



FAIR POLITICAL PRACTICES COMMISSION

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May 1, 2003

Daniel S. Hentschke, General Counsel
San Diego County Water Authority
4677 Overland Avenue
San Diego, CA 92123-1233

**Re: Your Request Informal Assistance
Our File No. I-03-031**

Dear Mr. Hentschke:

This letter is in response to your request for advice on behalf of Michael Madigan regarding the conflict of interest provisions of the Political Reform Act (the "Act").¹ Since you have not described a specific decision, we can offer only informal assistance.²

QUESTION

Does Mr. Madigan have a conflict of interest disqualifying him from decisionmaking relating to a proposed desalination project in the City of Carlsbad?³

CONCLUSION

The given facts do not suggest that a decision to advance or retard the project would have a reasonably foreseeable financial effect on Mr. Madigan's interest in his personal finances. Any conflict of interest Mr. Madigan might have in such a decision would therefore grow out of his economic interest in PDC. Since there is a nexus between his obligations to PDC and governmental decisions advancing or retarding progress on the desalination plant project, Mr. Madigan will be disqualified from such decisionmaking whenever the decision would have *any* reasonably foreseeable financial effect on PDC.

¹ Government Code sections 81000 – 91014. Commission regulations appear at Title 2, sections 18109-18997, of the California Code of Regulations.

² Informal assistance does not provide the official with the immunity conferred by formal written advice. (Regulation 18329(c)(3), copy enclosed.)

³ You asked two other questions which the Commission cannot answer. One of these questions related to Government Code § 1090, a statute not included in the Act, and the second related to matters on which you were unable to provide a complete factual background.

FACTS

The San Diego County Water Authority ("the Authority") is a governmental agency subject to the Act. Michael Madigan is a member of the Authority's board of directors, and as such he is a public official designated by the Authority's local conflict of interest code as a "public official who manages public investments," subject to the provisions of Government Code § 87200. Among his other duties as a member of the board of directors, Mr. Madigan is the chair of the Desalination Ad Hoc Committee, comprised of seven members of the Authority's board of directors.

Since December 31, 2002, Mr. Madigan has been employed as senior vice president of a business entity known as Project Design Consultants ("PDC"). His employment agreement with PDC indicates that his job duties include "doing business development to promote PDC and secure new contracts." In addition to his base salary, Mr. Madigan is eligible to participate in PDC's senior management performance-driven bonus program. This program does not guarantee any bonus amount, and is subject to the discretion of the employer. Mr. Madigan has no partnership or other ownership interest in PDC.

The Authority has been evaluating the feasibility of developing a seawater desalination facility in the City of Carlsbad on property adjacent to an existing power plant. In November 2002, the Authority entered into a non-binding term sheet with Poseidon Resources Corporation that more specifically defines the proposed desalination project. In general, the term sheet allocates responsibility for construction of the desalination plant to Poseidon, while the Authority would be responsible for appurtenant offsite water conveyance and distribution facilities. Poseidon has expended substantial sums pursuing an arrangement with the Authority for this project. Many of the Authority's decisions on the project will foreseeably have a financial effect on Poseidon.

When Mr. Madigan joined PDC, it was providing surveying services to Poseidon, in support of Poseidon's activities on the desalination project. The value of this contract with Poseidon was approximately \$30,000.00. You indicate that there are a number of firms in the San Diego region which can offer the kind of services that PDC has provided to Poseidon.

ANALYSIS

The Act's conflict of interest rules prohibit a public official from making, participating in making, or using his or her official position in any way to influence a governmental decision in which the official has a "financial interest." (Section 87100.) Section 87103 provides that a public official has a "financial interest" in a governmental decision if it is reasonably foreseeable that the decision will have a material financial effect, distinguishable from its effect on the public generally, on the official, a member of his or her immediate family, or on any of the official's economic interests.

As a board member of the Authority, Mr. Madigan is a public official as described under § 82048. Your inquiry presupposes that he will at least participate in making governmental decisions relative to developing a seawater desalination plant in the City of Carlsbad.⁴ The next portion of the conflict of interest analysis is identification of the public official's economic interests which, under § 87103, may be any of the following:

- A public official has an economic interest in a business entity in which he or she has a direct or indirect investment⁵ of \$2,000 or more (section 87103(a); regulation 18703.1(a)); or in which he or she is a director, officer, partner, trustee, employee, or holds any position of management (section 87103(d); regulation 18703.1(b));
- A public official has an economic interest in real property in which he or she has a direct or indirect interest of \$2,000 or more (section 87103(b); regulation 18703.2);
- A public official has an economic interest in any source of income, including promised income, which aggregates to \$500 or more within 12 months prior to the decision (section 87103(c); regulation 18703.3);
- A public official has an economic interest in any source of gifts to him or her if the gifts aggregate to \$340 or more within 12 months prior to the decision (section 87103(e); regulation 18703.4);
- A public official has an economic interest in his or her personal expenses, income, assets, or liabilities, as well as those of his or her immediate family—this is the “personal financial effects” rule (§ 87103; regulation 18703.5).

