

UNDERSTANDING THE BASICS OF

PUBLIC SERVICE ETHICS

Personal Financial Gain Laws

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UNDERSTANDING THE BASICS OF PUBLIC SERVICE ETHICS: Personal Financial Gain Laws

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Personal Financial Gain Laws

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About This Guide

What Is an “Ethics” Law?

Defining the subgroup of laws that constitute “ethics” laws is an imprecise undertaking. For those involved in public service, “ethics laws” tend to be those laws whose central purpose is to protect the public’s *trust* in its public institutions and those who serve in them. Trustworthiness is a key ethical value.¹

Many of these ethics laws are *prohibitions*: they forbid certain actions that would undermine the public’s trust that decisions are being made to benefit the public’s interests (as opposed to the personal or political interests of the decision-maker). Making decisions in the public’s interest is also a key *responsibility* of public service (responsibility is another key ethical value).² Prohibitions deter betrayals of the public’s trust by creating penalties for such betrayals.

Laws against misusing public resources are a form of prohibitory law, as are laws that prevent a decision-maker from being involved in a decision if the decision-maker has a real or perceived conflict of interest. Laws against bribery or other forms of “pay to play” are another important ethics law prohibition.

Other ethics laws simply require *transparency*: they provide the public and the media with information on how the public’s business is being conducted, who is receiving campaign contributions and gifts from whom, and what kinds of financial interests a public official has. With transparency laws, the public judges whether a public official or group of public officials is acting in a trustworthy

A key goal of this guide is to alert local officials as to when to ask for legal advice on how these laws apply in a particular situation.

fashion—typically as part of the elections process. Transparency laws also encourage trustworthy behavior by reminding public officials that their actions will likely be scrutinized and judged.

Other ethics laws require that public agency decision-making processes meet minimum standards of *fairness*. Fairness is another key ethical value.³

Because public trust and confidence is vital to the strength of a democratic system, ethics laws sometimes set very high standards for public official conduct. Even so, it is important to keep in mind that these standards are only *minimum* standards: it is simply not possible or practical to write laws that prevent all actions that might diminish the public's trust. For this reason, the laws should be viewed as a floor for conduct, not a ceiling. Just because a given course of conduct is legal does not mean that it is ethical (or the public will perceive it as such).

Understanding Ethics Laws

California has a complex set of ethics laws to guide local officials in their service to their communities. How does the well-intentioned local official keep track of them all?

Keeping four core principles in mind helps:

- Public officials may not use their offices for **personal financial gain**.
- Holding public office does not entitle one to **personal advantages and perks**.
- **Transparency** is an important element of public service.
- Merit-based decision-making based on **fair processes** produces the best results for the public.

This guide focuses on laws relating to public officials and **personal financial gain**. These laws are both complex and sometimes counter-intuitive. A key goal of this guide is to alert local officials as to when to ask for legal advice on how these laws apply in a particular situation.

▶ A COMPLETE LIBRARY ON PUBLIC SERVICE ETHICS ISSUES

As part of its *Understanding the Basics of Public Service Ethics*, the Institute for Local Government offers California local officials a series of resources designed to help them meet both the law's and the public's expectations for public service:

- *Personal Financial Gain Laws*
- *Perk Issues, Including Compensation, Use of Public Resources and Gifts*
- *Transparency Laws*
- *Fair Process Laws and Merit-Based Decision-Making*
- *Promoting Personal and Organizational Ethics*

In addition, as part of its “Everyday Ethics” series, the Institute regularly analyzes situations local officials face from both a legal and ethical perspective.

To access these resources, visit www.ca-ilg.org/trust.

Receiving Special Favors or Money for Official Actions

Basic Rules

Perhaps the most extreme form of using one's office for financial gain is graft. Graft involves using one's public position to get money or anything else of value. Examples of graft include bribery and extortion.

A bribe involves conferring a benefit on a public official to influence a person's vote, opinion or action.⁴ Asking for a bribe is illegal, of course, but so is receiving one or agreeing to receive one.⁵ Under the state's criminal laws, a "bribe" includes anything of value; it also includes receiving "advantages." The advantage can be a future one and need not involve the payment of money.⁶ The federal law definition of bribery is even broader.⁷

Extortion involves, among other things, getting something from someone by the wrongful use of one's public position.⁸ For example, a public official may not demand money in return for the performance of his or her official duties.⁹ This includes demanding campaign contributions in return for action in one's official capacity.

Public officials are also forbidden from receiving a reward for appointing someone to public office or permitting someone to perform the duties of their offices.¹⁰



Penalties

State Law Penalties

Bribery

Receiving or agreeing to receive a bribe is a criminal act, punishable by a combination of prison time, fines and losing one's office and being forever disqualified from holding public office.¹¹ The specified prison sentence is two to four years in state prison.

The fines vary according to whether the bribe was actually received. If it was, the fine is a minimum of \$2,000 up to either 1) \$10,000 or 2) double the amount of the bribe, whichever is greater. If a bribe

was not actually received, there still is a fine between \$2,000 and \$10,000. The specified prison sentence is two to four years in state prison.

Those who offer bribes also face penalties. Those who bribe a member of a legislative body of a city, county, school district or other special district face two to four years in state prison.¹²

Extortion

Extortion by public officials is a misdemeanor.¹³ Misdemeanors are punishable by up to six months in county jail, a fine of up to \$1,000 or both.¹⁴ Extortion can also be the basis for a grand jury to initiate removal-from-office proceedings for official misconduct.¹⁵

DON'T COUNT ON A CODE OF SILENCE

Faced with the temptation of receiving a bribe, it can be easy to underestimate the chances of being caught, let alone successfully prosecuted. Fortunately, bribery is fairly rare, which may lead one to mistakenly assume prosecutors never find out about bribery.

In some instances, prosecutors learn about illicit activities from informants from within an agency. In other instances, those who believe they have been asked for a bribe will turn the asking officials in. Sometimes, observers will notice that a public official seems to have more resources than before and start asking questions.

The media views itself as a key watchdog on such issues, of course.

Unfortunately, some officials discount the likelihood of getting caught and prosecuted. They figure that everyone involved in illicit activities will have a strong incentive to keep quiet. What they don't realize is that prosecutors can offer powerful incentives to those involved to testify against others in exchange for a reduced penalty.

