3 FPPC Ops. 62

BEFORE THE FAIR POLITICAL PRACTICES COMMISSION

In the Matter of: Opinion requested by: Samuel Siegel, City Attorney, City of Pico Rivera	No. 76-054 July 6, 1977

BY THE COMMISSION: We have been asked the following question by Samuel Siegel, City Attorney for the City of Pico Rivera:

Are the members of the Board of Directors of the Pico Rivera Water Development Corporation "public officials" within the meaning of Government Code Section 87100 by virtue of their membership on such Board?

CONCLUSION

The members of the Board of Directors are "public officials" within the meaning of the Political Reform Act.

ANALYSIS

On June 21, 1974, the Pico Rivera Water Development Corporation (hereinafter "the Corporation") was formed pursuant to the California General Nonprofit Corporation Law, Corporations Code Sections 9000, et seq. The City of Pico Rivera provided the impetus for formation of the Corporation, which enjoys tax-exempt status under both Federal [Internal Revenue Code Section 501(c)(4)] and State law [Revenue and Taxation Code Section 23701(f)]. As set forth in the Articles of Incorporation, the purpose for which the Corporation was founded was to "acquire, maintain and operate a water system." More specifically, it appears that the following agreements and arrangements were entered into between the City of Pico Rivera and the Corporation.

The Corporation obtained financing by issuing bonds in the approximate amount of $11 million. The Corporation used the proceeds from the sale of the bonds to pay advance rent to the City for the water system and its related facilities. The City in turn used the advance rent to acquire title to the facilities. The Corporation, having leased the facilities, then subleased the system back to the City, and is presently applying the rent it receives from the City to pay the principal and interest on the outstanding bonds, as well as any incidental costs of maintaining the Corporation. During the term of this arrangement, the City retains ownership of the water system itself, while the Corporation holds title to all improvements, fixtures and equipment. However, once the indebtedness on the bonds issued by the Corporation is satisfied, the Corporation will cease to exist and title to the facilities will vest completely in the City. The City also has the option of purchasing the facilities by accelerating its payments to the Corporation.

There is one class of membership in the Corporation, and the members are the five Directors of the Corporation. Bylaws, Article III, Section 1. The city council does not choose the board but has the right to disapprove, in advance of the election, the name of anyone submitted to serve on the board. Although city council members have a right to attend meetings of the Corporation, none of the members of the city council are members of the Corporation.[1/] The Corporation does not have the power to impose taxes or exercise the power of eminent domain. Nor may it establish the rates to be charged to users of water supplied through operation of the water system. Under the leasing arrangements, the City (city employees) will operate the system.

This manner of accomplishing financing for essentially public purposes is not uncommon in California. It is a convenient method of financing public works projects without exceeding statutory limitations on municipal indebtedness. Accordingly, there are numerous entities similar to the Corporation which possess mixed public and private character-

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1/ However, at least one member of the Corporation is a former city councilman. The names of the persons who became members of the Corporation were suggested by the city council or staff of the City.

istics.[2] The question for resolution is whether one's membership on the board of such a corporation renders one a "public official" within the meaning of Government Code Section 87100.[3]

"Public official" is defined in Section 82048 as:

> ... every member, officer, employee or consultant of a state or local government agency.

"Local government agency" is in turn defined as:

> ... a county, city or district of any kind including school district, or any other local or regional political subdivision, or any department, division, bureau, office, board, commission or other agency of these, but does not include any court or any agency in the judicial branch of government.
>
> Government Code Section 82041

Thus, the question becomes whether the "Corporation" is itself a "local government agency." In analyzing this question we believe several criteria should be considered, and that the true nature of the entity, not merely its stated purpose, should be analyzed in determining whether the entity is public or private within the meaning of the Act. These criteria include:

> (1) Whether the impetus for formation of the corporation originated with a government agency;
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> (2) Whether it is substantially funded by, or its primary source of funds is, a government agency;

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[2] This type of arrangement is known as "public leaseback," and is authorized, subject to some limitations, by Government Code Sections 54240, et seq.

[3] All statutory references are to the Government Code unless otherwise noted.

Government Code Section 87100 provides:

> No public official at any level of state or local government shall make, participate in making or in any way attempt to use his official position to influence a governmental decision in which he knows or has reason to know he has a financial interest.

(3) Whether one of the principal purposes for which it is formed is to provide services or undertake obligations which public agencies are legally authorized to perform and which, in fact, they traditionally have performed; and

(4) Whether the Corporation is treated as a public entity by other statutory provisions.

An examination of each of these factors in this case leads us to the conclusion that the Corporation is a public entity and, therefore, must be considered a "local government agency" within the meaning of the Act. First, we find it significant that the City Council of Pico Rivera was intimately involved in the creation of the Corporation. We are advised that the idea for the Corporation originated with the city council because of the City's long-range plans to acquire control of its water system. Indeed, there is no reason to believe that the Corporation would have ever come into existence were it not a part of the City's future planning. We are also advised that the city council took an active role in soliciting names of persons to become members of the Corporation.

