



Commitment to Nonprofit Causes and Public Service
AB 1234 Self-Study Materials
Part II — Conflict of Interest and Bias
One Hour of Self Study Credit

AB 1234 requires elected and appointed officials to take *two hours* of ethics training if they receive compensation for their service or are reimbursed for their expenses.¹ The ethics training requirement may also apply to agency employees designated by the agency's legislative body.² There are many ways to satisfy this requirement, including in-person training and self-study activities. **This self-study exercise is for officials who have completed a basic AB 1234 training course and wish to focus their subsequent training on specific areas of concern.**

Complete Part II for a second hour of AB 1234 self-study credit (or the second half of the minimum two-hour requirement) after completing Part I of the self-study exercise. To claim self study credit, log on to www.ca-ilg.org/AB1234selfstudy, print out and take the test, mail it to the address indicated with the \$25 processing fee. This fee covers grading the test, providing the correct answers (and explanations) and your proof of participation certificate for one hour of credit.

Scope of This Self-Study Exercise

These materials build on the content covered in Part I, which addressed legal and ethical issues associated with local officials being involved in nonprofit organizations in their communities. Specifically, these materials will focus on the following legal issues relating to such involvement:³

- The prohibition against public officials from having certain kinds of interests in contracts involving their agency;
- The requirement for public officials to step aside from decisions and the decision-making process if they have a financial interest in the decision; and
- Bias.

¹ Cal. Gov't Code § 53235(a), (b).

² Cal. Gov't Code § 53234(c).

³ Cal. Gov't Code § 53234(d)(3), (4).

For information on general ethical issues that arise when local officials are involved in nonprofit organizations in their communities and legal issues relating to gifts and travel payments from nonprofits, please see Part I of the self-study exercise.

Agency Financial Transactions with a Nonprofit

There are times when the nonprofit might have business with an agency. It may want to lease agency property or perform services for the agency. It may be seeking a donation to support its operations or an event (see April 2005 Everyday Ethics column on legal requirements relating to making donations to nonprofits).

It's important to note that there are two different laws an attorney will need to analyze for a public official if one these situations exists.

- One is a prohibition against public officials from having certain kinds of interests in contracts involving their agency. Attorneys call this a "Section 1090" issue after the section of the Government Code that contains the prohibition. The prohibition applies to public officials having a financial interest in a contract, but it is important to keep in mind that the definition of "financial interest" is very broad. So is the definition of "contract."
- The other is the provisions of the Political Reform Act that require public officials to step aside from decisions and the decision-making process if they have a financial interest in the decision. As with the prohibitions relating to contracts, the definition of "financial interest" is broad and the analysis of how the prohibition applies is quite complex. One aspect of this (whether receiving travel reimbursement from a nonprofit creates a disqualifying conflict of interest) was addressed in the preceding section.

The complexity of the analysis required under both laws is one of the reasons it is advisable to consult with your agency counsel as early as possible about these issues.

Section 1090/Contract Issues

Let's look more closely at the rules relating to contracts and nonprofits under Section 1090 of the Government Code. Section 1090 says that when a member of a decision-making body has a financial interest in a contract, the contract cannot occur.⁴ This means, for example, if an official has a business that does business with a nonprofit, they would need to speak with agency counsel about whether that financial relationship means that the local agency cannot enter into a contract with the nonprofit. Again, Section 1090 is a *prohibition* against decision-makers having an interest in contracts entered into by their agencies.

⁴ Cal. Gov't Code § 1090.

Putting aside business relationships, there are other kinds of relationships that officials can have with a nonprofit organization though. For example:

- **Nonprofit Officer.** An elected official could be an officer of the nonprofit (for example president) and the agency wishes to support the nonprofit;⁵
- **Nonprofit Employee.** An elected official or his or her spouse or partner could work for the nonprofit and the agency wishes to support the nonprofit;⁶

When an official has this kind of relationship with a nonprofit, typically what Section 1090 requires is that the official disclose the relationship and not participate in the decision-making relating to the nonprofit.

It's important to keep in mind that the "decision-making" process is not limited to the final vote on a matter. The public official needs to step aside from all steps leading up to the contract's approval, including preliminary discussions, negotiations, compromises, and planning.⁷ If the official doesn't and attempts to influence his or her colleagues, the official and the agency lose the benefit of the exception that allows the contract to be entered into.⁸

This requirement assures the public that no preferential treatment is occurring because of a nonprofit's connection with one or more public officials.

Note, however, that the official does *not* have to step aside if 1) he or she is a non-compensated officer of a tax exempt organization, and 2) one of the nonprofit's purposes is to support the functions of one's public agency.⁹ Also, just being a non-salaried member of the nonprofit doesn't require a public official to step aside from the decision-making process, all other things being equal.¹⁰ (For both of these exceptions to apply, the relationship needs to be disclosed in the agency's official records.) If however, there is a question about whether the official's relationship biases his or her decision, the official should speak with agency counsel about bias issues (see discussion below).

⁵ Cal. Gov't Code § 1091(b)(1); *see also* 89 Cal. Op. Att'y Gen. 258 (2006).