Appointing Someone to Office

An official who receives payment or favors for making an appointment faces the following punishments: forfeiture of office, disqualification from ever holding public office again and a fine of up to \$10,000.¹⁶

Federal Penalties

If an agency receives more than \$10,000 in federal monies an official could find him or herself subject to federal prosecution if the amount at stake (for example, a bribe) exceeds \$5,000.¹⁷ The

penalty for bribery under federal law is 1) a fine of up to three times the amount of the bribe or \$250,000 (whichever is greater), 2) up to 10 years imprisonment, or 3) both.¹⁸

Bribery, extortion, or embezzlement can also be basis of a federal income tax evasion charge. Federal prosecutors may treat money that an official receives through illicit means as income to the official. If the official fails to report this income at tax time (which of course, most don't), the official becomes subject to an action for income tax evasion.

▶ MAKING A FEDERAL CASE OUT OF CORRUPTION:

Honest Services Fraud

Under federal wire and mail fraud laws, the public has the right to the “honest services” of public officials.¹⁹ The basic concept is that a public official owes a duty of loyalty and honesty to the public—similar to a trustee or fiduciary.²⁰ That duty is violated when a public official makes a decision that is not motivated by his or her constituents’ interests but instead by his or her personal interests.²¹

A clear example is when an official receives a personal financial gain as the result of his or her public service. Examples include bribes and kickbacks (for example, receiving money back from proceeds paid to a company that does business with a public entity).

Sometimes violation of a state law is the basis of an “honest services” fraud claim (in addition to other charges, like income tax evasion). However, the courts have also held that such claims can also be based on common or judge-made law concepts relating to a public official’s fiduciary duties to his or her constituents.²²

The potential penalties for federal fraud are steep. The maximum penalty for being guilty of wire and/or mail fraud includes a jail term of up to 20 years and a \$250,000 fine.²³

For more information, see the Everyday Ethics for Local Officials column “Making a Federal Case Out of Corruption” (see www.ca-ilg.org/fedcase).

Income tax evasion carries with it a possible five-year prison term and a fine of up to \$100,000.²⁴ In addition, prosecutors can require the defendant to pay for the costs of prosecution (in addition to one's own costs associated with defending against the prosecution).²⁵ The sometimes-related crime of filing a false tax return is punishable by a maximum three-year prison term and a fine of up to \$100,000 (along with the costs of prosecution).²⁶

A court can also order a convicted official to pay restitution to the agency in the amount of the money or advantage received (or loss to the agency) as the result of criminal misuse of the official's position.²⁷

▶ IF I GET INTO TROUBLE, CAN THE AGENCY PAY MY DEFENSE?

Don't count on it. To provide a defense in a criminal action, for example, the agency must find that:

1. The criminal action or proceeding is brought on account of an act or omission in the official's service to the public entity;
2. Such defense would be in the best interests of the public entity; and
3. The individual's actions were in good faith, without actual malice and in the apparent interests of the public entity.²⁸

If the issue is claims a public official misused his or her office for personal gain, it may be particularly difficult for the agency to make the second finding, which is that the actions were in the apparent interests of the public entity. Moreover, even if the agency could make these findings, it is not required to. Indeed, there may be strong political pressures not to.

Similarly, an agency may refuse to provide a defense in a civil action if it finds the actions in question related to corruption or fraud.²⁹ Also, public agencies are not responsible for damage awards designed to punish or make an example of someone.³⁰

Note that, in these situations, the agency's attorney is not an individual public official's attorney, with attendant protections for attorney-client confidences. The agency attorney's obligations are to the entity as a whole – not to any one official in that agency.³¹

Disqualification Based on Economic Interests Under the Political Reform Act

Basic Rules

The voters have created an across-the-board, bright line rule: public officials may not participate in governmental decisions affecting their economic interests.

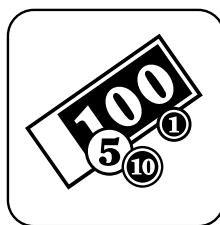
The rule is designed to have public officials avoid putting themselves in the position of choosing between advancing the public's interests and their own financial interests. That would be a potential conflict of interest.

This does not mean there is anything corrupt or dishonest about having a disqualifying conflict of interest. It typically means that a public official has a personal life, with all the financial entanglements that life can involve. The key is to be aware when one's economic interests are implicated by a public agency decision, so one can step aside from the decision-making process. This way, there is no question about whether one's personal interests affected the decision-making process in any way.

The rule is that a public official may not make, participate in, or influence a governmental decision that will have a reasonably foreseeable and material financial effect on the official, the official's immediate family, or any of the official's economic interests.³²

Economic interests include real property, sources of income, business entities in which a public official has an investment or holds a management position, and donors of gifts. See pages 13 to 15 for more information.

Note the breadth of the prohibition: it does not just apply to voting, but the entire process leading up to voting. This means conversations with fellow officials and staff are also against the law if one has a conflict of interest. Also, there may be even more restrictive local requirements.



DISCLOSURE OF CONFIDENTIAL INFORMATION

State law also makes disclosure of certain kinds of confidential information for personal financial gain (as defined) a misdemeanor.³³ The restriction applies to public officers and employees. Confidential information means information not subject to disclosure under the Public Records Act information which may not be disclosed by statute, regulation or rule.

Note the breadth of the prohibition: it does not just apply to voting, but the entire process leading up to voting.

The process for determining whether an official must disqualify oneself is described on page 13.

Note that disqualified officials do not count toward the quorum.³⁴

Penalties

A refusal to disqualify oneself is punishable by a variety of sanctions, depending on the severity of the violation and the degree of intent to violate the law that enforcement entities are able to demonstrate.³⁵

POLITICAL REFORM ACT PENALTIES

Criminal Sanctions

A knowing or willful violation of these requirements is a misdemeanor.³⁶ A person convicted of a misdemeanor under the Political Reform Act may not be a candidate for elective office for four years following the conviction.³⁷ Such a conviction may also create an immediate loss of office under the theory the official violated his or her official duties³⁸ or create a basis for a grand jury to initiate proceedings for removal on the theory failure to disclose constitutes willful or corrupt misconduct in office.³⁹ Jail time is also a possibility.⁴⁰

Civil Sanctions

District attorneys, some city attorneys, the Fair Political Practices Commission or a member of the public can bring an action to prevent the official from violating the law.⁴¹

If the action is brought by a member of the public, the violator may have to reimburse the costs of the litigation, including reasonable attorney's fees.⁴²

Administrative Fines

Violations may result in civil and criminal penalties. In addition, the Fair Political Practices Commission may impose administrative penalties. The administrative penalty for violation of the Political Reform Act is a fine of up to \$5,000 per violation.⁴³

▶ IMPRECISE TERMINOLOGY: ABSTENTIONS, DISQUALIFICATIONS AND RECUSALS

The terms “abstention,” “disqualification” and “recusal” are sometimes used interchangeably when describing an official’s decision to step aside from the decision-making process. The important thing is to be clear on *why* a decision-maker is stepping aside.

