



## STATE ETHICS COMMISSION

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### FORMAL ADVISORY OPINION-EDITED FOR PUBLICATION

November 19, 2010

Re: Conflicts of Interest Arising in Connection with Stock Ownership  
G.S. 138A-36(a), (b), and (c); G.S. 138A-38(a)(1)  
AO-E-10-005

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Dear Requester:

This formal advisory opinion addresses the question of the extent to which the State Government Ethics Act ("Ethics Act"), North Carolina General Statutes ("G.S.") Chapter 138A, restricts public servants who own stock in a bank or financial services corporation from taking official action in connection with the selection of that bank to provide certain financial services to the public servant's agency.

This opinion was adopted by the Commission at its November 19, 2010, meeting.<sup>1</sup>

#### **I. Brief Conclusion.**

In applying the conflict of interest provisions of the Ethics Act, the value of securities owned by a public servant in a particular business is the value at the time of the official action. If the securities are valued at \$10,000 or more, a public servant should consider whether the official action would result in a financial benefit or detriment to the business and if so, the extent to which the public servant would be influenced or would be viewed as being influenced by that financial benefit. If the public servant abstains from that official action, he or she should notify the employing entity in writing and disclose the reasons for that recusal, including the fact that the public servant owns securities valued at \$10,000 or more in the company.

#### **II. Facts.**

You serve on a non-advisory board that is subject to the requirement of the Ethics Act. Therefore, you and the other members of that board are public servants governed by the Act's conflict of interest standards. In conducting certain activities pursuant to its statutory authority,

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<sup>1</sup> Please see the enclosure entitled "Formal Advisory Opinions Issued by the State Ethics Commission" for further information regarding the protections offered to individuals receiving those opinions.

the board must consider and approve the selection of financial institutions to provide various services. Board members may own stock in those financial institutions.

### **III. Applicable Statutory Provisions.**

#### **A. G.S. 138A-36(a) and 138A-31(a) Conflicts Standards.**

G.S. 138A-36(a) prohibits a public servant from participating in an “official action”<sup>2</sup> if that public servant or a “person with whom the public servant is associated” may incur:

- “A reasonably foreseeable financial benefit”
- Which would impair the public servant’s “independence of judgment” or otherwise influence the public servant’s participation in that official action.

“Financial benefit” includes a “direct pecuniary gain or loss” to the public servant or a “person with which the ... public servant is associated” or a “direct pecuniary loss to a business competitor” of the public servant or a person with which the public servant is associated. G.S. 138A-3(14c).

“Person with which the public servant is associated” includes a “business with which associated,” defined to include a business in which the public servant or his/her immediate family owns an interest of \$10,000 or more or 5% of the business, whichever is less. G.S. 138A-3(3)c. and 138A-3(27d). This would include the ownership of securities (including stock) in a particular business if the value of those securities is \$10,000 or more.

G.S. 138A-36(b) requires that a public servant who has a conflict of interest as defined in subsection 36(a):

- “Abstain from taking any verbal or written action”
- “In furtherance of the official action.”

The public servant is also required to submit written “reasons for the abstention” to the employing entity.

G.S. 138A-31(a) similarly prohibits a public servant from taking an “official action” in certain circumstances where the public servant or a “business with which the public servant is associated” would derive a direct or indirect financial benefit from that action. That provision excludes circumstances where the financial benefit is “so remote, tenuous, insignificant, or speculative” that a reasonable person would conclude that the public servant’s ability to perform

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<sup>2</sup> “Official action” includes “[a]ny decision, including administration, approval, disapproval, preparation, recommendation, the rendering of advice, and investigation, made or contemplated in any proceeding, application, submission, request for ruling or other determination, contract, claim, controversy, investigation, charge, or rule making.” G.S. 138A-3(25).

his or her official duties would not be compromised. Subsection 31(a) does not specify the manner in which the public servant should abstain from taking official action.

**B. G.S. 138A-36(c) Conflict of Interest Standard.**

G.S. 138A-36(c) also requires that a public servant:

- “Remove himself or herself” from a “proceeding,”<sup>3</sup>
- “Considering the particular circumstances and type of proceeding involved,”
- “To the extent necessary to protect the public interest and comply with the Ethics Act,”
- If the public servant’s impartiality might reasonably be questioned due to a “familial, personal, or financial relationship” with a participant in the proceeding.

**C. G.S. 138A-38(a)(1) Class Safe Harbor.**

G.S. 138A-38(a) lists circumstances under which a public servant may take official action notwithstanding the existence of a conflict of interest. They include situations where the official action is ministerial only or where the public servant is the only person who has legal authority to take an official action. In addition, subsection 38(a)(6) provides that a public servant who abstains from an official action may be counted for purposes of establishing a quorum, but must abstain from taking further action.

G.S. 138A-38(a)(1) also allows a public servant to take an official action, notwithstanding the existence of a conflict of interest, if the financial benefit or detriment that would accrue to the public servant, a “person with which associated,” or a “participant” in a proceeding:

- As a member of “a profession, occupation, or general class,”
- Is “no greater” than that which would accrue to “all members of that profession, occupation, or general class.”

