

CONFLICT OF INTERESTS IN CONTRACTS

GOVERNMENT CODE SECTION 1090 ET SEQ.

Contracts

Section 1090 prohibits an officer or employee from entering into or participating in making contracts in which they have a financial interest:

Members of the Legislature, state, county, district, judicial district, and city officers or employees shall not be financially interested in any *contract* made by them in their official capacity, or by any body or board of which they are members. Nor shall state, county, district, judicial district, and city officers or employees be purchasers at any sale or vendors at any purchase made by them in their official capacity.



Purpose/Remedies

- ▶ “every public officer be guided solely by the public interest, rather than by personal interest, when dealing with contracts in an official capacity.” (*Thomson v. Call* (1985) 38 Cal.3d 633, 650.) Section 1090 is intended “not only to strike at actual impropriety, but also to strike at the appearance of impropriety.” (*City of Imperial Beach v. Bailey* (1980) 103 Cal.App.3d 191, 197.)
- ▶ “Resulting in a substantial forfeiture, this remedy provides public officials with a strong incentive to avoid conflict of interest situations scrupulously.” (*Thomson, supra*, at p. 650.)
- ▶ A contract that violates Section 1090 is void when the terms of the proposed contract are demonstrably fair and equitable, or are plainly to the public entity’s advantage. (*Id.* at pp. 646-649.)
- ▶ Courts have recognized that Section 1090’s prohibition must be broadly construed and strictly enforced. (*Stigall v. City of Taft* (1962) 58 Cal.2d 565, 569-571.)



Guidance

- ▶ Case law
- ▶ Attorney General Opinions
- ▶ FPPC Advice Letters



Assembly Bill 1090



- ▶ Authorized FPPC to issue advice on Section 1090 as of January 1, 2014. The FPPC has currently issued over 150 advice letters pertaining to Section 1090.
- ▶ Prohibits advice where it relates to past conduct.
- ▶ Requires the FPPC to forward a copy of each advice request to the Attorney General's office and the appropriate district attorney's office. Any response by those entities must be forwarded to the requestor. The lack of a response does not mean those entities concur with FPPC's advice.
- ▶ Advice may be offered as evidence of good faith conduct by the requester in an enforcement proceeding.

Guidelines for Requesting 1090 Advice from the FPPC

- ▶ **Written, Signed Request.** A request must be in writing and signed by the public official or head of the agency authorized to make the request or counsel for a private party.
- ▶ **Clear Questions and Facts.** The request should set out the question to be answered as clearly as possible with enough description of the background and context of the question to allow a precise legal analysis to be prepared.
- ▶ **Additional Information.** The FPPC may contact the requester for additional information, or to discuss if revisions to the question are desirable. No advice will be issued until these requests are satisfied. Informal assistance will not be provided.
- ▶ **Timing.** The 21 day deadline that applies to advice under the Act does not apply to Section 1090 advice. We are unable to expedite advice requests regarding Section 1090.
- ▶ **Public Records.** All written requests for FPPC opinions and supplemental information are public documents.

Enforcement

- ▶ Authorizes the FPPC to commence an administrative action, or a civil action, for an alleged violation of Section 1090 but such action requires written authorization from the appropriate District Attorney.



Steps for Section 1090 Analysis

- ▶ 1. Is the official subject to the provisions of Section 1090?
- ▶ 2. Does the decision at issue involve a contract?
- ▶ 3. Is the official making or participating in making a contract?
- ▶ 4. Does the official have a financial interest in the contract?
- ▶ 5. Does a remote interest or noninterest exception apply?
- ▶ 6. Does the rule of necessity apply?

Step 1: Who does Section 1090 apply to?

- ▶ **Section 1090 applies to virtually all state and local officers, employees, and multi-member bodies, whether elected or appointed, at both the state and local level. Examples include: Council Member, County Employee, Contract City Attorney, etc.**



Step 1: Who does Section 1090 apply to?

1090 also applies to:

- ▶ **Most consultants & independent contractors.**
- ▶ **Members of advisory bodies who serve in advisory positions if they participate in the making of a contract through their advisory function.**
- ▶ **Persons in advisory positions to contracting agencies.**

Step 1: Who does Section 1090 apply to: Consultants

- ▶ Whether 1090 applies to a consultant depends on the extent of influence the consultant has on the agency's contracting decisions or whether the consultant otherwise acts in a capacity that demands the public trust.
 - ▶ Developing city's tax revenue policies.
 - ▶ Holding a position specified in the agency's conflict of interest code.
 - ▶ Performing a public function (energy company selecting suppliers, establishing the facets of a contract and negotiating contracts).
 - ▶ Developing the RFP that is the subject of the contract decision.
- *1090 not applicable to a subcontractor who played limited technical role and who is far removed from influencing agency's contracting decisions.