There are instances in which a public official *voluntarily* chooses not to participate in a decision. The official may know it will be difficult to put personal interests aside and make a decision based solely on the public’s interest. Or, the official may worry the public will perceive the official cannot put personal interests aside even if the official knows the he or she can.

The decision to voluntarily not participate in the decision-making process can involve two conflicting values:

- 1) One’s responsibility to participate in decision-making; and
- 2) One’s responsibility to preserve the public’s trust in the decision-making process.

Both responsibilities are important, of course. Because of this, deciding not to participate should not be viewed as a way of avoiding difficult decisions.

By contrast, when someone has a disqualifying conflict of interest, one does not have a choice. The law prohibits that individual from participating in a decision—even if the official believes he or she can be fair. There is no choice; the law presumes the public will doubt a person’s ability to be fair. This is an example of avoiding the appearance of impropriety as well as the potential for actual impropriety.

RESOURCES FOR FURTHER INFORMATION

For more information, see the Everyday Ethics for Local Officials columns

- “Deciding When *Not* to Participate in an Agency Decision: Abstentions and Disqualifications” (see www.ca-ilg.org/abstentions) and
- “Property Ownership in Your Jurisdiction” (see www.ca-ilg.org/owningproperty).

Effect on Agency and Those Affected by Agency’s Decision

When a disqualified official participates in a decision, it can also void the decision.⁴⁴ This can have serious consequences for those affected by the decision as well as the public agency. If someone is encouraging an official to participate in spite of a disqualifying interest, consider pointing out the costs that would occur if the agency’s decision has to be undone—not to mention the legal consequences for the official.

Typically it is wise to err on the side of caution when there is a question regarding the appropriateness of an official’s participation in a matter. When in doubt, sit a decision out.

GETTING ADVICE AND STAYING OUT OF TROUBLE ON POLITICAL REFORM ACT ISSUES

Public officials should get advice on how these laws apply as early in the process as possible — as soon as a conflict of interest is even a possibility.

Early consultation allows an attorney to analyze all of the facts involved and the relevant law. Even though the analysis is laid out in eight steps, each step has various rules and Fair Political Practices Commission guidelines associated with it. As one seasoned local agency attorney has observed, the later in the process the consultation occurs, the more likely the advice will be that disqualification is required to make sure the official stays out of trouble.

Does such advice protect an official against a Fair Political Practices Commission enforcement action? No. Only a formal opinion or formal advice letter from the Fair Political Practices Commission will protect a public official if someone argues that a violation of the Political Reform Act has occurred. Receiving such advice from the Commission takes time (typically at least 21 days for advice letters, for example) — another good reason to raise the conflict issue as early as possible.

▶ THE EIGHT STEPS OF A DISQUALIFICATION ANALYSIS

The process of determining when an official is disqualified from participating in a decision is a very complex one. There are statutes, regulations and interpretive opinions that flesh out each aspect of the basic prohibition.

To organize the analysis, the Fair Political Practices Commission has adopted an eight-step procedure for identifying when one must disqualify oneself from participating in a matter. Although it is useful to be aware of the general outlines of the process, the analysis with all its twists and turns is best undertaken by agency attorneys and the Fair Political Practices Commission staff—particularly since the rules are not necessarily logical or intuitive.

1. Are you a public official within the meaning of the rules?
2. Are you making, participating in making, or influencing a governmental decision?
3. Do you have an economic interest in the decision?
4. Is your economic interest directly or indirectly involved in the decision?
5. Are the financial impacts on your economic interests considered important (material) enough to trigger a conflict of interest?
6. Is it reasonably foreseeable (substantially likely) the governmental decision will result in one or more of the materiality standards being met for one or more of your economic interests?
7. Is the decision's effect on your economic interest different from the effect on the public generally?
8. Even if you have a disqualifying conflict of interest, is your participation legally required?

Special Issues

What Kinds of Economic Interests Are a Concern?

A public official is in the best position to focus on step 3: Does an official have an economic interest in a particular decision? There are a number of different ways to have an economic interest in a decision:

- **Sources of Income.** Receiving \$500 or more in income from one source (including any income received from a business, nonprofit organization, government agency, or individual) within twelve months prior to the decision creates an economic interest. “Sources of income” includes a community property interest in a spouse or domestic partner’s⁴⁵ income, but not separate property income.⁴⁶ Additionally,

if someone promises an official \$500 or more twelve months prior to the decision, that person or entity promising the money is a source of income.⁴⁷

- **Personal Finances.** An official has an economic interest in the official's expenses, income, assets or liabilities and those of the official's immediate family (spouse or domestic partner⁴⁸ and dependent children).⁴⁹
- **Real Property.** An interest in real property when the interest is worth \$2,000 or more creates an economic interest. The interest may be held by the official, the official's spouse or domestic partner⁵⁰ (even as separate property) and children or anyone acting on their behalf. Real property interests can also be created through leaseholds, options and security or mortgage interests in property.⁵¹
- **Investments.** An economic interest is created if the official, the official's spouse or domestic partner⁵² (even as separate property) or dependent children or anyone acting on their behalf has created an investment worth \$2,000 or more in a business

entity (even if the official does not receive income from the business).⁵³

- **Business Employment or Management.** If the official serves as a director, officer or partner, trustee, employee or otherwise serves in a management position in a company, an economic interest is created.⁵⁴ Note this does not apply to a member of the board of a nonprofit entity.
- **Related Businesses.** The official has an economic interest in a business that is the parent, subsidiary or is otherwise related to a business where the official:
 - Has a direct or indirect investment worth \$2000 or more; or
 - Is a director, officer, partner, trustee, employee, or manager.⁵⁵
- **Business-Owned Property.** A direct or indirect ownership interest in a business entity or trust that owns real property is another form of economic interest.⁵⁶
- **Loans.** A loan from someone (including someone who guarantees the loan) can create an economic interest unless the loan is from a commercial institution issued on the same terms as available to anyone in the public.⁵⁷

When in doubt, sit a decision out.

- **Gifts.** Receiving gifts totaling \$420 or more in a twelve-month period prior to the decision from any one person or organization may create an economic interest depending on the type of public official involved and whether the gift-giver is in the agency's jurisdiction.⁵⁸ Being promised a gift of \$420 or more within a twelve-month period prior to the decision can also create a disqualifying financial interest.⁵⁹ The \$420 limit is adjusted every few years to reflect changes in the cost of living. For more discussion of the gift issue, please see *Understanding the Basics of Public Service Ethics: Perks, Including Laws Relating to Compensation Issues, Use of Public Resources and Gifts*, page 23.