⁶ Cal. Gov't Code § 1091(b)(1); *see also* 89 Cal. Op. Att'y Gen. 258 (2006); 85 Cal. Op. Att'y Gen. 76 (2002).

⁷ *See Stigall v. City of Taft*, 58 Cal. 2d 565, 569-71, 25 Cal. Rptr. 441, 443-44 (1962).

⁸ *See* Cal. Gov't Code § 1091(c) ("This section is not applicable to any officer interested in a contract who influences or attempts to influence another member of the body or board of which he or she is a member to enter into the contract.").

⁹ Cal. Gov't Code § 1091.5(a)(8) (a noninterest includes "That of a noncompensated officer of a nonprofit, tax-exempt corporation, which, as one of its primary purposes, supports the functions of the body or board or to which the body or board has a legal obligation to give particular consideration, and provided further that this interest is noted in its official records"; an officer is "noncompensated" even if he or she receives expense reimbursements).

¹⁰ Cal. Gov't Code § 1091.5(a)(7) (defining nonprofit membership as a non-interest). *See also* Attorney General Conflicts of Interest (2004) at 90 ("...this office believes that the reference to "members" [in section 1091(b)(1)] refers to persons who constitute the membership of an organization rather than to person who serve as members of the Board of Directors of such organizations.")

About those Agency-Affiliated Nonprofits

In some situations, public agencies will create nonprofit organizations to support a worthwhile objective. Because of the close tie to the public agency's interests, public officials sometimes sit on the nonprofit's governing board. These situations can create complex legal and ethical issues, because the agency's and nonprofit's interests are so closely intertwined.

For example, what if an agency decides to use its authority when approving a lease, permit or other entitlement to require a contribution to the agency's nonprofit? The idea can make complete sense as apparently was the case in one northern California city. The nonprofit supported the operation of a national park. Most of the buildings and land within the park are owned and maintained by the city. One of the responsibilities of board members is fundraising.

The city's holdings in the park apparently included land on which a company sought to lease for aggregate mining. The lease required environmental review. The council member/board member had the idea that one of the mitigation measures for the mining operation could include a \$250,000 contribution to the nonprofit to support the operations of the park. The company apparently agreed to do so and the council member/board member asked staff to include the commitment in the conditions for project approval.

When asked if the council member/board member could participate in the decision-making relating to the lease, the Attorney General said he could. This was largely because the nonprofit was so closely affiliated with the city and therefore the council member did not have a direct or indirect financial interest in the lease.¹ The special statutory provisions for nonprofits formed to support public agency objectives played a strong role in the Attorney General's analysis.

What are some ideas on how to handle such a situation that might minimize questions about the dual role an elected official/board member might be playing? One is to consult with the management and legal staff about the contribution idea. For example, agency attorneys can analyze whether the law permits an agency to ask for this kind of gesture in this situation. For example, if this were a situation not involving city land, the city's requirements would need to satisfy the laws relating to permissible exactions.¹ Management staff can work with planning staff and get their input on the concept.

Getting buy-in on the merits of the approach (in an open meeting, of course) is another option. That helps make the idea to support the nonprofit's activities the agency's idea, as opposed to the individual elected official's.

Note that if the financial arrangement pre-dates the official's service on the decision-making body, there is no problem as long as there is no change or renewal of the arrangement.¹¹ As an example, the Attorney General said that a city could continue to lease property to a nonprofit organization even though a newly elected council member was a paid executive director for the nonprofit.¹²

What about being a member of the board of directors of a nonprofit? Attorneys disagree on the best interpretation of the statutory language. The Attorney General believes that being a board member is akin to being an officer, which means board members must step aside from the decision-making process when it comes to agency financial relationships with their nonprofits.¹³ Some attorneys believe that the concept of being an "officer" of a nonprofit is limited to those positions specified as "officers" under state law relating to nonprofits.¹⁴

The question in this situation is: on which side does one want to err? If the official participates in decision-making relating to the contract in violation of Section 1090, the contract may be void.¹⁵ There are other penalties for purposeful failure to disclose one's status, including loss of office.¹⁶ To be safe, nonprofit board members may want to disclose and step aside from the decision-making process until the appellate courts provide guidance on this point.

Political Reform Act/Financial Interest Issues

Part I of the self-study materials analyzed the issue of travel reimbursement and other kinds of things an official might receive from a nonprofit. Such gifts or income can be the basis for having to disqualify oneself from participating in public agency decisions involving the nonprofit. A threshold issue is whether the official has received reportable income of \$500 or more or reportable gifts of \$390 (2008 limit) or more within the 12 months preceding the decision. If so, the next series of questions either the Fair Political Practices Commission or agency counsel will analyze is whether it is reasonably

¹¹ See *City of Imperial Beach v. Bailey*, 103 Cal. App. 3d 191, 162 Cal. Rptr. 663 (4th Dist. 1980).

¹² 85 Cal. Op. Att'y Gen. 176 (2002).

¹³ Cal. Gov't Code § 1091(b)(1). See also Attorney General Conflicts of Interest (2004) at 90 ("...this office believes that the reference to "members" [in section 1091(b)(1)] refers to persons who constitute the membership of an organization rather than to person who serve as members of the Board of Directors of such organizations.")