PDC is an economic interest to Mr. Madigan because he is employed by that company, he holds a position of management in the business and, we presume, because PDC has been a source of \$500 or more in income to him over the past twelve months.⁶

A public official always has an economic interest in his or her personal expenses, income, liabilities or assets, and those of his or her immediate family (defined at § 82029 as the official's spouse and dependent children). These are the only two economic interests evident from your account of the facts, and our analysis will be limited to conflicts of interest growing out of these economic interests.

⁴ Regulations 18702.1 through 18702.3 define “making,” “participating in making,” and “using or attempting to use his/her official position to influence” the making of governmental decisions. Regulation 18700(b) describes in detail the step-by-step process used to determine if a public official has a conflict of interest in a particular decision.

⁵ An indirect investment or interest includes any investment or interest of the official's spouse. (Section 87103.)

⁶ We presume likewise that any money paid to Mr. Madigan by the Authority is “[s]alary and reimbursement for expenses or per diem received from a state, local, or federal government agency,” exempting the Authority from classification as a “source of income.” (See § 82030(b)(2) and regulation 18232.)

After identifying the official's economic interests, we next determine whether they are directly or indirectly involved in the decisions at issue. As to business entities and sources of income, regulation 18704.1 provides that:

“(a) A person, including business entities, sources of income, and sources of gifts, is directly involved in a decision before an official's agency when that person, either directly or by an agent:

(1) Initiates the proceeding in which the decision will be made by filing an application, claim, appeal, or similar request or;

(2) Is a named party in, or is the subject of, the proceeding concerning the decision before the official or the official's agency. A person is the subject of a proceeding if a decision involves the issuance, renewal, approval, denial or revocation of any license, permit, or other entitlement to, or contract with, the subject person.

(b) If a business entity, source of income, or source of a gift is directly involved in a governmental decision, apply the materiality standards in California Code of Regulations, Title 2, section 18705.1(b), section 18705.3(a), or section 18705.4(a), respectively. If a business entity, source of income, or source of a gift is not directly involved in a governmental decision, apply the materiality standards in California Code of Regulations, Title 2, section 18705.1(c), section 18705.3(b), or section 18705.4(b), respectively.”

It appears from your account that the anticipated decisions on development of the desalination plant will not directly involve PDC, which is therefore involved only indirectly in these decisions.⁷ For a business entity or source of income that is indirectly involved in a governmental decision, the effect of the decision is “material” if it reaches the thresholds described in regulation 18705.1(c). (Regulation 18705.3(b)(1).) Thus, for example, if by reason of its economic size PDC is governed by regulation 18705.1(c)(4), an effect of a governmental decision is “material” when;

“(A) The governmental decision will result in an increase or decrease in the business entity's gross revenues for a fiscal year in the amount of \$20,000 or more; or,

(B) The governmental decision will result in the business entity incurring or avoiding additional expenses or reducing or eliminating existing expenses for a fiscal year in the amount of \$5,000 or more; or,

⁷ Economic interests in a public official's personal finances are not analyzed as “directly” or “indirectly” involved in a governmental decision. A financial effect on personal finances is “material” in every case where the effect amounts to at least \$250 over any 12 month period. (Regulation 18705.5.)

(C) The governmental decision will result in an increase or decrease in the value of the business entity's assets or liabilities of \$20,000 or more.”

There is, however, a *separate and distinct* materiality standard which applies in cases where there is a “nexus” between duties owed to a source of income and to the official’s public agency. Regulation 18705.3(c) provides:

“(c) Nexus. Any reasonably foreseeable financial effect on a person who is a source of income to a public official is deemed material if the public official receives or is promised the income to achieve a goal or purpose which would be achieved, defeated, aided, or hindered by the decision.”

Both of these materiality standards would be applicable when a decision would have a foreseeable financial effect on PDC, because PDC is Mr. Madigan’s employer *and* because Mr. Madigan’s job duties include generating new business revenues for PDC, establishing a “nexus” between his public and private obligations. The only difference between these materiality standards, in this case, is the size of the financial effect that constitutes a “material” effect. Under regulation 18705.3(c), *any* financial effect is “material.” Thus, if the reasonably foreseeable effect of a governmental decision is *any* financial gain or loss to PDC, that gain or loss is “material” and we need not separately consider whether the gain or loss reaches the threshold amounts of regulation 18705.1.