The timeline for determining whether an official has an economic interest is **twelve months before the decision** in question—not the calendar year.⁶⁰

If a public official thinks he or she has one of the economic interests described above, the next step is to consult with the agency attorney about the situation and how the Fair Political Practices Commission's eight-step analysis applies. One of the key purposes of the disclosure requirements is to enable the public to assess whether an official's financial interests may affect his or her decision-making. The disclosure requirements are discussed in further detail in *Understanding the Basics of Public Service Ethics: Transparency Laws* at page 3.

▶ REAL PROPERTY INTERESTS

Let's say an official has determined a decision may affect real property interests. The next step is whether that interest is directly (or indirectly) involved in the decision. This relates to step 4 of the eight-step disqualification process.



The Fair Political Practices Commission has endeavored to simplify the analysis by providing bright line rules. A real property interest is presumed directly involved in a decision if one of the following conditions is met:

1. The official's property is within 500 feet of the boundaries or proposed boundaries of the property that is the subject of the decision; or
2. The decision involves any of the following with respect to the official's property:
 - Zoning, rezoning, annexation, de-annexation, sale, purchase, lease, or inclusion in or exclusion from any local governmental subdivision of the property;
 - Issuance, denial or revocation of a license, permit or other land use entitlement;
 - Imposition, repeal or modification of any taxes or fees imposed on the official's property;
 - Designation of the survey area, selection of the project area, adoption of the preliminary plan, formation of a project area committee, certification of the environmental document or adoption of a redevelopment plan, or rescind or amend any of these decisions;⁶¹ or
 - Construction of, or improvements to, streets, water, sewer, storm drainage or similar facilities and the real property will receive new or improved services (excluding repairs, replacement or maintenance of existing services).⁶²

If a real property interest is directly involved in the decision, the effect is considered material (step 5 of the eight-step analysis) unless an official can prove the decision will not have any effect on the value of that property⁶³ or the "public generally" exception applies (step 7).⁶⁴

For more information on analyzing property-related financial interests, see the Everyday Ethics for Local Officials column "Property Ownership in Your Jurisdiction" (see www.ca-ilg.org/owningproperty).

What Happens if an Official is Disqualified?

General Rule

If an official is disqualified from participating on a specific agenda item under the conflict of interest rules established by the Political Reform Act, the official must:⁶⁵

- At the meeting, publicly identify the financial interest or potential conflict of interest in sufficient detail to be understood by the public.
- Not attempt to influence the decision in any way. This includes talking with colleagues or staff about the matter.
- Refrain from discussing or voting on the matter (ask for the item to be considered separately if it is on the consent calendar).

At the meeting, city council members, county supervisors, planning commissioners and top staff members who have conflicts of interest will typically need to leave the room when that matter is up for decision (unless the matter is on consent, in which case the official must declare the conflict and have the clerk record an abstention on that particular item). This may be a good practice for comparable officials at other local agencies as well.

Officials subject to the leave-the-room requirement⁶⁶ will also need to explain why they are disqualified from participating, based on the nature of the financial interest. For example:

- **Investment.** If the interest relates to an investment, provide the name of the business in which the investment is held.
- **Business Position.** If the interest relates to a business position, give a general description of the activity in which the business is engaged as well as the name of the business.

REDEVELOPMENT AGENCY PROJECT AREA COMMITTEES

Redevelopment agencies frequently decide to create “project area committees” to provide input on activities within a redevelopment project area. Under redevelopment law, certain types of interests must be represented on any project area committee, including residential owner occupants, residential tenants, business owners, and organizations within the proposed project area.⁶⁷ For purposes of the conflict of interest rules, project area committee members are considered public officials.⁶⁸

This creates a potentially sticky situation under the conflict of interest rules, which generally forbid individuals with an economic stake in a decision from participating in that decision. The analysis can become quite complex, as illustrated by a somewhat lengthy 2000 Fair Political Practices Commission advice letter that provides informal guidance to the members of a Southern California project area committee. The opinion goes through each of the eight steps (see page 13) and discusses the general application of the conflict of interest rules to each project area committee member given the nature of the member’s economic interest.⁶⁹

An element of this analysis is that state law says that project area committees must be constituted to represent these kinds of economic interests. The Attorney General has concluded in another context that the competing statutory schemes must be harmonized to the extent possible.⁷⁰

One way the Fair Political Practices Commission has done this is in its application of step 7 of the eight-step analysis. The Commission has determined that, in analyzing whether a decision’s impact on a project area committee member is different than the decision’s effect on the public generally, the definition of the relevant public is those persons within the project area who are similarly situated to the member of the project area committee.⁷¹ For example, if persons owning businesses are a significant segment of the project area, then business-owning project area committee members are disqualified only if the decision will have a material financial effect on their business that is distinguishable from other businesses in the project area. The Commission has adopted regulations that further define what constitutes a “significant segment.”⁷²

Does this analysis sound highly technical and complicated? It is. There are code sections, regulations and advice letters that all inform the analysis. Moreover, even if one could be aware of all these interpretative materials, it can be doubly challenging for a local official to objectively apply the legal standards when he or she may very much want to participate in a decision. This is why a major message of this guide is to encourage local officials to consult early and often with agency counsel whenever a personal economic interest may be affected by an agency’s decision.

- **Real Property.** If the interest relates to real property, supply the address or another indication of the location of the property (unless the property is the public official's principal or personal residence, in which case explain the property is a residence).
- **Income or Gifts.** If the interest relates to the receipt of income or gifts, then describe the source.
- **Personal Finances.** If the interest relates to a personal financial interest in the decision, then describe the expense, liability, asset or income affected.

Exceptions to the Leave-the-Room Requirement

There are limited exceptions that allow a disqualified official to remain in the room and participate in the discussion as a member of the public to represent himself or herself on matters related solely to the official's "personal interests." These include:

- Interests in real property wholly owned by the official or his or her immediate family;
- A business entity wholly owned by the official or his or her immediate family; and
- A business entity over which the official (or the official and his or her spouse or domestic partner⁷³) exercise sole direction and control.⁷⁴

Even though the law allows the public official to remain in the room when these interests are at stake, the public official may still wish to balance that option with the potential that the public may nonetheless perceive the official is improperly trying to influence his or her colleagues. Many officials balance their rights as individuals with their responsibility to maintain the public's trust in both their leadership and the agency that they serve by not remaining in the room.