¹⁴ Cal. Gov't Code §§ 1091(d) (specifying that willful failure to comply with the remote interest requirements is punishable under section 1097), 1097 (specifying that violations are "punishable by a fine of not more than one thousand dollars (\$1,000), or by imprisonment in the state prison, and is forever disqualified from holding any office in this state.").

¹⁵ See Cal. Gov't Code § 1091(c) ("This section is not applicable to any officer interested in a contract who influences or attempts to influence another member of the body or board of which he or she is a member to enter into the contract.")

¹⁶ Cal. Gov't Code §§ 1091(d) ("The willful failure of an officer to disclose the fact of his or her interest in a contract pursuant to this section is punishable as provided in Section 1097"), 1097 ("Every officer . . . who willfully violates any of such laws, is punishable by a fine of not more than one thousand dollars (\$1,000), or by imprisonment in the state prison, and is forever disqualified from holding any office in this state.").

foreseeable that a public official's decision would have a material financial effect on the nonprofit.¹⁷

Another issue to be aware of is whether an official does business with a nonprofit (for example, the nonprofit is a customer or client of a business that a public official is involved in). If so, a public official is well advised to speak with either the Fair Political Practices Commission or agency counsel about whether the disqualification requirements of the Political Reform Act apply.

For example, the Fair Political Practices Commission advised one public official not to participate in a decision regarding funding a nonprofit organization when his consulting firm provided services to the nonprofit. The Commission did the analysis required under the Political Reform Act. Key issues were whether the official had received income of \$500 or more from the nonprofit during the 12-month period before the decision and whether the financial effect of the decision met the materiality standards under the Act.¹⁸

The Fair Political Practices Commission also strongly advised the official to get advice from the Attorney General on how the prohibitions against having an interest in contracts apply.¹⁹

Bias Issues

In situations in which an official is applying an agency's policies to a specific situation (for example, in a permit or entitlement situation), another issue to be alert to is bias. Bias is a common law (judge-made law) concept. The issue to be concerned with is whether one's participation in a decision will subject the decision to invalidation.

Here's what happened to a planning commissioner. He ghost-wrote an article in a community newsletter that was critical of a project that ultimately came before the planning commission. When the project was turned down, the project proponent challenged the outspoken commissioner's participation in the decision. The theory was that the commissioner had pre-judged the merits of the application before the public hearing and couldn't fairly determine whether the project satisfied the city's requirements.²⁰ The appellate court agreed and set aside the decision.

When a decision-maker is applying existing policies to a specific situation, the decision-maker is acting more like a judge. In legal jargon, the official is acting in a quasi-judicial capacity. When one acts in this capacity, certain fair process requirements apply that

¹⁷ See Cal. Gov't Code §§ 87100 and following; 2 Cal. Code Regs. §§ 87200 and following. *See also* Pavlovich Advice Letter, FPPC No. A-94-391 (January 05, 1995).

¹⁸ See Mattas Opinion, FPPC Advice A-08-035 (April 08, 2008).

¹⁹ See Mattas Opinion, at n. 2.

²⁰ *Nasha L.L.C. v. City of Los Angeles*, 125 Cal. App. 4th 470, 483-842, 22 Cal. Rptr. 3d 772, 780-81 (2d Dist. 2004).

don't apply when a decision-maker is enacting those policies in the first place (and acting in a legislative capacity).

When an official is affiliated with a nonprofit organization that has strongly held views on a matter, the official should consult with agency counsel about whether the official will be acting in a quasi-judicial capacity. If so, the official should ask him or herself if he or she can truly be fair in applying the policies to the specific situation. If not, stepping aside satisfies one's legal and ethical obligations.

Even if one feels one can be fair, there's another step of the analysis in terms of whether the applicant and others will *perceive* the official as fair. Has the official made statements that suggest that the official has pre-judged the matter? Is there evidence that could be presented to a court to suggest bias? If so, it may be wise to step aside from the decision-making process.

For more information on bias and fair process requirements in adjudicative decision-making, see the Everyday Ethics column from October 2006 (available at www.ca-ilg.org/everydayethics).

Conclusion

When considering all the good and worthy things nonprofits contribute to a community, it can be very tempting to just think about those worthy *ends* and not think about the *means* used to achieve those ends. Some officials may even feel the-ends-justify-the-means.

It's important to know that ethics laws make it very clear that the means by which a public official pursues worthwhile ends matters. Using improper means can result in fines, jail time and other penalties, including the loss of one's standing in the community.

And of course, the laws just create the minimum standards for determining proper means. Merely satisfying the minimum requirements of the law may not satisfy either one's own or one's constituents' standards for what is appropriate. Dr. Martin Luther King Jr. encouraged everyone striving to make the world a better place to use means that are as pure as the end one seeks --- in other words, worthy ends never justify questionable means.

For more information on these rules, go to www.ca-ilg.org/ethicslaws. For more information on ethics principles, please visit www.ca-ilg.org/ethicsprinciples.