Step 2: Determine if it is a Contract

- ▶ **General Rule:** To determine whether a decision involves a contract, use general contract principles: mutual assent of parties and consideration.
- ▶ A broad interpretation of a contract is applied by courts. It includes all contracts, including oral contracts and purchases made outside the formal contract process.



If the Contract is not Ultimately Executed...

- ▶ **There is no Violation of Section 1090.**



Examples



- ▶ Development Agreements and Subdivision Improvement Agreements between a City and Developer are contracts (78 Ops.Cal.Atty.Gen. 230 (1995))
- ▶ Grants and donations are generally contracts (*People v. Honig* (1996) 48 Cal.App.4th 289)
- ▶ A civil service appointment is an employment contract (59 Ops.Cal.Atty.Gen. 223 (1960))
- ▶ The modification, extension or renegotiation of an existing contract constitutes the making of a contract (*City of Imperial Beach v. Bailey* (1980) 103 Cal.App.3d 191)

Scenario

- ▶ The Department of Technology is considering adopting regulations that would restrict access to the internet and adversely affect stocks owned by the Director of the agency. Does Section 1090 apply to this situation?



Answer



- No, Section 1090 does not apply to regulations. It only applies to contracts.

Step 3: Is the official making or participating in making a contract?

- ▶ Any participation in the development, negotiation or execution of a contract is sufficient for Section 1090.
- ▶ Participation where employee had the opportunity to and influenced the execution of the contract. (*People v. Sobel*, (1974) 40 Cal.App.3d 1046, 1052.)
- ▶ Any act involving preliminary discussions, negotiations, compromises, reasoning, planning, drawing of plans and specifications, and solicitation for bids. (*Millbrae Assn. for Residential Survival v. City of Millbrae* (1968) 262 Cal.App.2d 222, 237.)

Advisors

- ▶ Individuals in advisory positions can influence the development of a contract during these early stages of the contracting process even though they have no actual power to execute the final contract. (See, e.g., *Schaefer v. Bernstein* (1956) 140 Cal.App.2d 278, 291; *City Council v. McKinley* (1978) 80 Cal.App.3d 204.)

Example

- ▶ **Webber Advice Letter, No. A-15-127**



Presumption for Multi-Member Bodies



- ▶ Each board member or commissioner is presumed to have made any contract executed by the board or agency under its jurisdiction - even if they disqualified themselves from any participation in the contract. (*Thomson v. Call* (1985) 38 Cal3d 633, 645)
- ▶ *So....if one member of the body is financially interested in the contract, the contract cannot be made unless an exception applies, as discussed later.*

But...

- ▶ No Presumption where an employee has a financial interest.



Decisions to Modify etc.

- ▶ A decision to modify, extend, or renegotiate a contract constitutes involvement in the making of a contract under section 1090. (See, e.g., *City of Imperial Beach v. Bailey* (1980) 103 Cal.App.3d 191 [exercising a renewal option and adjusting the payment rates is making a contract within the meaning of Section 1090].)

Delegation does not avoid Section 1090

- ▶ A body such as a city council cannot avoid application of Section 1090 by *delegating* its contracting authority to another individual or body. (See 87 Ops.Cal.Atty.Gen. 9 (2004); 88 Ops.Cal.Atty.Gen. 122 (2005).)



Independent from Governing Body

- ▶ However, a governmental body may be able to avoid violating Section 1090 when the contract is made by government officials with independent contracting authority who do not have a conflict of interest. (See e.g., 81 Ops.Cal.Atty.Gen. 274 (1998); 57 Ops.Cal.Atty.Gen. 458 (1974).)



Step 4. Does the official have a financial interest in the contract?

- ▶ “However devious and winding the chain may be which connects the officer with the forbidden contract, if it can be followed and the connection made, the contract is void.” (*People v. Deysher* (1934) 2 Cal2d 141, 146)



Step 4: Interests

- ▶ Courts have applied the prohibition to include a broad range of interests. Including:
 - ▶ Employee, attorney, agent, or broker of a contracting party;
 - ▶ Supplier of services or goods to a contracting party;
 - ▶ Landlord or tenant of a contracting party; and,
 - ▶ Officer or employee of a nonprofit corporation that is a contracting party.

Financial Interest in Employer

- ▶ Employees have been found to have a financial interest in a contract that involves their employer, even where the contract would not result in a change in income or directly involve the employee, because an employee has an overall interest in the financial success of the firm and continued employment.



