

Precedent
Policies against membership in discriminatory social clubs continue to be enforced through Question 8S. Question 8S in its current form asks whether the filer has ever belonged to a social club that ever discriminated. Question 8S covers discriminatory policies that existed before filer was a member of the social club and even if filer was never aware of such past policies.

It appears that the principal focus concerning discriminatory organizations is on golf and social clubs, not other types of social and other organizations. For example, it does not appear that membership in college fraternities or sororities, which all had policies of discriminating on grounds of gender, might be disqualifying. Also unclear is whether membership in certain national fraternities and sororities, many of which had policies of racial discrimination before the 1960s, would be disqualifying.

6.9 Immigration Issues

The scope of Question 9S. Part a) concerning immigration (in contrast to the broad scope of other questions in the 86 Supp), is to individuals who are "currently living with you."

6.9.1 Bush II Administration

Precedent
For the most part, immigration status of household workers was not considered to be a disqualifying issue in the vetting process.

Case Study

Authority
Linda Chavez was nominated to be secretary of the Department of Labor in 2001 by incoming president George W. Bush. She withdrew after political attention surrounding an illegal immigrant from Guatemala who had lived with Chavez in the early 1990s had become a distraction to the administration.
Fournier, R., Chavez Withdraws As Labor Nominee, "The Washington Post" (January 9, 2001) Retrieved from http://www.washingtonpost.com/wp-srv/aponline/20010109/aponline172303_000.htm

6.9.2 Current Practice

Precedent
Focus on hiring undocumented workers as a threshold issue for vetting increased during the course of the Obama administration.

Independent Contractor Exception.
The vetting standard may differ depending upon whether the household workers are employees or independent contractors.

Accountant Letter.
In order to substantiate the status of a household worker as an independent contractor for both tax (see below) and immigration purposes, vetting attorneys will often request a letter from the filer's tax accountant or other professional advisor.

Authority
Committee on Finance U.S. Senate. Nominations of Dr. Lael Brainard, Mary John Miller, and Charles Collyns. (November 20, 2009). Retrieved from http://permanent.access.gpo.gov/gpo9505/659342.pdf

6.10 Nanny Tax Issues

6.10.1 Current Practice

Precedent
The "nanny tax" question (Question 9S. Part b)) asks about adults that the filer "employ[s]" (not "have employed"). The present tense used in this question appears to limit the inquiry to current service providers.

6.11 Embarrassment to the President

6.11.1 Current Practice

Precedent
The answer to Question 10S. is generally "no" and any responses other than "no" likely would be discussed directly with White House counsel staff in the initial vetting process, rather than included in detail in the form.

VII. OUTSIDE EMPLOYMENT & ACTIVITIES

7.1 Outside Income

7.1.1 Bush I Administration

Precedent
The Bush I administration restricted outside income for various types of appointees. Restriction was proposed by a presidential committee appointed to address the political fall-out from ethical scandals involving former Reagan administration officials.

Authority
Executive Order 12674 (Apr. 12, 1989) modified by Executive Order 12731 (Oct. 17, 1990)

G. Calvin Mackenzie with Michael Hafken, Scandal Proof: Do Ethics Laws Make Government Ethical? 50 (2002).

7.1.2 Current Practice

Precedent
The definition of "earned income" for purposes of the outside earned income limitation is similar to the definition used for purposes of the tax on self-employment income under section 1401 et seq. of the tax code, and also parallels the difference between earned income and investment income under now repealed provisions of the tax code that provided for differential tax rates depending upon character of income. Questions were raised during the administration of George W. Bush concerning whether "line 1" income for partnership tax return purposes (i.e., line 1 on the K-1 Form issued to partners to indicate the partner's share of business or operating income of the partnership) would be considered earned income, especially if the executive branch employee were a general partner of the partnership (even if the employee provided no services to the partnership), but these questions were not definitively answered.

It appears that line 1 income allocated to limited partners of a limited partnership, or, by extension, holders of LLC membership interests in a limited liability company, where no services are provided to the limited partnership or the LLC, should not be treated as earned income for these purposes, even though it might be earned income for purposes of self-employment tax.

7.2 Participation in Non-profit Organizations in Official Capacity

7.2.1 Current Practice

Precedent
Government employees may participate in particular matters that affect the financial interests of nonprofits in which they serve or seek to serve in their official government capacity. (N.B. this does not apply to government officials serving in nonprofits in their personal capacity). The exemption applies only to the prohibition of 18 U.S.C. § 208(a). Additionally, the employee still requires permission from a supervisor to be permitted to participate in a nonprofit in an official capacity. The employee remains subject to government ethics rules and other applicable statutes while serving in the nonprofit organization. Nonprofits for this purpose are those organizations that receive tax-exempt status under section 501 of the Internal Revenue Code. If an entity does not qualify, a section 208(b) (1) waiver is still an option.

