

ADVISORY OPINION NO. 88-8

The Commission received a request for an advisory opinion from a state official. The advice was requested in regard to possible conflicts of interest arising from a proposed private, nonprofit organization being developed by the official's state agency.

FACTS

Under the proposed by-laws of the organization, an employee of the state agency would become the secretary-treasurer of the organization and the secretary-treasurer would work out of the office of the employee's supervisor (the requester of the opinion) and would be subject to the supervision of the employee's supervisor.

The employee explained that he had done extensive research on such organizations. He stated that he had looked at several models of similar organizations on the mainland in order to select a model which might be appropriate. The requester of the advisory opinion explained that the state agency was fifteen to twenty years or more behind other state agencies on the mainland in terms of forming such an organization. The requester stated that the state agency was trying to catch up in this respect.

The Commission was provided with a copy of the proposed by-laws of the organization. The organization was intended to be a nonprofit organization. In the by-laws of the organization, the purpose of the organization was explained as follows:

The organization shall stimulate, promote and enhance the growth and enrichment of the state agency. It shall foster a spirit of loyalty and fraternity.

The employee explained that the organization would act as an umbrella organization for all similar organizations, including currently existing organizations, related to the state agency. The employee explained that there were several areas that they were looking into as to what the organization could do for the state agency. Among these areas were fundraising and providing feedback to the state agency without negative publicity.

In terms of funding, the requester explained that the state agency asked three foundations for seed money to get started. These contributions would be a one-time matter. The requester explained that the state agency would be asking for funds from the legislature at the next legislative session for the coming biennium.

The employee would not be receiving compensation as secretary-treasurer of the organization. The state agency would continue to pay the employee's salary, and it appeared that the employee's duties would expand to include the work of the secretary-treasurer of the organization. The organization would conduct its affairs through the employee and his staff who were located in the office of the employee's supervisor. The employee's staff currently consisted of a secretary.

The employee explained that he saw his state position as administering and coordinating the work between his state office and the organization. The employee, as the secretary-treasurer of the organization, would see to it that the organization stayed honest, and would provide continuity for the organization.

The employee stated that as a state employee and secretary-treasurer of the organization, he would be wearing two hats. As a state employee, he would insure that the organization's programs and projects were in compliance with all regulations of the state agency. In his position as secretary-treasurer, he would make sure that the organization's programs and projects interfaced with and complimented the programs of the state agency. When asked whether the employee would serve the interests of the organization or the interests of the state agency if a conflict arose between the desires of the organization and the employee's duties as a state employee, the employee emphasized that he had made it clear that if a conflict arose he would act as a state employee. The requester explained that if there were any conflict between the desires of the organization and the interest of the state agency, the matter would be worked on to achieve an amicable resolution.

The employee explained that when the organization was fully operational in six to ten years, a decision would have to be made as to whether the employee in serving as the secretary-treasurer of the organization would continue to be paid entirely by the state agency, or partly by the state agency and partly by the organization, or entirely by the organization. The employee explained that the decision would depend upon how the organization evolved.

The employee also provided an alternative to having the employee serve as the secretary-treasurer of the organization. In the proposed alternative, the employee would serve as an ex officio, nonvoting member of the organization's council and executive committee. The employee would serve as the state agency's liaison between the state agency and the organization. The employee would review materials pertaining to the organization's operations and advise the executive committee. When asked if it would be possible at that point in time to use the alternative instead of the proposal that the employee serve as the secretary-treasurer of the organization, the employee indicated that because he was the person developing the organization, he was not able to separate what he did as a state employee and what he did for the organization.

In the by-laws of the organization, the structure of the organization was replete with the participation of other state agency officials in addition to the state employee and the state employee's supervisor. The executive committee of the organization would act as the board of directors of the organization. The council to the organization would make recommendations to the executive committee on matters which would improve the organization and its service to the state agency. Both the council and the executive committee of the organization would have had ex officio, nonvoting members which would have included various officials of the state agency in addition to the employee and the employee's supervisor. The state officials, other than the employee, would serve on a voluntary basis. Their positions as ex officio, nonvoting members were provided for to allow for the input of these various state officials.

