



OHIO ETHICS COMMISSION

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Advisory Opinion Number 89-011
October 18, 1989

Syllabus by the Commission:

- (1) For purposes of Division (A)(4) of Section 2921.42 of the Revised Code a creditor has an interest in the contracts of a debtor corporation, unless he is able to meet all of the criteria for the exemption of Division (B) of Section 2921.42;
- (2) Division (B) of Section 2921.42 of the Revised Code provides that, in the absence of bribery or fraud, a public servant shall not be considered to have an "interest" in a public contract with his own political subdivision when: (a) the public servant's interest in a corporation doing business with his own political subdivision is limited to being a creditor of the corporation; (b) the amount due the public servant does not exceed **five** per cent of the total indebtedness of the corporation; and (c) the public servant files with the political subdivision an affidavit giving his exact status in connection with the corporation;
- (3) As used in Division (B) of Section 2921.42 of the Revised Code, the term "creditor" includes the beneficiary of an irrevocable trust that is created as a method of meeting the debtor's obligation to pay a pre-existing debt;
- (4) Division (A)(4) of Section 2921.42 of the Revised Code prohibits a corporation from entering into a contract with a metropolitan housing authority, where the corporation is obligated to pay a member of the metropolitan housing authority an amount which is over five per cent of the total indebtedness of the corporation, unless all of the criteria for the exemption of Division (C) of Section 2921.42 of the Revised Code are met.

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In your letter to the Ohio Ethics Commission you ask whether the Ohio Ethics Law and related statutes prohibit a corporation from contracting with a Metropolitan Housing Authority (Authority) in light of the fact that a member of the Board of Commissioners of the Authority (Commissioner) is an employee and also a creditor of the corporation. You state that the Authority proposes to enter into a contract with the corporation for the purchase of services consisting of rental applicant screening and rental history reporting.

By way of history, you state that the Commissioner and her former husband were joint shareholders of the corporation but that, upon their divorce, the corporation purchased the Commissioner's stock in exchange for a promissory note. You also state that she sold her stock before she was appointed to the Authority's Board of Commissioners. You further state that the

sole shareholder of the corporation, her former husband, desires to cancel the promissory note and place all or a substantial majority, of the shares of the corporation in an irrevocable trust. Under the terms of the proposed trust, the Commissioner will be a beneficiary of the trust and will receive the amount owed her under the promissory note, which exceeds five per cent of the total indebtedness of the corporation, upon the sale of the corporation. You further state that the Commissioner is employed by the corporation as general manager, but that she is not a corporate officer or director, and will neither share in the profits nor receive any commission, fee, or payment of the proposed contract between the corporation and the Authority.

Division (A)(4) of Section 2921.42 of the Revised Code provides:

(A) No public official shall knowingly do any of the following: . . .

(4) Have an interest in the profits or benefits of a public contract entered into by or for the use of the political subdivision or governmental agency or instrumentality with which he is connected.

The term "public official" is defined in R.C. 2921.01(A) for purposes of R.C. 2921.42 to include any appointed officer of any political subdivision of the state. A member of a metropolitan housing authority is a public official for purposes of R.C. Section 2921.42 and is subject to its statutory prohibitions. See R.C. 3735.27, 3735.31.

The term "public contract" is defined in R.C. 2921.42(E)(1) for purposes of that section to include the purchase or acquisition or a contract for the purchase or acquisition of property or services by or for the use of a political subdivision. The Authority's purchase of services from the corporation to secure rental applicants and report rental histories is a public contract for purposes of R.C. 2921.42. The Ethics Commission has held that an interest which is prohibited by R.C. 2921.42 must be a definite and direct interest which may be either pecuniary or fiduciary in nature. See Ohio Ethics Commission Advisory Opinions No. 78-005, 81-003, and 81-008.

The first issue is whether the Commissioner would have an "interest" in the proposed contract between the Authority and the corporation as a result of her employment with the corporation. The Ethics Commission has held that an employee of a firm, who has neither an ownership interest nor a fiduciary interest in the firm, will not generally have an "interest" in the contracts entered into by his employer. See Advisory Opinion No. 78-006. However, an employee will be deemed to have an interest in his employer's contracts if: (1) he has an ownership interest in, or is a director, trustee, or officer of his employer; (2) he takes part in contract negotiations; (3) his salary is based or dependent upon the contract; (4) he receives a share of the contract's proceeds in the form of a commission or fee; (5) his employment responsibilities include participation in the administration or execution of the contract or he serves in a management position, with the responsibility to oversee the execution or administration of the contract; (6) the establishment or operation of the employing agency is dependent upon receipt of the contract; or (7) the creation or continuation of the employee's position is dependent upon his employer receiving the award of such contract. See Advisory Opinions No. 78-006, 81-008, 82-003, 86-005, and 89-006.

