

March 25, 2014

Anne M. Russell
Interim City Attorney
City of Morro Bay
595 Harbor Street
Morro Bay, CA 93442

Re: Your Request for Advice
Our File No. C-14-033

Dear Ms. Russell:

This letter responds to your request for advice regarding the conflict-of-interest provisions under Government Code section 1090 et seq.¹ Because the Fair Political Practices Commission (the “Commission”) does not act as a finder of fact when it renders assistance (*In re Oglesby* (1975) 1 FPPC Ops. 71), this letter is based on the facts presented.

Please note that after forwarding your request to the Attorney General’s Office and the Santa Ana District Attorney’s Office, we did not receive a written response from either entity. (See Section 1097.1(c)(4).) Finally, we are required to advise you that the following advice is not admissible in a criminal proceeding against any individual other than the requestor. (See Section 1097.1(c)(5).)

QUESTION

Does Section 1090 prevent the Morro Bay City Council from modifying an existing lease with a corporation in which Morro Bay Councilmember George Leage has a financial interest?

CONCLUSION

Yes. Section 1090 prevents the City Council from modifying the existing lease with the corporation as long as Councilmember Leage is a member of the City Council.

¹ All further statutory references are to the Government Code, unless otherwise indicated.

FACTS

You are writing on behalf of George Leage, a member of the Morro Bay City Council. In addition to that position, Councilmember Leage is the President of the Great American Fish Company, Inc. (“GAFCO”). According to his Statement of Economic Interests (Form 700), he owns stock in GAFCO valued at over \$1 million, and receives annual income between \$10,000 and \$100,000 from the business. Prior to Councilmember Leage’s election to the Morro Bay City Council, GAFCO entered into a contract with the City to operate a restaurant, bar, fish market and slips for boats or any other uses subsequently approved for the premises by the City. Councilmember Leage now seeks to modify the contract with the City.

ANALYSIS

Section 1090 generally prohibits public officers, while acting in their official capacities, from making contracts in which they are financially interested. Section 1090 is concerned with financial interests, other than remote or minimal interests, that prevent public officials from exercising absolute loyalty and undivided allegiance in furthering the best interests of their agencies. (*Stigall v. Taft* (1962) 58 Cal.2d 565, 569.) 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.)

Under Section 1090, “the prohibited act is the making of a contract in which the official has a financial interest.” (*People v. Honig* (1996) 48 Cal.App.4th 289, 333.) A contract that violates Section 1090 is void. (*Thomson v. Call* (1985) 38 Cal.3d 633, 646.) The prohibition applies regardless of whether the terms of the contract are fair and equitable to all parties. (*Id.* at pp. 646-649.)

We employ the following six-step analysis to determine whether Councilmember Leage has a conflict of interest under Section 1090.

Step One: Is Councilmember Leage subject to the provisions of Section 1090?

Section 1090 provides, in part, that “[m]embers 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.” City councils and their members are plainly covered by this prohibition. (See, e.g., *Thomson, supra*, at p. 645; *City Council v. McKinley* (1978) 80 Cal.App.3d 204, 213.) Therefore, Councilmember Leage is subject to the provisions of Section 1090.

Step Two: Does the decision at issue involve a contract?

To determine whether a contract is involved in the decision, one may look to general principles of contract law (84 Ops.Cal.Atty.Gen. 34, 36 (2001);² 78 Ops.Cal.Atty.Gen. 230, 234 (1995)), while keeping in mind that “specific rules applicable to Sections 1090 and 1097 require that we view the transactions in a broad manner and avoid narrow and technical definitions of ‘contract.’” (*People v. Honig, supra*, at p. 351 citing *Stigall, supra*, at pp. 569, 571.) A decision to modify, extend or renegotiate a contract constitutes involvement in the making of a contract under Section 1090. (See *City of Imperial Beach, supra*, 103 Cal.App.3d at p. 197.)

Here, Councilmember Leage wishes to modify the existing contract between GAFCO and the City. Thus, the decision at issue necessarily involves a contract.

Step Three: Is Councilmember Leage making or participating in making a contract?

As a member of the Morro Bay City Council, which presumably must approve any modification to the existing lease, Councilmember Leage would be participating in the making of a contract.

Step Four: Does Councilmember Leage have a financial interest in the contract?