Officials from the state agency would also participate in the organization in other ways. These state officials would be involved in the appointment of the members of the council and of the executive committee of the organization.

In regard to the officers of the organization, the by-laws specifically provided that the state employee would serve as the secretary-treasurer of the organization. The by-laws provided that the secretary-treasurer would be the custodian of the monies of the organization and would make disbursements in such manner as was authorized by the by-laws and the executive committee. The by-laws provided that the secretary-treasurer would work under the supervision of the employee's current supervisor. The by-laws provided that the secretary-treasurer would be responsible for hiring, firing, and supervising all staff of the organization.

The other officers of the organization provided for under the by-laws of the organization were a president, a first vice president, and a second vice president. In response to an inquiry as to whether any of the ex officio, nonvoting members of the council or executive committee who are state officials (not including the state employee) may be elected to be an officer, the state employee responded that it would be possible to include in the by-laws that the other state officials who were ex officio, nonvoting members of the council or the executive committee may not be elected as officers of the organization. The employee indicated that it was his preference that the other state officials not serve as officers of the organization.

The by-laws of the organization also provided for a nomination committee which would be responsible for filling vacancies on the council and the executive committee. The nomination committee would nominate ten persons at-large for appointment to the council by a state official, the officers of the organization to be elected by the council, five persons from the council for appointment to the executive committee by a state official, and three persons from the council for election to the executive committee by the council. The nomination committee would consist of six voting members which included the first vice president of the association and other members elected by state officials. The state employee would chair the committee as a nonvoting, ex officio member. However, in the case of a tie vote, the state employee would cast the deciding vote.

In regard to various groups which would have wanted to receive a charter as an official component of the organization, each group would have had to comply with the by-laws set forth by the organization and must have agreed to follow the policy and procedure established by the state agency.

The by-laws also provided that chartered groups may receive assistance with programs and activities from the staff of the state employee's office, which office would serve as a direct liaison between the groups and the organization. The chartered groups would have been encouraged to use the office of the state employee for access to lists and labels of their members. The staff of the office of the state employee would also have been available to help chartered groups maintain accurate records of their members.

Under the by-laws of the organization, each constituent group would have determined its own programs and activities. However, each constituent group was required to engage in certain specified activities which would serve the purpose of the state agency.

In regard to the organization's dues, the organization would not recommend dues for constituent groups. If a constituent group decided to assess dues, the rate of dues would be determined jointly by the executive committee and the officers of the constituent group. Dues assessed by a constituent group would be held in the custody of the organization.

DISCUSSION

The provision of the State Code of Ethics which appeared to be most applicable to this situation was HRS §84-14(b) which states as follows:

(b) No employee shall acquire financial interests in any business or other undertaking which he has reason to believe may be directly involved in official action to be taken by him.

The organization was construed to be a business for the purposes of HRS §84-14(b). The Ethics Code defines "business" as including "a corporation, a partnership, a sole proprietorship, a

trust or foundation, or any other individual or organization carrying on a business, whether or not operated for profit."

"Financial interest" is defined under the Ethics Code as follows:

"Financial interest" means an interest held by an individual, the individual's spouse, or dependent children which is:

- (1) An ownership interest in a business.
- (2) A creditor interest in an insolvent business.
- (3) An employment, or prospective employment for which negotiations have begun.
- (4) An ownership interest in real or personal property.
- (5) A loan or other debtor interest.
- (6) A directorship or officership in a business.

This provision of the Ethics Code prohibited state employees from acquiring a financial interest as a director or an officer in the organization if there was reason to believe that the employee would be taking official action directly affecting the organization. "Official action" under the Ethics Code means a "decision, recommendation, approval, disapproval, or other action, including inaction, which involves the use of discretionary authority."