The Commissioner, an employee of the firm, would be considered to have a definite and direct interest in the proposed contract, if her position, duties, or compensation as general manager fall within one of the situations described above. You have stated that an applicant who has been denied housing on the basis of a report of his rental history has the right to inspect the reporting agency's information, explain the circumstances of his rental history, and include his own statement in the reporting agency's files. You have stated that it is conceivable that, under the proposed contract, an unsuccessful applicant could have contact with the Commissioner as an employee of the corporation during the process of inspecting the reporting agency's information and submitting his own statement concerning his rental history. This responsibility on the part of the Commissioner, along with her general supervisory and management responsibilities as manager of the corporation, indicate that she would have an "interest" in the contract between the Authority and the corporation, under criterion number five listed above.

You have also stated that the Commissioner was a shareholder of the corporation, but that, before her appointment to the Authority, the corporation purchased her stock in exchange for a promissory note.

Division (B) of Section 2921.42 provides:

(B) In the absence of bribery or a purpose to defraud, a public servant, member of his family, or any of his associates 'shall not be considered as having an interest in a public contract or the investment of public funds, when all of the following apply:

(1) The interest of such person is limited to owning or controlling shares of the corporation, or being a creditor of the corporation or other organization, which is the contractor on the public contract involved, or which is the issue of the security in which public funds are invested;

(2) The shares owned or controlled by such person do not exceed five per cent of the outstanding shares of the corporation, and the amount due such person as creditor does not exceed five per cent of the total indebtedness of the corporation or other organization;

(3) Such person, prior to the time the public contract is entered into, files with the political subdivision or governmental agency or instrumentality involved, an affidavit giving his exact status in connection with the corporation or other organization.
(Emphasis added.)

It is implicit from the language of Division (B) that a creditor of a corporation has, as a general matter, an "interest" in the contracts of the debtor corporation for purposes of R.C. 2921.42. Otherwise, the exception found in Division (B) for creditors who are owed five percent or less of the total indebtedness of the corporation would have no meaning or be of no effect. See Dougherty v. Torrence, 2 Ohio St. 3d 69 (1982) (in interpreting a statute, effect must be given to words used, and words used may not be deleted). Therefore, a creditor has an "interest" in the contracts of a debtor corporation for purposes of Division (A)(4) of Section 2921.42 of the Revised Code. However, Division (B) of Section 2921.42 of the Revised Code provides that, in the absence of bribery or fraud, a public servant shall not be considered to have an "interest" in a

public contract with his own political subdivision when: (1) the public servant's interest is limited to being a creditor of a corporation which is doing business with his political subdivision; (2) the amount due the public servant does not exceed five per cent of the total indebtedness of the corporation; and (3) the public servant files with the political subdivision an affidavit giving his exact status in connection with the corporation. See Advisory Opinions No. 78-001 and 78-002.

The term "creditor" is not defined for purposes of R.C. Section 2921.42. A primary rule of statutory construction is that words used in a statute must be construed according to rules of grammar and common usage. See R.C. 1.42. Furthermore, statutes "must be construed in light of the mischief they are designed to combat." City of Mentor v. Giordano, 9 Ohio St. 2d 140, 144 (1967). Black's Law Dictionary (5th ed. 1979) defines the term "creditor" as:

In its broad sense, one who has any legal liability upon a contract, express or implied . . . ; in its narrow sense, the term is limited to one who holds a demand which is certain and liquidated. In statutes the term has various special meanings dependent upon context, purpose of statute

In the instant situation, the Commissioner became a creditor of the corporation when she sold her stock to the corporation in exchange for a promissory note. The amount the corporation was obligated to pay to the Commissioner exceeded five per cent of the total indebtedness of the corporation, and the Commissioner would have been deemed to have an "interest" in the contracts of the corporation such that 2921.42(A)(4) would have prohibited the corporation from entering into a contract with the Authority.