Note on Closed Sessions

If a decision will be made in a closed session, an official with a conflict may not be present in the closed session during the discussion and decision. That official also may not obtain non-public information about the closed session.⁷⁵

Effect of Disqualification

The general rule is a majority of the membership of a body must be present in order for the decision-making body to conduct business—a concept known as a quorum.⁷⁶

For some kinds of agencies, a majority of the quorum is necessary for an item to pass, although there are special rules that apply to certain kinds of actions. Note, however, the rule is different for county boards of supervisors, community college boards and school boards, which generally require a majority vote of the entire membership of the board to act.⁷⁷

Those who are disqualified from participating in the decision are not counted toward the quorum.⁷⁸ However, those who abstain because of a pending question concerning a conflict of interest (for example, an elected official is waiting to receive an advice letter from the Fair Political Practices Commission) may be counted toward the quorum. This is because they have not yet been disqualified (typically their agency attorneys will recommend they abstain pending resolution of the conflict issue)⁷⁹.

RESOURCES FOR FURTHER INFORMATION

The Fair Political Practices Commission has produced “Can I Vote? An Overview of the Conflicts Laws,” which is available online at www.fppc.ca.gov. For specific questions, please contact the Fair Political Practices Commission or one’s public agency’s attorney.

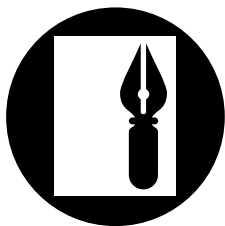
For more information, see the Everyday Ethics for Local Officials column “Using Public Office to Promote One’s Business Interests” (see www.ca-ilg.org/publicoffice).

Interests in Agency Contracts Barred

Basic Rules

State law strictly forbids public officials from having an economic interest in their agencies' contracts. In essence, this is a prohibition against self-dealing. This particular law has been traced back to the earliest days of California's statehood—to 1851.⁸⁰

This means that, *if elected officials have an interest in a contract being contemplated by their agency, the agency may not enter into the contract.* If a staff member has an interest in the contract, the staff member may not participate in any way in the contract negotiations. Contracts are broadly defined and include employment and a variety of other relationships.



Key things to keep in mind include the following.

- **Making a Contract.** The prohibition applies to preliminary discussions, negotiations, planning and solicitation of bids, as well as voting on the contract itself. This means the affected official can't be involved in those as well.
- **Disqualification Doesn't Fix the Problem.** When the prohibition applies, the agency may not enter into the contract in question. Members of the governing board of a local agency (including a board of supervisors, board of directors, city council or school board members) are *deemed* to have made any contract executed by the board, or any person or agency under its jurisdiction, *even if* officials disqualify themselves from participating in the contract.

- **Financial Interest.** A “financial interest” in a contract includes a direct or indirect financial interest. A direct financial interest is present when the official is the party contracting with the agency. An indirect financial interest involves an official who has a financial relationship with the contracting party or will receive some benefit from the making of the contract with the contracting party. It does not matter if the official’s financial interest is positively or negatively affected. This provision covers financial relationships that go beyond the official’s immediate family.

Officials will sometimes hear their agency counsel refer to this issue as a “section 1090 problem,” in reference to the Government Code section containing this prohibition. These restrictions on contracts are *in addition to* the restrictions of the Political Reform Act.

A key question to ask oneself in evaluating an agency’s contracts is: “will this contract affect my economic interests in any way?” If the answer is “yes,” speak with agency counsel immediately.

Penalties

The penalties for violating the prohibition against interests in contracts are severe.

Criminal Penalties

Willful violations are a felony and may be punished by fines of up to \$1,000, imprisonment and being disqualified from ever holding public office again.⁸¹

Effect on Contract

The contract also is “void,” which means the local agency does not have to pay for goods or services received under the contract.⁸² The agency may also seek repayment of amounts already paid.⁸³

WHAT IS THE THEORY OF NOT ALLOWING DISQUALIFICATION?

When the prohibition against interests in contracts applies, the agency may not enter into the contract, even if the official with the interest disqualifies him- or herself. Why? The theory seems to be decision-makers may be favorably influenced to award a contract to a colleague—perhaps with the expectation the favor may be returned in the future. The absolute prohibition guards against such a tendency toward what might be described as “you-scratch-my-back-I’ll-scratch-yours” dynamics within the agency.

Exceptions to Rules

There are limited exceptions to the general prohibition against interests in contracts.

Non-Interest Exception

Some potential interests in a contract are so small the Legislature has classified them as “non-interests” in a contract. One is when an official receives public services provided by the official’s board on the same terms that the services are provided to the general public. In other words, a member of a water district board may receive water service. In such cases, the official and the official’s agency may participate in the contract. State law provides a full list of exceptions.⁸⁴

Remote Interest Exception

A local agency may enter into a contract when an official has a “remote” interest.⁸⁵ Examples of remote interests include:

- Being an employee of the contracting party, if the contracting party has ten or more employees, the employee commenced his or her employment at least three years prior to initially assuming office, and certain other requirements are met; or
- Being a supplier of goods or services to the contracting party, when those goods or services have been supplied to the contracting party by the public official for at least five years prior to assuming office.⁸⁶

If the decision-maker qualifies as having a remote interest, the agency must then take these steps to stay on the right side of the law:

A key question to ask in evaluating an agency’s contracts is: “will this contract affect my economic interests in any way?” If the answer is “yes,” speak with agency counsel immediately.

► REDEVELOPMENT AGENCIES AND PROPERTY ACQUISITION

A variation on the prohibition of interests in contract theme is another statutory prohibition restricting how a redevelopment agency can acquire property from board members or officers. That statute says that the only way an agency can acquire such property is through eminent domain proceedings.⁸⁷

- The board or council member must disclose the financial interest to the board or council, and disqualify himself or herself from participating in all aspects of the decision;
- The disclosure must be noted in the official records of the board or council; and
- The board or council, after such disclosure, must approve, ratify or authorize the contract by a good faith vote of the remaining qualified members of the board or council.

Limited Rule of Necessity

Even if there is not an exception from the prohibition, the agency may still enter into a contract if the rule of necessity applies.⁸⁸ In general, this rule will allow an agency to acquire an essential supply or service. The rule also allows a public official to carry out essential duties of his or her office

where he or she is the only one who may legally act. Consult with agency counsel whether the intricacies of this rule may apply in any given situation.

Special Rule for School District Boards

The Education Code specifically allows school board members to vote on collective bargaining agreements and personnel matters that affect a class of employees to which a relative belongs.⁸⁹ Whether this rule also applies to domestic partners is not clear under the statute.