As we have noted, such arrangements are not at all unusual in cities which are restricted in their ability to raise funds for municipal projects because of limitations on the amount of debt they are allowed to incur. Nonetheless, it is apparent that the Corporation would not have been created were it not for the interest and involvement of the city council. We conclude therefore that the first of our four criteria is satisfied.

With respect to the second criterion, the Corporation initially sold bonds within the private sector just as the City might have. Thus, although there was no initial flow of capital to the Corporation from the City, under the leaseback agreements substantial public monies are flowing to the Corporation to pay the indebtedness on the bonds. Furthermore, the City is required to pay rent to the Corporation even if the receipts from the operation of the system are not sufficient to meet these costs. Thus, the Corporation is assured of a continuing source of capital from the City to retire the bonds it issues.

The obligation of the City to pay rent to the Corporation until the bonds are retired also demonstrates

the public character of the Corporation's involvement in this arrangement and, therefore, relates to our third criterion. The City is, in essence, guaranteeing the bonds of the Corporation. Although the legal form of this arrangement is valid and significant for purposes of the City's legal debt limitations, there is little meaningful difference, so far as the public or private character of the Corporation is concerned, between this leaseback agreement and the City simply issuing the bonds itself to pay for acquisition of the system.

Further evidence that the Corporation is fulfilling a public function under this plan is that the water system is to be operated solely by city employees. Moreover, the city has the option at any time to accelerate the payments due in order to take control of the system completely.

Finally, we consider it significant that the acquisition and operation of a water system is a service commonly provided by municipalities in their public capacities. The Corporation itself apparently recognizes the "public function" it is serving, as evidenced by its effort to qualify its bond offering for tax-exempt status under Section 103(a) of the Internal Revenue Code of 1954, as amended. That provision exempts from federal income tax interest earned on bonds which have been issued by a nonprofit corporation acting "on behalf" of a political subdivision of the state. To determine if bonds have been issued "on behalf" of a government entity, the Internal Revenue Service requires that the issuing corporation meet the following standards:

> ... (1) the corporation must engage in activities which are essentially public in nature ... (4) the state or a political subdivision thereof must have a beneficial interest in the corporation ... (5) the corporation must have been approved by the state or a political subdivision thereof, either of which must also have approved the specific obligations issued by the corporation.
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> ... Revenue Ruling 63-20 quoted in the Opinion Request

The Corporation considers itself covered by this provision. While that fact may not be determinative of the question presented here, in conjunction with the other factors we have noted, it leads us to conclude that the Corporation serves a public function and that our third criterion is therefore met.

We turn, lastly, to a consideration of whether the Corporation is treated as a public entity in the context of other statutory provisions. We are satisfied that it is. The Corporation enjoys the same legal status as a public body under the tax and securities laws. As we have noted, interest on bonds issued by the Corporation are not taxable under federal law under the exemption generally applicable to bonds issued "on behalf" of a government entity. The Corporation also enjoys tax-exempt status under California Revenue and Taxation Code Section 23701(g). The Corporation's bonds are exempt from California Corporations Code Sections 25110, 25120 and 25130 dealing with the sale and offering of securities by virtue of Section 25100(a) which exempts from regulation:

> ... Any security (including a revenue obligation) issued or guaranteed by ... any city, county, ... public district, public authority, public corporation, public entity, or political subdivision ... or agency or corporate or other instrumentality of any one or more of the foregoing; ...

In addition, under Government Code Sections 5800, et seq., governing the sale of local securities, a nonprofit corporation of this type is given the same protections and responsibilities as joint power agencies and parking authorities, entities clearly public in nature.

Based on all the facts presented we conclude that the Corporation is intrinsically "public" in character. It is an almost fictional entity created by the City to accomplish the City's purposes. We conclude that it is a "department, division, bureau, office, board, commission or other agency" of the City within the meaning of Section 82041 and that, accordingly, its members are "public officials" within the meaning of Sections 82048 and 87100. [4]

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[4] At the time this opinion was requested, the Corporation had not yet issued any bonds. Since that time, however, all the bonds have been issued and sold. This fact does not alter our conclusion that the members of the Corporation are public officials, but it may have a bearing on whether the Corporation must now adopt a conflict of interest code and, if so, what disclosure the code might require. If, for example, the only functions which the Corporation still performs are purely ministerial, a code may no longer be required. See Section 87302 and 2 Cal. Adm. Code Section 18751. Even if a code is required, the disclosure responsibilities imposed on the Corporation's directors would be limited and specific in light of the limited role the Corporation now plays in operating the water system project. See Section 87302.

Approved by the Commission on July 6, 1977. Concurring: Lowenstein, McAndrews, Quinn and Remcho. Commissioner Lapan abstained.

Daniel H. Lowenstein
Chairman