Inasmuch as the state employee was developing the organization, was the employee through whose efforts and office the organization would be organized, was the employee who would watch over the activities of the organization to make sure that the activities complied with the state agency's regulations and policies, and was the employee who would act as a liaison between the state agency and the organization, the state employee would be taking official action directly affecting the organization. The state employee's supervisor in also developing the organization and as a supervisor of the state employee would also be taking official action directly affecting the organization. Moreover, the organization would be utilizing the staff of the office of the state employee, which office was a part of the office of the state employee's supervisor.

If the state employee became a member of the board of directors or an officer of the organization, and if the state employee's supervisor became a member of the organization's board of directors, both the state employee and the state employee's supervisor may have been construed to be acquiring a financial interest as a director or officer in the organization in regard to which the employee and the employee's supervisor would be taking direct official action in their state capacities in violation of HRS §84-14(b). Other state officials who may have been construed to be acquiring a financial interest in the organization by virtue of their membership on the board of directors may have also taken direct official action in their state capacities in regard to the organization if they had chosen to exercise their right under the by-laws to each select one member of the organization's nomination committee.

However, there were existing advisory opinions which indicated that HRS §84-14(b) should not be applied to this situation. In two recent opinions, Advisory Opinions Nos. 86-1 and 86-2, the Commission set forth guidelines which the Commission would use in determining whether the spirit and intent of HRS §84-14(b) requires that HRS §84-14(b) be applied to a situation involving a nonprofit corporation and a state employee who wishes to serve as a director or officer of that nonprofit corporation in his or her state capacity. In setting forth these guidelines, the Commission provided the following explanation in Advisory Opinions Nos. 86-1 and 86-2, for the establishment and application of the guideline:

It is not clear, however, whether when drafting HRS §84-14(b) the legislature had envisioned the situation in which state employees serve as directors or officers of private corporations as part of their state duties. Because state employees who serve in their official capacities as directors or officers of private corporations have no "personal" financial interest in the corporations, the Commission believes that HRS §84-14(b) does not necessarily prohibit them from accepting directorships or officerships with the private corporations. The Commission believes, however, that in allowing state employees to accept positions as directors or officers of private corporations certain conditions must normally be met, and the Commission has set forth these conditions in the list of guidelines found below. The Commission would like to emphasize that these guidelines are meant to serve only as general principles and are not meant to suggest that any particular case would be subject to either automatic rejection or approval. Although the Commission believes that each case must be presented to the Commission for its approval, the Commission issued these guidelines to inform state employees of the various factors involved

In Advisory Opinion No. 86-1, the Commission allowed a state official to serve in his state capacity as the president of a private, nonprofit corporation which was established and funded by the legislature to accomplish state goals and which was subject to official action taken by the state official.

In Advisory Opinion No. 86-2, a state official was allowed by the Commission to serve in his state capacity as one of the members of the board of directors of a private, nonprofit corporation. This opinion confirmed Advisory Opinion No. 280 in which a state employee holding the state official's position at that time was permitted to serve in his state capacity as a board member of this private corporation even though the employee's department occasionally entered into contracts with the corporation for services and the employee was responsible for approving and monitoring the contracts. The nonprofit corporation was funded by the federal government to do research and assist the states in a certain geographical area.

In applying the guidelines set forth by Advisory Opinions Nos. 86-1 and 86-2 to the state agency's situation, each guideline was discussed in application to this particular situation as follows:

1. There is a valid state purpose that justifies a state *agency having one of its employees serve in a state capacity as the director or officer of a private corporation.*

The intent of having the state employee serve as the secretary-treasurer of the organization was to be sure that the monies of the organization were expended lawfully, to provide staff assistance to the organization, to provide continuity for the organization, and, very importantly, to make sure that the organization complied with the policies and regulations of the state agency. The state employee would also have been acting as a liaison between the state agency and the organization.