Under Section 1090, “the prohibited act is the making of a contract in which the official has a financial interest” (*People v. Honig, supra*, at p. 333), and officials are deemed to have a financial interest in a contract if they might profit from it in any way. (*Ibid.*) Although Section 1090 nowhere specifically defines the term “financial interest,” case law and Attorney General opinions state that prohibited financial interests may be indirect as well as direct, and may involve financial losses, or the possibility of losses, as well as the prospect of pecuniary gain. (*Thomson, supra*, at pp. 645, 651-652; see also *People v. Vallerga* (1977) 67 Cal.App.3d 847, 867, fn. 5; *Terry v. Bender* (1956) 143 Cal.App.2d 198, 207-208; *People v. Darby* (1952) 114 Cal.App.2d 412, 431-432; 85 Ops.Cal.Atty.Gen. 34, 36-38 (2002); 84 Ops.Cal.Atty.Gen. 158, 161-162 (2001).)

As President of the corporation seeking to modify its existing lease with the City, Councilmember Leage would have a financial interest in the contract.

Step Five: Does either a remote interest or non-interest exception apply?

As a general rule, when Section 1090 applies to one member of a governing body of a public entity, as here, the prohibition cannot be avoided by having the interested board member

² It is noteworthy to point out that opinions issued by the Attorney General’s Office are entitled to considerable weight (*California Assn. of Psychology Providers v. Rank* (1990) 51 Cal.3d 1, 17), especially where, as here, it has regularly provided advice concerning a particular area of law. (*Thorpe v. Long Beach Community College Dist.*, (2000) 83 Cal.App.4th 655, 662; *Freedom Newspapers, Inc. v. Orange County Employees Retirement System* (1993) 6 Cal.4th 821, 829.)

abstain; the entire governing body is precluded from entering into the contract. (*Thomson, supra*, at pp. 647-649; *Stigall, supra*, at p. 569; 86 Ops.Cal.Atty.Gen. 138, 139 (2003); 70 Ops.Cal.Atty.Gen. 45, 48 (1987).) However, the Legislature has created various statutory exceptions to Section 1090's prohibition where the financial interest involved is deemed to be a "remote interest," as defined in Section 1091, or a "noninterest," as defined in Section 1091.5.

If a "remote interest" is present, the contract may be made if (1) the officer in question discloses his or her financial interest in the contract to the public agency, (2) such interest is noted in the entity's official records, and (3) the officer abstains from any participation in the making of the contract. (Section 1091(a); 88 Ops.Cal.Atty.Gen. 106, 108 (2005); 83 Ops.Cal.Atty.Gen. 246, 248 (2000).) If a "noninterest" is present, the contract may be made without the officer's abstention, and generally a noninterest does not require disclosure. (*City of Vernon v. Central Basin Mun. Water Dist.* (1999) 69 Cal.App.4th 508, 514-515; 84 Ops.Cal.Atty.Gen. 158, 159-160 (2001).)

As stated above, GAFCO entered into a contract with the City to operate a restaurant, bar, fish market and slips for boats or any other approved uses on City property. Therefore, because GAFCO appears to be a tenant of the City, you question whether the landlord/tenant exceptions in either Section 1091 or 1091.5 would apply in this matter. We do not find them applicable. Under 1091(b)(5), an official has a remote interest in a contract where his or her relationship is "[t]hat of a landlord or tenant of the contracting party." Under Section 1091.5(a)(4), an official is deemed not interested in the subject contract if his or her interest constitutes:

[t]hat of a landlord or tenant of the contracting party if the contracting party is . . . any county or city of this state . . . unless the subject matter of the contract is the property in which the officer or employee has the interest as landlord or tenant in which event his or her interest shall be deemed a remote interest within the meaning of, and subject to, the provisions of Section 1091.

In either situation, Councilmember Leage would need to have a landlord/tenant relationship with *the contracting party* for the exception to even potentially apply. The issue then distills to a determination of who is *the contracting party* in the present matter. In all of the matters we have reviewed under Section 1090 where a councilmember has a financial interest, the "contracting party" is never the city that the councilmember represents. Instead, that term refers to the party who is attempting to contract with the city of the financially interested councilmember. (See, e.g., 84 Ops.Cal.Atty.Gen. 158 (2001) [councilmember had "landlord" relationship with the contracting party (architectural firm) who was seeking to contract with city]; 89 Ops.Cal.Atty.Gen. 193 (2006) [councilmember had "tenant" relationship with the contracting party (condominium developer) seeking to enter into a subdivision improvement agreement with the city].)

In the present matter, *the contracting party* is GAFCO, not the City of Morro Bay. As a result, the "tenant" relationship that GAFCO has with the City does not trigger the application of

the landlord/tenant exceptions under Section 1090. In order for either of those exceptions to potentially apply, Councilmember Leage would need to have a landlord/tenant relationship with GAFCO, which he does not. Rather, he is the President of GAFCO.