However, you state that the corporation's sole shareholder, her ex-husband, desires to cancel the promissory note and place all, or a substantial majority, of the shares of the corporation into an irrevocable trust which would name the Commissioner as a beneficiary of a stated sum equal to the amount represented by the promissory note, which she would receive only upon the sale of the corporation. As stated above, this sum exceeds five percent of the total indebtedness of the corporation. The issue is whether the proposed cancellation of the promissory note and the creation of the irrevocable trust as an alternative method for the corporation to satisfy its obligation to pay a preexisting debt to the Commissioner will change the debtor-creditor relationship to the extent that the Commissioner would not have an "interest" in the contracts or the corporation.

The Ethics Commission has previously held that, for purposes of Section 102.02 of the Ohio Revised Code, a trust is a relationship in which one person holds a property interest, subject to an equitable obligation to keep or use that interest for the benefit of another. See Advisory Opinion No. 76-011. A debtor may create a trust as a method of paying his debt by providing a fund to be applied to the payment of those debts and by transferring legal ownership in the assets to a third person. See Cleveland Trust Co. v. Pomeroy, 16 Ohio Op. 2d 131, 134 (C.P. Cuyahoga County 1961). In the instant situation, the original obligation of the corporation to the Commissioner would not be altered by the cancellation of the promissory note and the simultaneous creation of an irrevocable trust in her favor. R.C. 2921.42(B) mandates that the amount due the public official as a creditor of a corporation doing business with her political

subdivision ' not exceed five percent of the total indebtedness of the corporation in order that the public official not be considered as having an "interest" in the contract with her own political subdivision. To hold that the sole shareholder's proposed creation of an irrevocable trust as an alternative method of satisfying the pre-existing obligation to the Commissioner alters the previously established debtor-creditor status between the corporation and the Commissioner would be to effectively circumvent the clear limitation of R.C. 2921.42(B) and the prohibition of R.C. 2921.42(A)(4). It has been stated that a public official cannot do indirectly what he cannot lawfully do directly. See City of Parma Heights v. Schroeder, 26 Ohio Op. 2d 119, 122 (C.P. Cuyahoga County 1963). Therefore, in the instant situation, even if the proposed trust were created as a method for the corporation to pay a pre-existing debt to the Commissioner, she would still be considered to be a "creditor" of the corporation for purposes of R.C. 2921.42(B) and would have an "interest" in the proposed contract between the corporation and the Authority, since the amount due her exceeds five per cent of the total indebtedness of the corporation. As described above, R.C. 2921.42 (A)(4) prohibits a public official from having an "interest" in the profits or benefits of a public contract entered into by or for the use of the political subdivision with which she serves.

R.C. 2921.42(C) however, provides an exception to the prohibition of R.C. 2921.42(A)(4), as follows:

This section does not apply to a public contract in which a public servant, member of his family, or one of his business associates has an interest, when all of the following apply:

- (1) The subject of the public contract is necessary supplies or services for the political subdivision or governmental agency or instrumentality involved;
- (2) The supplies or services are unobtainable elsewhere for the same or lower cost, or are being furnished to the political subdivision or governmental agency or instrumentality as part of a continuing course of dealing established prior to the public servant's becoming associated with the political subdivision or governmental agency or instrumentality involved;
- (3) The treatment accorded the political subdivision or governmental agency or instrumentality is either preferential to or the same as that accorded other customers or clients in similar transactions;
- (4) The entire transaction is conducted at arm's length, with full knowledge by the political subdivision or governmental agency or instrumentality involved, of the interest of the public servant, member of his family, or business associate, and the public servant takes no part in the deliberations or decision of the political subdivision or governmental agency or instrumentality with respect to the public contract.

Each of the four items enumerated above are issues of fact which, when applied to the circumstances of an individual situation, will determine whether a particular transaction fits within the parameters of R.C. 2921.42(C). See Advisory Opinions No. 80-003 and 82-007. These criteria are strictly applied against the public official, and the burden is on the official to

demonstrate that he is in compliance with the exemption. See Advisory Opinions No. 83-004 and 84-011.

Competitive bidding may be used to indicate that the services are "unobtainable elsewhere for the same or lower cost" although it is not determinative. See Advisory Opinion No. 83-004. The bidding process must be open and fair and provide for readily available and adequate notice to competitors. Id. As stated in Advisory Opinion No. 83-004:

If a particular bid is lowest, it would be some indication that the goods are "unobtainable elsewhere for the same or lower cost," but it is not determinative. Factors such as the availability and adequacy of notice to potential competitors, the openness and fairness of the bidding process, and the conditions of the market must be considered in determining whether the public official complied with Division (C)(2) of Section 2921.42 of the Revised Code.