It appeared that as the supervisor of the employee, the supervisor was also intended to supervise the employee in the employee's capacity as the secretary-treasurer of the organization. The organization would also receive support services from the office of the employee which was a part of the office of the employee's supervisor.

The requester explained that state agency officials who were designated to be ex officio, nonvoting members of the organization's board of directors were so designated to allow the officials' input into the organization. The intent was to have the organization maintain ties to the state

agency to make sure that the activities of the organization did not stray from the mission of the state agency. The state officials would also provide state leadership to the organization but would not vote.

2. The state agency authorizes in writing that serving as *the director or officer of a private corporation is one of the official responsibilities of the state employee.*

The requester and the employee indicated that it would be possible to add to the employee's job description the duties required of the secretary-treasurer of the organization. The by-laws of the organization which were being drawn up by the requester and the employee specifically provided that the employee would be the secretary-treasurer of the organization.

Other state officials in serving as ex-officio, nonvoting members of the board of directors would serve on a voluntary basis, and if they chose to serve they would be serving in their official state capacities with the state agency.

3. A state employee who serves in an official capacity as a *director or officer of a private corporation serves or acts solely on behalf of the State's interest.*

The employee made it clear that although he would be wearing two hats as a state employee and the secretary-treasurer of the organization, he would be acting as a state employee. If there was ever a conflict arising between the desires of the organization and the interests of the state agency, the state employee would be acting in behalf of the state agency.

There was no reason to believe at that time that the other state officials while serving on the board of directors in their official capacities would not act solely in behalf of the state agency. The intent of having these officials serve on the board of directors was to make sure that the organization's activities did not stray from the mission of the state agency.

4. The state employee receives no compensation from *the private corporation.*

The state employee would continue to receive compensation from the state agency. The state employee explained that when the organization was fully operational in six to ten years, at that time, a decision should be made as to whether the employee's position should be continued to be funded by the state agency or whether in light of the employee's duties as secretary-treasurer of the organization the organization should compensate the employee in whole or in part. For the time being, neither the employee nor any other state official would be receiving any compensation from the organization or from the legislature for their respective positions with the organization.

5. The state employee has no financial interest in the *private corporation.*

Neither the state employee nor any other state official would have a personal financial interest in the organization.

6. *The state employee's service as a director or officer of the private corporation does not violate any of the provisions of the State Ethics Code.*

- a. *The purpose of the corporation. The Commission believes that ethical problems are less likely to arise in situations in which the private corporation has been created to further the public's interest as a whole or the interest of the State of Hawaii, rather than individual or private interests.*

It was evident that the intended purpose of the organization was to create a strong support group for the state agency. In the by-laws of the organization, the purpose of the organization was explained as follows:

The organization shall stimulate, promote and enhance the growth and enrichment of the state agency. It shall foster a spirit of loyalty and fraternity. The organization shall have the power to do any and all things of every kind and nature permitted by law and by the internal revenue code with respect to section 501(c)(3), qualified exempt organization for the benefit of the state agency. The organization shall comply with all state agency policies.

- b. *The funding source. The Commission believes that ethical problems are less likely to arise in situations where the federal or state government, charities, or foundations fund the private corporation.*

In order to proceed in 1988 with the formation of the organization, the state agency sought one-time contributions from three foundations. For the following biennium, the state agency would be seeking funding from the legislature.

- c. *Whether the corporation is a profit or nonprofit corporation. The Commission believes that ethical problems are less likely to arise when state employees serve as directors or officers of nonprofit corporations.*

It was clear that the organization would function as a nonprofit corporation.

7. *The question of whether a state employee may serve in a state capacity as a director or officer of a private corporation has been presented to the Commission, and the Commission has granted its approval.*

The state agency, through the requester, sought this advisory opinion at a time when the state agency was working on the formation of the organization. The organization did not yet exist. The requester and the employee were in the planning stages of the organization.