Authority
5 C.F.R. § 2640.203(m). LA-13-05: 18 U.S.C. § 208(b) (2) Exemption for Official Participation in Nonprofit Organizations.

Shaub, W. M. U.S. Office of Government Ethics - LA-13-05: 18 U.S.C. § 208(b)(2) Exemption for Official Participation in Nonprofit Organizations. (April 9, 2013). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/CE1F23774940E1E685257E96005FBEFB/$FILE/9182469fbb6f484db9fc9c2e6dc837a92.pdf

7.3 Stock Purchases in IPOs

7.3.1 Current Practice

Precedent
Section 12 of the STOCK Act prohibits certain government employees from "purchasing" securities that are subject to an IPO if "done in a manner that is not available to members of the public generally." According to the Securities and Exchange Commission, an employee who has acquired stock from a former private employer will not be considered to have "purchased" the stock if, during her time in the Government, her

shares are automatically converted to common stock when that company goes public. Additionally, in the similar case of an employee exercising a pre-existing right to convert previously held shares to common stock, the employee would not be considered to have "purchased" the stock. Importantly, neither agency ethics officials nor the OGE will be able to advise employees concerning the application of this section of the STOCK Act because it is a matter of securities law.

Authority
LA-14-02: Participation in Initial Public Offerings by Certain Employees
Apol, D. J. U.S. Office of Government Ethics - LA-14-02: Participation in Initial Public Offerings by Certain Employees. (March 7, 2014). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/B8EAA52BEB5BB52685257E96005FBF06/$FILE/29e20ef2652d455e9242bd382b0acd882.pdf

7.4 Future Employment Restrictions

7.4.1 Current Practice

Precedent
E.O. 13490 Sec. 1, Paragraph 4. section 207(c) prohibits executive branch employees from making, "with intent to influence any communication to, or appearance before any officer or employee of the department or agency in which such person served . . . on behalf of any other person (except the United States), in connection with any matter on which such person seeks official action by any officer or employee of such department or agency . . . ."

Case Study
Capricia Marshall needed a waiver to serve on the Board of Trustees of the Blair House Restoration Fund, which has a close relationship with Marshall's former government employer, the State Department.

Authority
Visek, R. C. Limited Waiver Pursuant To Section 3 of Executive Order 13490. (November 5, 2014). Retrieved from https://www.oge.gov/Web/OGE.nsf/All%20Documents/EA288A272973FB1D85257EBC0066955E/$FILE/50cc0deef2aa440c82fb0c3f395c77bb2.pdf

VIII. TAXES

8.1 Nanny Taxes

8.1.1 Clinton Administration

Precedent
Prior to 1994, if the taxpayer paid a nanny, babysitter, or other household worker more than $50 in a calendar quarter, the taxpayer had to withhold FICA contributions from that person's wages and remit those taxes along with share of FICA tax to the IRS using IRS Form 942. Following Zoe Baird's failed nomination for Attorney General, in which it was revealed Baird hired undocumented workers and failed to pay their FICA contributions, Congress adopted the nanny tax law, raising the amount that triggered FICA payments from $50 a quarter to $1,000 a year and indexing it to inflation, and creating a new annual tax filing on Form 1040, Schedule H.

Authority
Block, J., New Nanny Law Still Unforgiving on Unpaid Taxes. "Chicago Tribune." (August 13, 1995). Retrieved from http://articles.chicagotribune.com/1995-08-13/business/9508130273_1_social-security-taxes-household-employee-unpaid-taxes

8.1.2 Bush II Administration

Precedent
Curing nanny tax liability. During the administration of George W. Bush, many nominees and appointees came forward with potential nanny tax liabilities. For the most part, the administration adopted the position that if such tax liabilities were fully satisfied by filing amended returns and paying all back taxes, interest

and penalties, prior liability for unpaid taxes for household workers (including gardeners, housekeepers, and childcare workers) would not prevent a nomination from proceeding, with the exception of nominations for positions in the Treasury Department (because of its authority over tax collection).

Case Study
The Linda Chavez and Bernard Kerik nominations for Secretary of Labor and Secretary of Homeland Security respectively were withdrawn, in part, for failing to pay the post-1994 nanny tax, although in the case of Kerik, it was not clear whether the nanny tax issue was the actual reason for his withdrawal; in the case of Chavez, immigration issues were at least as important as tax issues in the withdrawal.

