CONFLICTS OF INTEREST:
BEYOND THE BASICS

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Conflict of Interest Laws
that may apply to charter schools:
• Political Reform Act, Gov. Code, § 87100 et seq.
• Government Code § 1090
• Nonprofit Corporation “interested persons” rules, Corp. Code, §5230 et seq.
• Nonprofit Public Integrity Act, Gov. Code §12586(g)
• Federal funding/grant rules
• SB 740 “related party” limits, 4 CCR §10170.14
• Authorizer-imposed policies

Political Reform Act
• Charter schools may be subject to the California Political Reform Act of 1974 (Gov. Code § 81000, et seq.) (“CPRA”)
  – Requires adoption of conflict code
  – Requires annual financial disclosures by designated employees and officials (April 1st filing Form 700)
  – Requires disclosure and disqualification from decisions that may affect “material” financial interests
Conflicts of Interest
The Political Reform Act

- Under CPRA, public officials/employees may not participate in making, or in any way attempt to use their official position to influence, a governmental decision in which they know or have reason to know they have an economic interest. (Note the CPRA limits participation but not membership.)
- To determine whether a conflict of interest exists under CPRA, five questions must be asked:
  1. Is a public official involved?

Conflicts of Interest
The Political Reform Act (continued)

2. Does the official have a statutory defined economic interest? (interests of spouse and dependents count; can be indirect interest)
3. Is the official making, participating in making, or using his or her official position to influence, a governmental decision?
4. Is it reasonably foreseeable that the decision could materially affect the official’s economic interest?

Conflicts of Interest
The Political Reform Act (continued)

5. Will the effect of the decision on the public official’s economic interest be distinguishable from its effect on the public generally?
   - If the answer to all five questions is “yes,” a conflict of interest exists and the conflicted individual must disqualify herself from participation in the decision. (Note non-employee board members have no personal financial interest in the schools’ budget or operations. Employee board members disclose and disqualify themselves from participation in decisions that could affect their interests.)
Conflicts of Interest
The Political Reform Act (continued)

- Your examples and questions here . . .
- Our examples:
  - Executive Director’s spouse is employed by curriculum vendor whose contract is up for renewal
  - Board member leases school site to charter school and annual rent increase is pending
  - Board member is a teacher; budget on agenda
  - CFO’s house is a block from proposed new site being considered

Conflicts of Interest
The Political Reform Act – Reporting

Form 700 Annual Report of Economic Interests.

- In order to identify and avoid potential conflicts of interest, the CPRA requires that designated employees disclose interests that could impact their decision-making by filing a Statement of Economic Interest, Form 700.

Conflicts of Interest
The Political Reform Act – Reporting (continued)

- Form 700 requires disclosure of income, gifts and interests (defined in Government Code sections 82028, 82030, 82033, 82034)
  - A charter school’s conflict of interest code and state law identify employees who must file a Form 700.
  - Those employees must disclose certain assets and income.
Conflicts of Interest
The Political Reform Act – Reporting
( Form 700 continued)
• Certain types of gifts, honoraria and loans are prohibited.
• Filers may not accept gifts totaling more than $470 in a calendar year from a single source.
• Civil and criminal penalties for violation www.fppc.ca.gov/forms/700-11-12/RefPamphlet11-12.pdf

Gov. Code § 1090
“The law does not permit a public officer to place himself in a position in which he might be tempted by his own private interest to disregard the interests of the public”
Government Code, § 1090 may apply to charter schools
• Charter schools do not fit within § 1090’s definition of local public entities since they do not operate within limited boundaries. Legislative intent and Ed. Code, § 47610’s “megawaiver” also suggest § 1090 should not apply. A California Attorney General opinion pending since 2011.

Conflicts of Interest – Gov. Code § 1090
• Prohibits public officials/employees from participating in the process by which a contract is developed, negotiated, or executed if the official or employee has a financial interest in the contract.
• These contracts are void and cannot be enforced.
(Gov. Code, § 1092.)
Conflicts of Interest -- Gov. Code § 1090

• Section 1090 does not define when an official is financially interested in a contract; however, courts have applied the prohibition to include a broad range of interests.
• Sections 1091-1091.6, enumerate certain “remote” and “non-interests” that, once disclosed, do not prevent an officer from participating in the making of a contract.

Conflicts of Interest -- Gov. Code § 1090

• Your examples?