RESOURCES FOR FURTHER INFORMATION

For more information, see the following columns:

- “How Your Agency Counsel Should Advise You When Agency Contracts Represent a Conflict of Interest” (see www.ca-ilg.org/coi)
- “Securing Goods and Services: Contracting Issues” (see www.ca-ilg.org/procurement)

GETTING ADVICE AND STAYING OUT OF TROUBLE ON CONTRACT ISSUES

As with issues under the Political Reform Act, advice of counsel does *not* provide a defense in a criminal prosecution relating to unlawful interests in contracts.⁹⁰

Moreover, the Fair Political Practices Commission does not interpret and provide advice on Section 1090/contract issues.

The Attorney General will provide such advice, but only certain kinds of officials are entitled to ask the Attorney General for an opinion. In addition, the process can take months.

Restrictions on Property Ownership in Redevelopment Areas

Basic Rules

Special rules apply to redevelopment agency officials (including employees) and property ownership in redevelopment areas.

Existing Property Interests

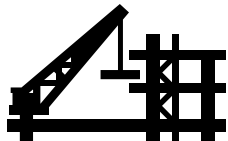
If an official has an interest in any property included within the project area, that officer or employee must immediately disclose that interest in writing to the agency and the legislative body. The disclosure must be included in the official minutes of the agency and the legislative body.⁹¹

New Interests

Officials who participate in policy-making activities for redevelopment agencies may not acquire interests in property in project areas.⁹²

Penalties

The statutory language could be clearer, but it appears that violation of these requirements constitutes misconduct in office.⁹³ The usual penalty for misconduct in office is removal from office based upon grand jury proceedings and then judicial pronouncement.⁹⁴



Exceptions

Property Acquisitions in Connection with Existing Business Activities

A public official who is a business owner may acquire an interest in property within a project area. However, the official must have owned a substantially equal interest to that being acquired for three years immediately preceding the selection of the project area.⁹⁵

Rental Agreements for Business Property

A redevelopment agency official may enter into a rental agreement or lease of business property only if four conditions are met.⁹⁶ Among other requirements, the agreement must have terms available to anyone else and must prohibit subletting. The property must be used for the official's principal business. The interest must also be disclosed.

Post Improvement Acquisition of Residential Property

A redevelopment agency official may acquire property for personal residential use within a project area. This acquisition must occur after the agency has certified all improvements to the property have been completed. The official must immediately disclose the acquisition in writing to the agency, recording the disclosure in the minutes. The official may not vote on any matters directly affecting the property.⁹⁷

RESOURCES FOR FURTHER INFORMATION

For more information, see the Everyday Ethics for Local Officials column "*Property Ownership in Your Jurisdiction*" (see www.ca-ilg.org/owningproperty).



Employment-Related Restrictions

Basic Rules

Another kind of “personal financial gain” law prohibits elected officials and top-level managers from, in essence, trading on the relationships developed in public service.

For example, top level officials who leave government service are prohibited from representing people for pay before their former agencies for one year after leaving their agency.⁹⁸ This is known as a “revolving door” restriction.

In addition, under the conflict of interest/disqualification rules, a public official may not influence agency decisions when the interests of a prospective employer are at stake.⁹⁹ The situation arises when an official is negotiating or has “any arrangement” concerning prospective employment with someone with business before the agency.

Penalties

These requirements are part of the Political Reform Act. Violations of the Act are punishable by a variety of sanctions, depending on the severity of the violation and the degree of intent to violate the law that enforcement entities are able to demonstrate.¹⁰⁰

RESOURCES FOR FURTHER INFORMATION

For more information, see *Revolving Door Restrictions for Local Officials* (see www.ca-ilg.org/revolvingdoor).



POLITICAL REFORM ACT PENALTIES

Criminal Sanctions

A knowing or willful violation of these requirements is a misdemeanor.¹⁰¹ A person convicted of a misdemeanor under the Political Reform Act may not be a candidate for elective office for four years following the conviction.¹⁰² Such a conviction may also create an immediate loss of office under the theory the official violated his or her official duties¹⁰³ or create a basis for a grand jury to initiate proceedings for removal on the theory failure to disclose constitutes willful or corrupt misconduct in office.¹⁰⁴ Jail time is also a possibility.¹⁰⁵

Civil Sanctions

District attorneys, some city attorneys, the Fair Political Practices Commission or a member of the public can bring an action to prevent the official from violating the law.¹⁰⁶

If the action is brought by a member of the public, the violator may have to reimburse the costs of the litigation, including reasonable attorney's fees.¹⁰⁷

Administrative Fines

Violations may result in civil and criminal penalties. In addition, the Fair Political Practices Commission may impose administrative penalties. The administrative penalty for violation of the Political Reform Act is a fine of up to \$5,000 per violation.¹⁰⁸

▶ **WHEN AN EMPLOYEE RUNS FOR A SEAT ON THE GOVERNING BOARD**

State law says that, with a few exceptions, local agency employees must resign their employment before taking a seat on the governing board of their local agency.¹⁰⁹

This restriction applies to cities, counties, special districts and other public agencies and corporations.¹¹⁰ There are parallel restrictions for employees who run for school boards¹¹¹ and community college district governing boards.¹¹² All of the sections note that, if an employee refuses to resign, his or her position will automatically terminate upon being sworn into office on the governing board.¹¹³

These restrictions prevent the dual role conflicts associated with being both in the role of employee and employer.¹¹⁴

Endnotes

- 1 Rushworth M. Kidder, *How Good People Make Tough Choices* (Simon and Schuster, 1995).
- 2 *Id.*
- 3 *Id.*
- 4 Cal. Penal Code §§ 7 (definition number 6), 68(a).
- 5 *See* Cal. Penal Code §§ 68(a), 86.
- 6 *Id.* *See also* *People v. Anderson*, 75 Cal. App. 365, 242 P.2d 906 (1925).
- 7 *See* 18 U.S.C. § 201.
- 8 *See* Cal. Penal Code § 518.
- 9 *In re Shepard*, 161 Cal. 171 (1911) (in the context of removal-from-office proceedings for misconduct).
- 10 Cal. Penal Code § 74.
- 11 *See generally* Cal. Penal Code § 68(a).
- 12 *See* Cal. Penal Code § 85.
- 13 Cal. Penal Code § 521.
- 14 Cal. Penal Code § 19.
- 15 Cal. Gov't Code §§ 3060-3074.
- 16 Cal. Penal Code § 74.
- 17 18 U.S.C. § 666.
- 18 *See* 18 U.S.C. §§ 666 (specifying maximum 10-year prison term and fine “under this title”), 3571 (general fine for violating federal criminal laws).
- 19 18 U.S.C. §§ 1341 (mail fraud), 1343 (wire fraud), 1346 (honest services).
- 20 *U.S. v. Sawyer*, 239 F.3d 31, 39 (1st Cir. 2001) (finding sufficient evidence of guilt apart from proof of violation of state law).
- 21 *U.S. v. Lopez-Lukis*, 102 F.3d 1164, 1169 (11th Cir. 1997) (noting that effort to improperly control composition of decision-making body constituted an effort to deprive public of honest services); *McNally v. U.S.*, 483 U.S. 350 at 362-63 (Justice Stevens, dissenting).
- 22 *See U.S. v. Sawyer*, 239 F.3d 31, 47 (1st Cir. 2001).
- 23 18 U.S.C. §§ 1341 (“... shall be fined under this title or imprisoned not more than 20 years, or both.”), 1343 (“shall be fined under this title or imprisoned not more than 20 years, or both.”).
- 24 26 U.S.C. § 7201.
- 25 *Id.*
- 26 26 U.S.C. § 7206(1).
- 27 *U.S. v. Gaytan*, 342 F.3d 1010 (9th Cir. 2003).