Authority
Lipton, E and W. K. Rashbaum. Kerik Pulls Out as Bush Nominee for Homeland Security Job. "The New York Times." (December 11, 2004). Retrieved from http://www.nytimes.com/2004/12/11/politics/kerik-pulls-out-as-bush-nominee-for-homeland-security-job.html?_r=0

8.1.3 Current Practice

Precedent
Nanny Tax Rule: Liability for nanny taxes and other taxes of household employees has become a "threshold" question in initial due diligence. The Obama administration put significant emphasis on worker classification issues. On the independent contractor issue, support in the form of an "accountant letter" is often sufficient to provide support.

Case Study
Nancy Killefer withdrew her candidacy to become Chief Performance Officer (within the Office of Management and Budget) in part because she failed to pay a nanny tax.

Authority
Kravitz, D. 'Nanny' Problems Ensnare Another Obama Pick. "Washington Post Investigations." (February 3, 2009). Retrieved from http://voices.washingtonpost.com/washingtonpostinvestigations/2009/02/tax_problems_ensnare_another_o.html?wprss=washingtonpostinvestigations

8.2 Personal Income Taxes

8.2.1 Current Practice

Precedent
Income Tax Errors. A focus on avoiding income tax errors, or anticipating questions that might be raised concerning individual income tax returns became a principal part of the review of the nominations, especially in connection with nominations under the jurisdiction of the Senate Finance Committee. A full-time detailee from the Internal Revenue Service reviewed individual tax returns.

Amended returns.
Normally, if inadvertent errors are identified in already-filed tax returns, a taxpayer has the legal right to correct those errors by filing an amended return (Form 1040X).

Case Study
Tom Daschle withdrew his nomination for Secretary of Health and Human Services because of numerous tax problems, including his failure to pay income taxes on a luxury car and driver.

Authority
U.S. Senate Committee on Finance. Finance Committee Releases Memo Regarding Brainard Nomination. "The United States Senate Committee on Finance." (November 18, 2009). Retrieved from http://www.finance.senate.gov/newsroom/chairman/release/?id=8a7c3c5a-6da6-4b67-8084-2102e2518bc7
Hulse, C., & Pear, R. Daschle Apologizes Over Taxes as Allies Give Support. "The New York Times." (February 2, 2009). Retrieved from http://www.nytimes.com/2009/02/03/us/politics/03daschle.html

8.3 Non-income Taxes and Tax Liens

8.3.1 Current Practice

Case Study
During Timothy Geithner's nomination for Secretary of the Treasury, the Senate Finance Committee disclosed that Mr. Geithner failed to pay over $30,000 in FICA taxes from his time with the International Monetary Fund (IMF). The IMF is a tax-exempt organization and it does not withhold taxes for Social Security and Medicare although U.S. citizens must still pay the FICA taxes.

Authority
Bernard, T. S. Geithner's Tax Mistake Was Honest, Experts Say. "The New York Times." (January 14, 2009). Retrieved from http://www.nytimes.com/2009/01/15/us/politics/15tax.html?_r=0

8.4 Foreign Bank Account Reporting

8.4.1 Current Practice

Precedent
New emphasis on foreign bank account reporting and international transparency.

8.5 Tax Penalties

8.5.1 Current Practice

Precedent
Since 2009, tax "penalties" have taken on special significance, especially for nominations under the jurisdiction of the Senate Finance Committee.

8.6 Substantiation of Charitable Contributions

8.6.1 Current Practice

Precedent
A nominee who receives income from an honorarium cannot avoid tax liability by assigning it to a charity and must both substantiate the contribution and pay taxes on the payment of the honorarium.

Case Study
U.S. Trade Representative nominee Ronald Kirk asked for his speaking engagement honoraria to be given to his alma mater to fulfill a scholarship fund pledge.

IX. DRUG AND ALCOHOL ISSUES

9.1 General Policy Issues

Current drug use is rarely an issue in the vetting process. Prior drug use is subject to a complex analysis that appears to vary depending upon elapsed time (how long since the last use of drugs), types of drugs (essentially, marijuana versus other drugs), frequency of use (including specific timelines), etc., all in context of rapid changes in societal norms and generational views of drug use.