See also Advisory Opinion No. 88-001.

Division (A)(3) of Section 2921.42 provides that no public official shall:

During his term of office or within one year thereafter, occupy any position of profit in the prosecution of a public contract authorized by him or by a legislative body, commission, or board of which he was a member at the time of authorization, and not let by competitive bidding or let by competitive bidding in which he is not the lowest and best bid.

R.C. 2921.42(A)(3) would, therefore, prohibit a member of the Board of Commissioners from profiting from a public contract authorized by the Metropolitan Housing Authority when such contract was not made pursuant to competitive bidding or where it was awarded after competitive bidding but was not the lowest and best bid. A public contract will be considered to be "authorized" by the Board of Commissioners under R.C. 2921.42(A)(3) where the contract would not have been awarded without the Board's approval. See Advisory Opinion No. 87-004.

The Commissioner will be deemed to profit from the contract between the Authority and the corporation if: (1) the establishment or operation of the corporation is dependent upon receipt of the contract; (2) the creation or continuation of her position with the corporation is dependent upon the award of the contract; or (3) the proceeds from the contract would be used by the corporation to compensate her or as a basis for her compensation. See Advisory Opinion No. 88-008. Furthermore, the Commissioner will be deemed to profit from the contract if the proceeds of the contract would affect whether she receives payment upon the sale of the corporation's stock or the amount she would receive.

The Commissioner is bound by the prohibition of R.C. 2921.42(A)(3) regardless of the fact that she did not deliberate, vote upon or otherwise authorize the public contract. (See R.C. 2921.42(A)(1) discussed below.) This prohibition continues during the Commissioner's service and for one year after she leaves the Authority. Even if the contract from which the Commissioner would profit is competitively bid and is the lowest and best bid, all of the criteria

of Division (C) of Section 2921.42, as discussed above, must still be met before the Authority and the corporation may enter into the proposed contract.

Division (A)(1) of Section 2921.42 provides:

(A) No public official shall knowingly do any of the following:

(1) Authorize, or employ the authority or influence of his office to secure authorization of any public contract in which he, a member of his family, or any of his business associates has an interest.

Division (A)(1) of Section 2921.42 prohibits a public official from authorizing or employing the authority or influence of his office to secure authorization of a public contract in which she or a business associate has an interest. As discussed above, the Commissioner would have an interest in the contract between the Authority and the corporation. Furthermore, a public officials outside employer is considered to be her "business associate" for purposes of R.C. 2921.42(A)(1). See Advisory Opinions No. 78-006, 80-003, 81-001, 84-009, and 89-008. Thus, the Commissioner is prohibited by R.C. 2921.42(A)(1) from discussing, voting upon, or otherwise using her authority or influence to secure a contract between the corporation and the Authority.

Sections 102.03 and 102.04 of the Revised Code will also restrict the conduct of the Commissioner with respect to the Authority's decision to contract with the corporation. If all criteria necessary to meet the requirements of R.C. 2921.42 as described above have been met, and the Authority contracts with the corporation, Sections 102.03 and 102.04 will condition and limit the conduct of the Commissioner in her employment as general manager of the corporation.

Division (C) of Section 102.04 reads:

(C) Except as provided in division (D) of this section, no person elected or appointed to an office of or employed by a county, township, municipal corporation, or any other governmental entity, excluding the courts, shall receive or agree to receive directly or indirectly compensation other than from the agency with which he serves for any service rendered or to be rendered by him personally in any case, proceeding, application, or other matter which is before any agency, department, board, bureau, commission, or other instrumentality, excluding the courts, of the entity of which he is an officer or employee.

Division (C) of Section 102.04 of the Revised Code prohibits the member of the Board of Commissioners of the Metropolitan Housing Authority from receiving compensation from any source, including the corporation with which she is employed as general manager, for personally rendering any service in any case, proceeding, application, or other matter that is before the agency with which she serves, the Metropolitan Housing Authority. R.C. 102.04(C) would prohibit the Commissioner from receiving compensation from the corporation for personally rendering any service with regard to the corporation's proposal to contract with the Authority that is pending before the Authority. Furthermore, an unsuccessful rental applicant could, as

described above, have contact with the Commissioner as general manager of the corporation during the process of inspecting the reporting agency's information and submitting his own statement concerning his rental history. R.C. 102.04(C) would prohibit the Commissioner from receiving compensation from the corporation for any personal service she renders on any application or any other matter that is pending before the Authority.