In applying the Commission's guidelines to the situation at hand, it was apparent that the state agency and its organization clearly met all of the Commission's guidelines. Moreover, in addition to meeting the Commission's guidelines, the organization's situation was similar to the situations of the advisory opinions issued prior to Advisory Opinions Nos. 86-1 and 86-2 which dealt with the application of HRS §84-14(b) and HRS §84-14(a), another conflict of interest provision under the Ethics Code. In Advisory Opinion No. 403, a state employee who worked at a state facility had inquired as to whether the employee would be able to continue serving as an officer and a member of the board of directors of an independent, nonprofit corporation located on the grounds of the state facility. The Commission found that HRS §84-14(a) would be applicable to the employee except that the Commission also found that the interrelationship between the state facility and the nonprofit corporation provided a real benefit to the State of Hawaii and that programs of the corporation were, in a sense, state programs. The Commission, therefore, created an exception to the conflict of interest provision for the state employee.

In Advisory Opinion No. 445, an administrator of a state program served as an uncompensated officer of a private, nonprofit organization. In this advisory opinion, the Commission also found that a real benefit accrued to the State of Hawaii from the interrelationship of the nonprofit organization and the state program, and that the nonprofit organization was, in a

sense, a state organization. The Commission, therefore, made an exception to HRS §84-14(b) and allowed the administrator to continue to serve as an officer of the nonprofit organization.

In the situation at hand, the Commission found that in applying the guidelines set forth in Advisory Opinions Nos. 86-1 and 86-2 to the state agency and the organization, that HRS §84-14(b) did not apply to the state agency and the organization. The Commission found that the state agency's administrative decision to form the organization to benefit the state agency constituted a legitimate state purpose in establishing the organization and that a public benefit accrued to the State by the establishment of the organization. It was the opinion of the Commission that the spirit and intent of HRS §84-14(b) argued against the application of HRS §84-14(b) to this situation.

However, another provision of the Ethics Code which was considered for application to this situation was HRS §84-13(3) which prohibits the use of state time, equipment, or other facilities for private business purposes. Inasmuch as the by-laws of the organization called for the involvement of various state officials in their state capacities, especially the state employee and the state employee's supervisor, and for the use of staff time and facilities of the office of the state employee which was located within the office of the state employee's supervisor, this provision of the Ethics Code may have been construed to be violated by the use of such state time, equipment, or facilities for the purposes of the organization. Nevertheless, since the Commission found that the organization served a legitimate state purpose and by administrative policy the state agency decided that the time of state officials and their staff and the equipment and other facilities of the state agency should be used to carry out the activities of the organization, the Commission additionally found that HRS §84-13(3) would not be violated because the organization served a state purpose rather than a private purpose.

The findings of the Commission were based upon the proposed structure and operation of the organization and other relevant factors which were discussed with the Commission by the requester and the state employee. The requester was advised that if there should be a substantial change in the situation, that the state agency seek further advice and assistance from the Commission in regard to the application of the Ethics Code. The Commission appreciated the sensitivity shown by the requester and the state employee in regard to the application of the Ethics Code to the situation while in the process of establishing the organization. However, recognizing that the situation would raise further ethical considerations as the organization began to operate, the Commission invited the requester to contact the Commission for advice at any time should any further question arise in regard to the Ethics Code.

The Commission thanked the requester for consulting with the Commission and for the cooperation of the requester and the state employee in the matter.

Dated: Honolulu, Hawaii, May 11, 1988.

STATE ETHICS COMMISSION
Rabbi Arnold J. Magid, Vice Chairman
K. Koki Akamine, Commissioner
Cynthia T. Alm, Commissioner
Rev. David K. Kaupu, Commissioner

Note: Chairperson Laurie A. Loomis was not present during the discussion and consideration of this opinion.