**IV. Application of the Ethics Act’s Conflicts Provisions to Your Questions.**

A response to your specific questions follows:

- A. In determining whether the value of securities is \$10,000 or more, should the original cost basis for the securities, the amortized basis for determining gain or loss on disposition, or the market value at the time of the official action be considered?**

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<sup>3</sup> Defined to include a “quasi-judicial” proceeding or a “quasi-legislative” proceeding.

In considering whether a public servant owns \$10,000 or more in securities for purposes of determining whether a company is a “business with which associated” under G.S. 138A-36(a) and G.S. 138A-31(a), the value of the securities should be calculated at the time the public servant is considering taking the official action. Therefore, if individual members of the board own securities in a financial institution valued at \$10,000 or more at the time of an official action, and that action would result in a financial benefit to that financial institution, the conflicts standards of G.S. 138A-36(a) and 31(a) would be triggered. This ownership interest could also be considered a “financial” relationship under G.S. 138A-36(c).

However, determining that the value of an interest in a business is \$10,000 or more is just the first step in identifying whether a public servant has a conflict of interest that would require that he or she abstain from taking an official action.

**B. Are we correct in that the \$10,000 is the amount that precludes a member from voting?**

The value of the public servant’s interest is just one of the criteria for determining whether the conflicts standards of G.S. 138A-36(a), 31(a), and 36(c) would require that a public servant abstain from the matter.

Once it is determined that an official action could affect a “business with which associated,” the public servant must consider whether the business may incur a reasonably foreseeable financial benefit (or detriment to a business competitor) from the matter under consideration,<sup>4</sup> and if so, whether that financial benefit (or detriment to a competitor) would influence or could reasonably be seen to influence the public servant’s official actions. Similarly, G.S. 138A-36(c) requires that a public servant “remove himself or herself to the extent necessary” if the public servant’s “impartiality might reasonably be questioned” due to a financial relationship with the business.

Although the board’s decision to hire a financial institution would likely result in a financial benefit to that business, it is unclear whether a member’s ownership of a threshold amount of securities in that business would influence the member in approving the award of a contract. This would depend upon several factors, including the amount of the financial benefit to the business relative to its overall size and worth and whether that financial benefit would impact the value of securities owned by the public servant. However, if the financial benefit to the financial institution is relatively insignificant, that benefit would be unlikely to influence the board member in awarding a contract to that business.

You have not provided sufficient facts to determine if an actual conflict of interest exists. The existence of a conflict of interest is determined on a case by case basis and varies according to the individual facts. We have provided general guidance of how to proceed in this circumstance but we recommend that you proceed with caution in determining if an actual conflict exists.

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<sup>4</sup> Or a “direct or indirect financial benefit” under G.S. 138A-31(a).

In general, if a conflict of interest exists that would otherwise preclude the public servant's actions, the next step would be to consider whether the G.S. 138A-38(a)(1) "class" safe harbor applies. However, subsection 38(a)(1) would be inapplicable here, since the actions taken by the board members would apply to an individual financial institution, not a class of those businesses.

**C. Is it necessary for the member to divulge the amount and identity of the financial services corporation in which he or she owns securities at the time of the voting, or may the member abstain without disclosure of the information?**

Subsections 31(a) and 36(c) do not provide any guidance regarding the information that must be provided by the public servant in connection with his or her recusal from taking an official action. Subsection 36(b), applicable to recusals required by subsection 36(a), requires that the public servant "submit in writing to the employing entity the reasons for the abstention." It also requires that the abstention be recorded in the employing entity's minutes.

The information provided by the public servant in connection with that abstention should include the facts underlying the public servant's reasons for abstaining. In circumstances where the public servant's abstention results from his or her ownership of stock in a particular business, the public servant must disclose the fact that he or she owns at least \$10,000 worth of stock in the business. However, the total value of the shares owned by the public servant need not be disclosed in connection with that abstention.

**V. Closing.**

Thank you for contacting the State Ethics Commission. Please do not hesitate to call the Commission's staff if you have any questions about the foregoing formal advisory opinion.

State Ethics Commission

By: \_\_\_\_\_  
Robert L. Farmer  
Chairman

**Formal Advisory Opinions Issued by the State Ethics Commission**  
**Pursuant to the Ethics Act**

Upon the written request of a public servant or legislative employee, G.S. 138A-13(a) of the State Government Ethics Act (“the Ethics Act”) authorizes the State Ethics Commission (“Commission”) to issue formal advisory opinions on the “meaning and application” of the Ethics Act “and the public servant’s or legislative employee’s compliance therewith.” All opinions have prospective application only, are limited to the particular facts presented, and confer limited civil immunity upon a requester who follows the advice given. G.S. 138A-13(a) and (a2).

Reliance upon a formal advisory opinion immunizes the public servant or legislative employee making the request from (1) investigation by the Commission, except the alleged violation of criminal law while performing his or her official duties, (2) adverse action by his or her employing entity, or (3) investigation by the Secretary of State. G.S. 138A-13(a2).

Once issued by the Commission, formal advisory opinions are published in a redacted format on the Commission’s website within 30 days of issuance. G.S. 138A-13(d). Otherwise, requests for advisory opinions, the opinions themselves, and all materials related to the opinions are confidential and are not public records. G.S. 138A-13(e).