There will only be a “nexus” between Mr. Madigan’s private-sector obligations and decisions relating to construction of the desalination plant *if it is reasonably foreseeable* that a decision by the Authority to proceed (or not) with construction of the plant would aid or hinder the accomplishment of his job duties with PDC – which include business development and securing new contracts.⁸ The existence of a disqualifying nexus therefore turns on whether or not it is reasonably foreseeable that PDC would secure additional business from Poseidon if the project moves forward, or lose that opportunity if the project is halted. PDC has already provided services to Poseidon in support of this project, and an established connection on this very project is strongly suggestive of such foreseeability.

A material financial effect on an economic interest is reasonably foreseeable, within the meaning of § 87103, if it is “substantially likely” that one or more of the materiality standards applicable to that economic interest will be met as a result of the governmental decision. (Regulation 18706; *In re Thorner* (1975) 1 FPPC Ops. 198.) A financial effect need not be a certainty to be considered reasonably foreseeable. On the

⁸ You have not provided us with a description of any particular decision “relating to” the desalination plant project, although you have said that many of these decisions would have a foreseeable financial effect on Poseidon. For purposes of this analysis, we will assume that the decisions you speak of will either advance this project, requiring additional work by Poseidon and making still further work more probable, or will retard the project, with opposite effects.

other hand, if an effect is only a mere possibility, it is *not* reasonably foreseeable. (*In re Thorner, supra.*) Whether financial consequences to a business entity are reasonably foreseeable at the time of a governmental decision depends on the facts of each particular case. (*Id.*) In each case, the official must look at the facts surrounding each decision to determine whether the decision is substantially likely to cause a material financial effect on the economic interest. (*Id.*)

In the *Thorner* Opinion, the Commission considered a situation where a certain contractor had been awarded a contract. This contractor was a regular customer of the public official's construction business, "McPhail's." From these facts the Commission reached the following conclusion:

"Although there is no agreement, express or implied (citation) between McPhail's and the contractor, there is, without question, a sufficient likelihood that McPhail's will receive business to make the financial effect on Director McPhail 'reasonably foreseeable'." (*In re Thorner, supra.*)

In the present case, as we understand matters, there is a "non-binding term sheet" which at least creates an expectation that, if the desalination plant is built, Poseidon will be involved in its construction. Poseidon has already expended substantial sums towards preliminary work on the project, and it has employed PDC in support of that work. Although there may be no binding agreement to employ PDC on later stages of the project, the Commission's logic in *Thorner* indicates that here, too, there is "without question" a substantial likelihood that PDC will receive further business from Poseidon, if the Authority decides to move forward with the desalination plant project. We conclude that a decision by the Authority to advance or retard this project would have a reasonably foreseeable material financial effect on PDC.

We cannot rule out the possibility that the Authority may be called on to make some decisions "relating to" this project which do not advance or retard the project, whose effects are simply unrelated to its progress – a decision on what color to paint a gate on an access road built last year, for example. Since we do not have information on specific decisions coming before the Authority, we can only provide advice on decisions to move forward, or not, on the project – the *kind* of decisions you described in your account of the facts as having foreseeable financial effects on Poseidon.

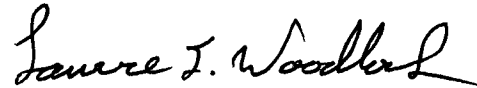
Available information suggests that a decision to advance or retard the project would not have a reasonably foreseeable financial effect on Mr. Madigan's interest in his personal finances. Any conflict of interest Mr. Madigan would have in such a decision would therefore grow out of his economic interest in PDC. Since there is a nexus between his obligations to PDC and decisions advancing or retarding progress on the desalination plant project, Mr. Madigan will be disqualified from playing any part in such decisionmaking, so long as there is *any* reasonably foreseeable financial effect on PDC.⁹

⁹ There are two exceptions to disqualification from decisions that would have a reasonably foreseeable material financial effect on a public official's economic interests. The first is applicable in cases where the

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

Sincerely,

Luisa Menchaca
General Counsel



By: Lawrence T. Woodlock
Senior Counsel, Legal Division

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effect on the public official is not distinguishable from the effect of the decision on the public generally. (Regulation 18707.) The second exception permits an official to participate in a decision notwithstanding a conflict of interest, where such participation is legally required. (Regulation 18708.) Nothing in your account of the facts indicates that either of these exceptions would apply to Mr. Madigan, but we call your attention to them in case facts arise where one or the other exception might apply.