Conflicts of Interest -- Gov. Code § 1090

• Our examples:
  - California Department of Education enters into contracts with nonprofit group headed by State Superintendent’s wife
  - Chief development officer hires her own company to print gala event brochures at cost
  - School founder and manager leases property to charter school
  - Board member architect who prepared, for free, “needs assessment” for new school to be built submits proposal to design the campus
  - School hires spouse of board member to provide legal services
  - School leases office space from nonprofit; school board member is also board member of nonprofit
Nonprofit Corporation Law

Corporations Code section 5233 applies to charter schools operating as nonprofit public benefit corporations

- No more than 49% of a board of directors may be interested persons. 
  An interested person is a director who provides nondirector services to the nonprofit public benefit corporation and is paid for the services rendered (e.g. employee-director). (Corp. Code § 5227.)

Conflicts of Interests – Nonprofit Corporation Law

Limitation on self-dealing transactions. “Self-dealing” is where a director has a personal material financial interest in a transaction, except:

- Setting director stipends
  - Benefits received from charitable programs when the director is within the class of persons served
  - When the lesser of 1% of gross receipts of company or $100,000

Conflicts of Interests – Nonprofit Corporation Law (continued)

- A self-dealing transaction can be approved if:
  - It benefits the corporation
  - Terms are fair and reasonable
  - A majority of the Board, excluding the “interested” directors, approves or ratifies
  - The Board finds no more advantageous deal could have been obtained

  (Corp. Code section 5233)
Conflicts of Interests – Nonprofit Corporation Law

- Under nonprofit corporate law, arrangements between corporations with directors in common are not void because common directors are present if:
  - Material facts are fully disclosed/known AND
  - A majority of the Board approves or ratifies in good faith without counting the votes of common directors OR the contract was just and reasonable at the time of approval
  (Corp. Code § 5234)

Conflicts of Interests – Nonprofit Corporation Law

- Corporations Code section 5234 describes directors’ fiduciary “duty of loyalty” to the corporation
  - Does the transaction advance and achieve the corporation’s charitable purposes?
  - Is the transaction “arms-length” or unfair and inequitable?

Conflicts of Interests – Nonprofit Corporation Law

- Your examples . . .
- Our examples:
  - School founder wrote texts school wants to purchase
  - School hires director’s design firm to handle school recruiting and promotional materials
  - School outsources information technology support to firm owned by board member’s cousin, or best friend
  - Member of affiliated foundation board grants school $18 million for school facilities
Nonprofit Public Integrity Act, Gov. Code § 12586(g)

Board of directors or board committee must approve just and reasonable compensation of chief executive and chief financial officers.

What should you consider?

• Survey peers
• Pay executive gets from affiliates on Form 990
• Include benefits in analysis
• Data from Guidestar, compensation consultants
• Whether to apply Government Code limits on severance and health benefits, clawbacks, etc.
• Policy putting limits on reimbursements, business expenses
• Include a summary of total compensation in agreement

Federal Funding and Grant Rules

2 C.F.R. § 200.112 Conflicts of Interest

• The Federal awarding agency must establish conflict of interest policies for Federal awards. The non-Federal entity must disclose in writing any potential conflict of interest to the Federal awarding agency or pass-through entity in compliance with the applicable policy.
  – So, check your funding source for particular conflict policies.
    • Ex: Federal School Lunch Program
• State and Federal Grants typically establish conflict of interest policies as conditions of award.
• Affirmative duty to adopt rules, or risk sanctions.
Federal Funding and Grant Rules

- **7 C.F.R. Part 3019** – Establishes uniform administrative requirements for Federal grants and agreements awarded to non-profit organizations (among others).
- **7 C.F.R. 3019.42** Code of Conduct says:
  
  "No employee, officer, or agent shall participate in the selection, award, or administration of a contract supported by Federal funds if a real or apparent conflict of interest would be involved."
- Nearly identical regulations apply to many federal grants and programs.
- Federal conflict rules are broader than State rules sometimes!

SB 740 Facility Funding

- For charter schools accepting SB740 funds from the State, special conflict of interest rules apply.
- **4 CCR §10170.14** governs Conflicts of Interest for Charter School Facility Grant Program: “Grantees must avoid actual conflicts of interest when applying for or receiving grants from the Authority”.
- Regulations designed to allow “Related Party” lease arrangements.
- But not with private person or for-profit entities which are related to the charter school.

Authorizer-Imposed Policies

- Some authorizers demanding that charter schools adopt Conflict of Interest Policies, with particulars.
- Yet another layer of red tape to navigate.
- Fight it or comply? Best to evaluate on a case-by-case basis.
Thank you!
Questions? Please feel free to contact us any time for guidance.

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