- 28 See Cal. Gov't Code § 995.8. See also *Los Angeles Police Protective League v. City of Los Angeles*, 27 Cal. App. 4th 168, 32 Cal. Rptr. 2d 574 (1994) (finding city was not required to provide the defense of police officers accused of vandalism and conspiracy to commit vandalism).
- 29 See Cal. Gov't Code § 995.2 (public agency may refuse defense of civil action if, among other reasons, the agency finds the official acted because of "actual fraud, corruption or actual malice.") See also Cal. Gov't Code § 822.2 (immunity from liability for misrepresentation does not apply in instances of corruption).
- 30 See Cal. Gov't Code § 818.
- 31 California Rules of Professional Conduct for Lawyers, Rule 3-600(A); *Ward v. Superior Court*, 70 Cal. App. 3d 23, 138 Cal. Rptr. 532 (1977) (county counsel's client is county, not assessor in his individual capacity).
- 32 See Cal. Gov't Code §§ 87100 and following.
- 33 See Cal. Gov't Code § 1098.
- 34 2 Cal. Code Regs. § 18702.5(b)(3).
- 35 See generally Cal. Gov't Code §§ 91000 and following.
- 36 See Cal. Gov't Code § 91000(a).
- 37 See Cal. Gov't Code § 91002.
- 38 See Cal. Gov't Code § 1770(h) (providing a vacancy occurs upon conviction of a felony or of any offense involving a violation of official duties).
- 39 Cal. Gov't Code §§ 3060-3074 (providing for proceedings to be brought by the grand jury for removal from office).
- 40 See Cal. Penal Code § 19 (providing misdemeanors are punishable by imprisonment in county jail up to six months, a fine not exceeding \$2,000, or both).
- 41 Cal. Gov't Code §§ 83116, 91001(b), 91001.5, 91004, 91005.
- 42 Cal. Gov't Code § 91012.
- 43 Cal. Gov't Code § 83116.
- 44 See Cal. Gov't Code § 91003(b).
- 45 2 Cal. Code Regs. § 18229.
- 46 Cal. Gov't Code §§ 82030, 87103(c); 2 Cal. Code Regs. § 18703.3.
- 47 Cal. Gov't Code § 87103(c). See also *Larsen Advice Letter*, No. A-82-192.
- 48 2 Cal. Code Regs. § 18229.
- 49 2 Cal. Code Regs. § 18703.5.
- 50 2 Cal. Code Regs. § 18229.
- 51 See Cal. Gov't Code §§ 82033, 87103(b).
- 52 2 Cal. Code Regs. § 18229.
- 53 Cal. Gov't Code §§ 82034, 87103(a); 2 Cal. Code Regs. § 18703.1.
- 54 Cal. Gov't Code § 87103(d); 2 Cal. Code Regs. § 18703.1(b).
- 55 2 Cal. Code Regs. § 18703.1(c).

- 56 Cal. Gov't Code § 82033 (pro rata interest, if own 10 percent interest or greater).
- 57 Cal. Gov't Code § 82030(b)(8), (10).
- 58 Cal. Gov't Code § 82028, 87103(e), 2 Cal. Code Regs. § 18703.4. The amount is adjusted biennially pursuant to Government Code section 89503(f).
- 59 Cal. Gov't Code § 87103(e); 2 Cal. Code Regs. § 18703.4.
- 60 *Id.*
- 61 2 Cal. Code Regs. § 18704.2(a)(5).
- 62 *See* 2 Cal. Code Regs. § 18704.2.
- 63 2 Cal. Code Regs. § 18705.2.
- 64 2 Cal. Code Regs. § 18707.1.
- 65 *See* Cal. Gov't Code § 87105 and 2 Cal. Code Regs. § 18702.5.
- 66 2 Cal. Code Regs. § 18702.5(b)(1)(B).
- 67 *See* Cal. Health & Safety Code § 33385(c).
- 68 *In re Rotman*, 10 FPPC Op. 1 (1987).
- 69 *Gutierrez Advice Letter*, No. I-00-050 (2000).
- 70 82 Cal. Op. Att'y Gen. 126 (1999) (analyzing issue in context of Government Code section 1090 and prohibited interests in contracts).
- 71 *In re Rotman*, 10 FPPC Op. 1 (1987).
- 72 *See* 2 Cal. Code Regs. §§ 18707(b) 18707.1 and 18707.4.
- 73 2 Cal. Code Regs. § 18229.
- 74 2 Cal. Code Regs. §§ 18702.5(d)(3), 18702.4(b)(1).
- 75 *See* 2 Cal. Code Regs. § 18702.1(c). *See also* *Hamilton v. Town of Los Gatos*, 213 Cal. App. 3d 1050, 261 Cal. Rptr. 888 (1989).
- 76 *See* Cal. Gov't Code § 36810 (for general law cities). *See also* Cal. Civ. Proc. Code §§ 12 and 15.
- 77 *See* Cal. Gov't Code § 25005; Cal. Educ. Code §§ 35164 (K-12 districts), 72000(d)(3) (community college districts).
- 78 2 Cal. Code Regs. § 18702.5(b)(3) and *Farwell v. Town of Los Gatos*, 222 Cal. App. 3d 711, 271 Cal. Rptr. 825 (1990) (subsequently ordered not published). *See also* 62 Cal. Op. Att'y Gen. 698, 700 (1979).
- 79 *Id.*
- 80 California Attorney General, *Conflict of Interest* (2004) (available on the Attorney General's website at <http://ag.ca.gov/publications/coi.pdf>).
- 81 *See* Cal. Gov't Code § 1097.
- 82 *Thomson v. Call*, 38 Cal. 3d 633, 214 Cal. Rptr. 139 (1985).
- 83 *See* Cal. Gov't Code § 1092.
- 83 Cal. Health & Safety Code § 33393.
- 84 *See* Cal. Gov't Code § 1091.5.