The conclusion that the landlord/tenant exceptions under Section 1090 do not apply in the present matter is bolstered by looking to other matters in virtually identical circumstances. For example, in *City of Imperial Beach v. Bailey* (1980) 103 Cal.App.3d 191, the city sought declaratory relief as to whether the city council could renew or extend the contract it had with a beach concession operator who was also a councilmember. (*Id.* at p. 193.) The contract, which had been in effect prior to the councilmember's election, involved the operation of a concession stand to sell bait, fishing tackle and refreshments on a municipal pier. (*Id.* at p. 194.) After her election to the city council, the councilmember sought to exercise the option to renew the contract, but the city refused on the ground that it was prohibited by Section 1090. (*Ibid.*)

The *Imperial Beach* Court held, in part, that the exercise of the option to renew would constitute the "making" of a contract in violation of Section 1090 as long as she was a member of the city council. (*Id.* at p. 197.) In doing so, it emphasized that although the councilmember's integrity was above reproach and she would have to decide whether to remain on the city council or as owner of the concession, the purpose of Section 1090 is "not only to strike at actual impropriety, but also to strike at the appearance of impropriety." (*Ibid.*; *City of Imperial Beach v. Bailey* (1980) 103 Cal.App.3d 191, 197.) Importantly, even though the councilmember had an apparent "tenant" relationship with the city, similar to the one here, the Court never analyzed or discussed either of the landlord/tenant exceptions under Section 1090.

In another matter, a general partnership had a real property lease and water purchase agreement with a city. (81 Ops.Cal.Atty.Gen. 134 (1998).) The lease required renegotiation of the rental rate and water fees every five years in accordance with guidelines specified in the agreement. (*Ibid.*) After entering the agreement but before the mandatory deadline for renegotiation, one of the general partners was elected to the city council. (*Ibid.*) The opinion addressed the effects Section 1090 had on the ability of the city council to renegotiate a contract executed prior to the election of a city councilmember with a financial interest. (*Ibid.*)

The opinion stated that the circumstances were similar to those in the *Imperial Beach* matter and concluded, in part, that where one of the general partners was a councilmember, Section 1090 prohibited the city council from approving a new rental rate and fees because that would constitute the making of a contract:

The court's reasoning in *Imperial Beach* is applicable to the specified renegotiation of the contract between the city and the partnership. Even though the original contract contains guidelines for establishing the rental rates and water fees for each subsequent five-year period, negotiation of the actual amounts would both constitute the "making" of a contract and present, at the least, the appearance of a conflict of interest that section 1090 prohibits.

Hence, such renegotiation would be impermissible under the statute.

(*Id.* at p. 137.)

The opinion goes on to determine whether Section 1090 would continue as an impediment to renegotiation if the councilmember transferred his partnership to someone else in order to eliminate his financial interest:

We have no doubt that the council member here may terminate his proscribed financial interest by transferring his partnership interest to someone else. In *Imperial Beach v. Bailey*, *supra*, 103 Cal.App.3d at 197, the court noted that the concessionaire had a choice between remaining on the city council or continuing her ownership of the concession. Simply put, if the city council member in question divests himself of his financial interest, the proscription of section 1090 will not bar renegotiation of the rental rate and water fees. [Internal cite omitted].

(*Id.* at p. 138.) Again, as in the *Imperial Beach* matter, even though the councilmember had an apparent “tenant” relationship with the city, the opinion never discussed or analyzed either of the landlord/tenant exceptions to Section 1090.

As mentioned, the present matter is virtually identical to the *Imperial Beach* matter and the Attorney General opinion just described. Specifically, Councilmember Leage would like to modify a contract with the City, in which he is financially interested, that was entered into prior to his election to the City Council and concerns the operation of a business on City property. As explained above, this is exactly the type of action prohibited by Section 1090. And unless Councilmember Leage divests himself of the proscribed financial interest, the City Council is prohibited from modifying the existing lease, even if he abstains from participating in the decision.

Step Six: Does the rule of necessity apply?

In limited circumstances, a “rule of necessity” has been applied to allow the making of a contract that Section 1090 would otherwise prohibit. (88 Ops.Cal.Atty.Gen. 106, 110 (2005).) Under the rule of necessity, a government agency may acquire an essential service, despite the existence of a conflict, when no source other than that which triggers the contract is available; the rule “ensures that essential government functions are performed even where a conflict of interest exists.” (*Eldridge v. Sierra View Hospital Dist.* (1990) 224 Cal. App. 3d 311, 322.)

You have provided no facts to suggest the “rule of necessity” would apply in the present situation.

If you have other questions on this matter, please contact me at (916) 322-5660.

Sincerely,

Zackery P. Morazzini
General Counsel

By: Jack Woodside
Senior Counsel, Legal Division

JW:jgl