9.2 Forms and Reporting

Detailed reporting concerning drug use is provided in SF-86, section 23 ("illegal use of drugs and drug activity") and a "yes" answer to any question in this section will likely elicit further questions. In addition, certain preliminary questionnaires separate from the SF-86 used as screening mechanisms have asked for information about "illegal" use of drugs. For all such purposes, illegality is determined by federal, not state or local, law (which have in many cases either eliminated statutes prohibiting the use of certain drugs, or have sharply reduce the penalties for such use, e.g., to a misdemeanor or an administrative fine). Illegality presumably could include use of certain prescription drugs without proper prescriptions, and depressants and tranquilizers are listed as types of drugs or controlled substances in section 23 of SF-86.

9.3 Past Illegal Drug Use

9.3.1 Reagan Administration

Case Study
In November 1987, Judge Douglas H. Ginsburg withdrew his nomination to the Supreme Court after publicly disclosing that he used marijuana before becoming a judge, and while a professor at Harvard law school. Subsequent FBI investigations indicated the possibility that individuals with knowledge of Prof. Ginsburg's past drug use had lied to investigators in the course of his security investigation. As a result of the Ginsburg matter, at the end of the Reagan administration, and during the administration of Pres. George H. W. Bush, in a change in procedure, all candidates for positions such as federal judges were to be asked directly if they had used illegal drugs.

Authority
Shenon, P., F.B.I. Study Hints Some Lied to Hide Ginsburg Drug Use. "The New York Times." (January 13, 1988). Retrieved from http://www.nytimes.com/1988/01/13/us/fbi-study-hints-some-lied-to-hide-ginsburg-drug-use.html

9.3.2 Bush I Administration

Precedent
Initially, applicants for senior positions were disqualified for any illegal drug use in the past 15 years. This restriction was later reduced to 10 years, apparently in recognition that some drug use was common among Baby Boomers.

Authority
Barr, S., & White, B. Agencies Vary in Handling Drug Issue. "Washington Post." (August 23, 1999). Retrieved from http://www.washingtonpost.com/wp-srv/politics/campaigns/wh2000/stories/frules082399.htm

9.3.3 Clinton Administration

Precedent
The White House asked appointees to disclose all illegal drug use going back to age 18. There were no automatic disqualifications based on past drug use. Each appointee was judged on a case-by-case basis.

Authority
Barr, S., & White, B. Agencies Vary in Handling Drug Issue. "Washington Post." (August 23, 1999). Retrieved from http://www.washingtonpost.com/wp-srv/politics/campaigns/wh2000/stories/frules082399.htm

9.3.4 Bush II Administration

Precedent
In 2006, the State Department's website published adjudicative guidelines for determining eligibility for access to classified information. Under the section titled "Guideline H: Drug Involvement," the department outlined potentially disqualifying activities. These included: drug abuse (defined as "the illegal use of a drug or use of a legal drug in a manner that deviates from approved medical direction"), testing positive for illegal drug use, illegal drug or drug paraphernalia possession (including cultivation, processing, manufacture, purchase, sale, or distribution), diagnosis by a qualified medical professional of drug abuse/dependence, evaluation of drug abuse/dependence by a licensed clinical social worker who is a staff member of a recognized drug treatment program, failure to successfully complete a properly prescribed drug treatment program, any illegal drug use after being granted a security clearance, expressed intent to continue illegal drug use, or failure to clearly and convincingly commit to discontinue drug use.

The department also published a list of mitigating factors. These included: infrequent use, a significant amount of time having been passed after the behavior, a demonstrated intent not to abuse drugs in the future, abuse of prescribed drugs occurring "after a severe or prolonged illness," and the completion of a prescribed drug treatment program with a favorable prognosis from the appropriate medical professional.

Authority
U.S. Department of State. Adjudicative Guidelines for Determining Eligibility for Access to Classified Information. (February 3, 2006). Retrieved from http://www.state.gov/m/ds/clearances/60321.htm
See also 32 C.FR. § 147.9 “Guideline H—Drug Involvement,” (outlining similar guidelines for the Department of Defense).

9.3.5 Current Practice

Precedent
Legalization of Marijuana. The fact that a number of states have legalized, or at least de-criminalized the recreational use of marijuana has not limited the analysis of the drug use issue in connection with vetting.

9.4 Alcohol Use

9.4.1 Bush II Administration

Precedent
The 2008 version of the national security questionnaire added questions related to the effect of alcohol on an applicant’s employment within the past seven or ten years, depending on the applicable reporting period for the particular nominee or appointee.