- 85 See Cal. Gov't Code § 1091(a).
- 86 See Cal. Gov't Code § 1091(b).
- 87 Cal. Health & Safety Code § 33393.
- 88 See 70 Cal. Op. Att'y Gen. 45 (1987).
- 89 See Cal. Educ. Code § 35107(e).
- 90 *People v. Chacon*, 40 Cal. 4th 558, 53 Cal. Rptr. 3d 876 (2007).
- 91 Cal. Health & Safety Code § 33130(a).
- 92 *Id.*
- 93 See Cal. Health & Safety Code § 33130(a) (specifying failure to make disclosure constitutes misconduct).
- 94 Cal. Gov't Code §§ 3060-3074.
- 95 Cal. Health & Safety Code § 33130(b).
- 96 Cal. Health & Safety Code § 33130(c).
- 97 Cal. Health & Safety Code § 33130.5.
- 98 Cal. Gov't Code § 87406.3; 2 Cal. Code Regs. § 18746.3.
- 99 Cal. Gov't Code § 87407.
- 100 See generally Cal. Gov't Code §§ 91000 and following.
- 101 See Cal. Gov't Code § 91000(a).
- 102 See Cal. Gov't Code § 91002.
- 103 See Cal. Gov't Code § 1770(h) (providing a vacancy occurs upon conviction of a felony or of any offense involving a violation of official duties).
- 104 Cal. Gov't Code §§ 3060-3074 (providing for proceedings to be brought by the grand jury for removal from office).
- 105 See Cal. Penal Code § 19 (providing misdemeanors are punishable by imprisonment in county jail up to six months, a fine not exceeding \$2,000, or both).
- 106 Cal. Gov't Code §§ 83116, 91001(b), 91001.5, 91004, 91005.
- 107 Cal. Gov't Code § 91012.
- 108 Cal. Gov't Code § 83116.
- 109 Cal. Gov't Code § 53227(a).
- 110 Cal. Gov't Code § 53227.2(a).
- 111 Cal. Educ. Code § 35107(b)(1).
- 112 Cal. Educ. Code § 72103(b)(1).
- 113 Cal. Gov't Code § 53227(a); Cal. Educ. Code §§ 35107(b)(1) and 72103(b)(1).
- 114 *Board of Retirement of Kern County Employees' Retirement Association v. Bellino*, 126 Cal. App. 4th 781, 24 Cal. Rptr. 3d 384 (2005).

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General Websites

Fair Political Practices Commission

www.fppc.ca.gov/

Institute for Local Government

www.ca-ilg.org

Office of the Attorney General

<http://ag.ca.gov/>



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Personal Financial Gain

Fair Political Practices Commission

Can I Vote? A Basic Overview of Public Officials' Obligations under the Political Reform Act's Conflict-of-Interest Rules (revised 7/05) (www.fppc.ca.gov/index.html?id=37)

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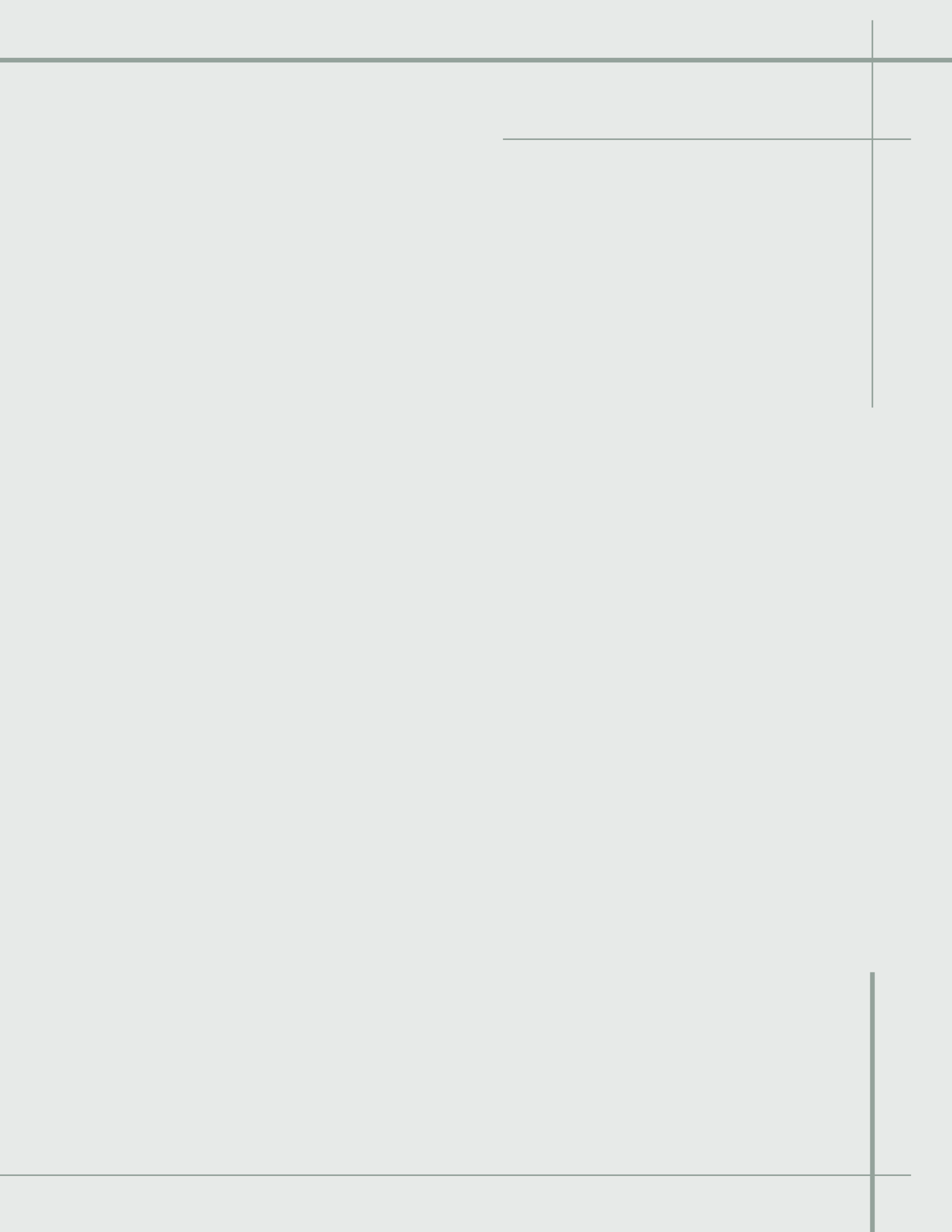
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