Division (D) of Section 102.03 prohibits a public official or employee from using the authority or influence of his position to secure anything of value that is of such character as to manifest a substantial and improper influence upon him with respect to his duties. This provision would prohibit the Commissioner from using her official position to secure any benefit or other thing of value for the corporation. She must refrain from participating as a Commissioner, formally or informally, in the Authority's decision to contract with the corporation, and, if the Authority does contract with the corporation, in any matter regarding the contract. See Advisory Opinions No. 88-004 and 88-005.

Division (A) of Section 102.03 of the Revised Code provides, in pertinent part:

No present or former public official or employee shall, during his public employment or service or for twelve months thereafter, represent a client or act in a representative capacity for any person on any matter in which he personally participated as a public official or employee through decision, approval, disapproval, recommendation, the rendering of advice, investigation, or other substantial exercise of administrative discretion As used in this division, "matter" includes any case, proceeding, application, determination, issue, or question, but does not include the proposal, consideration, or enactment of statutes, rules, ordinances, resolutions, or charter or constitutional amendments. As used in this division, "represent" includes any formal or informal appearance before, or any written or oral communication with any public agency on behalf of any person. (Emphasis added.)

The Commissioner is prohibited by R.C. 102.03(A) from representing her employing corporation or any other person before the Metropolitan Housing Authority or any other public agency on any matter in which she personally participated as a member of the Board of Commissioners of the Metropolitan Housing Authority. See Advisory Opinion No. 87-001.

Division (B) of Section 102.03 reads:

No present or former public official or employee shall disclose or use, without appropriate authorization, any information acquired by him in the course of his official duties which is confidential because of statutory provisions, or which has been clearly designated to him as confidential when such confidential designation is warranted because of the status of the proceedings or the circumstances under which the information was received and preserving its confidentiality is necessary to the proper conduct of government business.

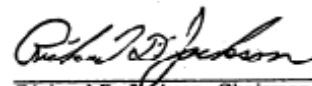
The Commissioner is prohibited from disclosing confidential information to her employing corporation or any other party, or using such confidential information, without

appropriate authorization. No time limitation exists for this prohibition, and it is effective while the Commissioner serves with the Metropolitan Housing Authority and after she leaves the Metropolitan Housing Authority. See Advisory Opinion No. 88-009.

Section 3735.29 of the Revised Code prohibits a member or employee of a metropolitan housing authority from having "any interest, directly or indirectly in any contract for property, materials, or services to be acquired by said authority." (Emphasis added.) See Advisory Opinions No. 78-006 and 84-006; and Ohio Op. Att'y. Gen. No. 82-008 for discussions of analogous provisions. The Ethics Commission does not render advisory opinions with respect to R.C. 3735.29. The application of R.C. 3735.29 to the Commissioner's situation is for the determination of the legal advisor to the Metropolitan Housing Authority.

This advisory opinion is based on the facts presented, and is rendered only with regard to questions arising under Chapter 102. and Sections 2921.42 and 2921.43 of the Revised Code.

Therefore, it is the opinion of the Ethics Commission, and you are so advised, that: (1) For purposes of Division (A)(4) of Section 2921.42 of the Revised Code a creditor has an interest in the contracts of a debtor corporation, unless he is able to meet all of the criteria for the exemption of Division (B) of Section 2921.42; (2) Division (B) of Section 2921.42 of the Revised Code provides that, in the absence of bribery or fraud, a public servant shall not be considered to have an "interest" in a public contract with his own political subdivision when: (a) the public servant's interest in a corporation doing business with his own political subdivision is limited to being a creditor of the corporation; (b) the amount due the public servant does not exceed five per cent of the total indebtedness of the corporation; and (c) the public servant files with the political subdivision an affidavit giving his exact status in connection with the corporation; (3) As used in Division (B) of Section 2921.42 of the Revised Code, the term "creditor" includes the beneficiary of an irrevocable trust that is created as a method of meeting the debtor's obligation to pay a pre-existing debt; and (4) Division (A)(4) of Section 2921.42 of the Revised Code prohibits a corporation from entering into a contract with a metropolitan housing authority, where the corporation is obligated to pay a member of the metropolitan housing authority an amount which is over five per cent of the total indebtedness of the corporation, unless all of the criteria for the exemption of Division (C) of Section 2921.42 of the Revised Code are met.


Richard D. Jackson, Chairman
Ohio Ethics Commission