Spouse's Source of Income

- ▶ Generally, a member of a board or commission always has a financial interest in his or her spouse's source of income for purposes of Section 1090. (See 78 Ops.Cal.Atty.Gen. 230, 235 (1995).)



Exceptions to 1090

- ▶ Look to Remote/Noninterest Exceptions in Sections 1091 and 1091.5.

Remote Interests

- ▶ There are 17 “remote interests” in Section 1091
- ▶ Remote Interest exceptions apply only to members of multi-member bodies (e.g., city council, planning commission)
- ▶ Allow the board to make the contract if:
 - ▶ The conflicted officer discloses his or her financial interest in the contract to the public agency.
 - ▶ Such interest is noted in the entity’s official records.
 - ▶ The officer abstains from any participation in the making of the contract.

Section 1091(b)(1)

- ▶ (1) That of an *officer or employee of a nonprofit entity* exempt from taxation pursuant to Section 501(c)(3) of the Internal Revenue Code, pursuant to Section 501(c)(5) of the Internal Revenue Code, or a nonprofit corporation, except as provided in paragraph (8) of subdivision (a) of Section 1091.5.

Section 1091(b)(2)

That of an employee or agent of a private contracting party when all of the following are present:

- ▶ The private contracting party has 10 or more employees;
- ▶ The official/employee has been an employee or agent of that party for at least 3 years prior to the initial term in office;
- ▶ The officer owns less than 3% of the shares of stock of the contracting party;
- ▶ The employee or agent is not an officer or director of the contracting party, and;
- ▶ The employee or agent did not directly participate in formulating the bid of the contracting party. (1091(b)(2))

Section 1091(b)(5)

- ▶ A public official who is a landlord or tenant of a contracting party has a remote interest in the contracts of that party.



Section 1091(b)(8)

- ▶ An official only has a remote interest in a party that seeks to contract with the official's government agency when the official has been a supplier of goods or services to the contracting party for at least 5 years prior to the official's election or appointment to office.



Noninterests

- ▶ **Currently 15 noninterests listed under Section 1091.5**
- ▶ **More common noninterests include:**

Section 1091.5(a)(1)

- ▶ Corporate Ownership and income - The ownership of less than 3 percent of the shares of a corporation for profit, provided that the total annual income to him or her from dividends, including the value of stock dividends, from the corporation does not exceed 5 percent of his or her total annual income, and any other payments made to him or her by the corporation do not exceed 5 percent of his or her total annual income.

Section 1091.5(a)(3)

- ▶ **Public Services**—An official has a noninterest in the receipts of public services provided by his or her agency or board as long as he or she receives them in the same manner as if he or she were not a public official. (1091.5(a)(3))
- ▶ Will generally apply where provision of services involves no exercise of discretion by the public body that would allow favoritism

(1091.5(a)(6))

- ▶ Spouses—A non-interest exists when both spouses in a family are public officials. One spouse has a non-interest in the other's employment or holding office if it has existed for at least one year prior to his or her election or appointment to office.



(1091.5(a)(7))

- ▶ Unsalariated Members of Nonprofit Corporations—A non-interest exists when a public official is an unsalaried member of a non-profit corporation provided the official's interest is disclosed to the board at the time the contract is first considered and is noted in it's official records.

“Limited” Rule of Necessity

- ▶ The rule of necessity applies where public policy concerns authorize the contract and to ensure that essential government functions are performed despite the conflict of interest.



“Limited” Rule of Necessity

- ▶ It allows agencies to enter into a contract that that 1090 would otherwise prohibit under very narrow circumstances. Generally, the conflicted official should refrain from participation if possible.

“Limited” Rule of Necessity

- ▶ Rule of Necessity has been applied in two situations:
 - ▶ Procurement of essential supplies or services.
 - ▶ Non-procurement situations to carry out essential duties of the office when the official or board is the only one authorized to act.

“Limited” Rule of Necessity

- ▶ **Procurement of essential supplies or services.**
- ▶ **Emergency hardware supplies.**
 - ▶ (Ramos Advice Letter, No. A-14-105.)
- ▶ **Emergency nighttime services.**
 - ▶ (4 Ops. Cal.Atty.Gen 264 (1944).)
- ▶ **Emergency medications.**
 - ▶ (Headding Advice Letter, No. A-16-219.)



“Limited” Rule of Necessity

- ▶ **Non-procurement situations to carry out essential duties**
 - ▶ **Approval of claims or settlements.**
 - ▶ *(Devaney Advice Letter, A-14-142.)*
 - ▶ **Approval of contracts for repairs needed in the interest of public safety and risks to general public welfare.**
 - ▶ *(Dietrick Advice Letter, No. A-15-174.)*





The End

Thank you!