In 2006, the State Department posted adjudicative guidelines concerning alcohol on its website. Under the section titled “Guideline G: Alcohol Consumption,” the department outlined potentially disqualifying activities. These included: “alcohol-related incidents” of concern (e.g. DWI’s or domestic abuse), “alcohol-related incidents at work,” “habitual or binge consumption of alcohol to the point of impaired judgment,” a proper medical diagnosis of alcohol abuse/dependence, a proper evaluation of alcohol abuse/dependence as part of an alcohol treatment program, relapse after said diagnosis, or “failure to follow any court order regarding alcohol education, evaluation, treatment, or abstinence.”

Mitigating factors included: infrequent behavior, a significant amount of time having passed since the behavior, the presence of unusual circumstances, acknowledgment of and proper steps to treat alcohol abuse, current participation and progress in a counseling/treatment program with no history of relapse, and the successful completion of counseling/rehabilitation along with a demonstrated “clear and established pattern of modified consumption or abstinence” and a favorable prognosis from a qualified medical professional or “a licensed clinical social worker who is a staff member of a recognized alcohol treatment program.”

Authority
U.S. Department of State. Adjudicative Guidelines for Determining Eligibility for Access to Classified Information. (February 3, 2006). Retrieved from http://www.state.gov/m/ds/clearances/60321.htm
See also 32 C.FR. § 147.9 “Guideline G—Alcohol Consumption.” (Outlining similar guidelines for the Department of Defense).

9.5 Driving While Intoxicated (DWI)

9.5.1 General Policy Issues

In some cases, arrests for DWI are “expunged” if certain procedures are followed (remedial training, etc.). However, questions regarding arrests on the SF-86 still require disclosure of such arrest records, and therefore, regardless of whether DWI offenses are no longer contained in official police records, they must be fully disclosed and described in the SF-86.

X. MEDICAL ISSUES (INCLUDING MENTAL HEALTH)

10.1.1 Bush II Administration

Precedent
State Department Adjudicative Guidelines. The State Department’s website explains in a section titled “Guideline I: Psychological Conditions” that a negative inference should not “be raised solely on the basis

of seeking mental health counseling" and lists a number of causes for concern, which, among others, may include failure "to follow treatment advice related to a diagnosed emotional, mental, or personality condition, e.g. failure to take prescribed medication." Mitigating factors may include demonstrated compliance with treatment, voluntary entry into counseling or treatment "with a favorable prognosis," a mental health professional's recent opinion that the individual's condition is no longer a problem, the condition having been a temporary one, and the lack of indications of a current problem.

Authority
U.S. Department of State. Adjudicative Guidelines for Determining Eligibility for Access to Classified Information. (February 3, 2006). Retrieved from http://www.state.gov/m/ds/clearances/60321.htm
See also 32 C.FR. § 147.11 "Guideline I—Emotional, mental, and personality disorders." (Outlining similar guidelines for the Department of Defense).

10.1.2 Current Practice

Precedent
Attention to mental health issues has been reflected in evolution of national security questionnaire. The question (now in section 21 of SF-86) reflects the historic view that mental health treatment might be a disqualifying condition for a security clearance. In order to avoid automatic disqualification for mental health treatment, the national security questionnaire has added various "exemptions," which essentially disregard psychiatric and other mental health treatment in selected categories, presumably because these are deemed not to be indicative of security risks. Thus, for example, the mental health portion of the 2008 form SF-86 provides an additional exemption for any counseling or treatment "strictly related to adjustments from service in a military combat environment." The mental health section of the 2010 version of SF-86 included an exemption for anyone who sought or received treatment as a victim of sexual assault. Since the 2010 version of the SF-86 has been issued, various defense and intelligence officials have stressed the mental health exemptions available to returning servicemen and survivors of sexual assault, noting the importance of seeking treatment to the long term health and well-being of both categories of people.

Precedent
In light of the above discussion concerning military survivors of sexual assault, section 21 of SF-86 now includes the following instruction: "Victims of sexual assault who have consulted with the health care professional regarding an emotional or mental health condition during this period strictly in relation to the sexual assault are instructed to answer 'No.'

Authority
Memorandum from Secretary of Defense Leon Panetta for Secretaries of the Military Departments et al. (Sept. 4, 2012); Memorandum from Undersecretary of Defense James Clapper for Secretaries of the Military Departments et al. (Nov. 20, 2009); Memorandum from National Intelligence Director James Clapper for Distribution (Apr. 12, 2013).

Miller, M. W. Revised Instructions for Completing Question 21, Standard Form 86, "Questionnaire for National Security Positions." United States Office of Personnel Management. (April 19, 2013). Retrieved from https://www.opm.gov/investigations/background-investigations/federal-investigations-notices/2013/fin13-02.pdf

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