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February 10, 2005

RQ-0320-GA

FILE # ML-44129-05
I.D. # 044129

The Honorable Greg Abbott
Attorney General
Office of the Attorney General
P. O. Box 12548
Austin, Texas 78711-2548

Subject: Request for Opinion re Conflict of Interest Question

Dear General Abbott:

A Member of the Board of Regents of The Texas A&M University System is a partner in a law firm that had an outside counsel agreement with The Texas A&M University System in FY 2003-2004 for legal services. The Member has been sworn in and has performed the duties of a Regent, although his confirmation by the Senate cannot take place until the next session of the Legislature. The contract predates both his appointment to the Board and his joining the law firm. The firm continued to provide intellectual property legal services to the A&M System since then, and has submitted for payment a number of bills for fees and expenses incurred in prosecuting various patents belonging to the A&M System.

We respectfully request an opinion from your office on the following issues:

1. What effect, if any, did the fact that a firm partner became a Member of the Board of Regents have on the legal status of the pre-existing contract between the law firm and the A&M System?

2. Is the firm entitled to payment for services it rendered under the agreement subsequent to the date the partner became a regent?

BACKGROUND

The Texas A&M University System ("TAMUS") had a contract for outside counsel services with the law firm of Locke Liddell & Sapp ("the firm") for the beginning in the 2001-2002 state fiscal year and renewing for each subsequent year. The contract was awarded after a Request for Proposals for legal services was published and proposals received by TAMUS. This was one of many contracts that were awarded to numerous firms to provide intellectual property legal services. The firm performed various legal services and was paid on several occasions during the year.

On October 22, 2003, the Honorable Bill Jones was sworn in as a member of the Board of Regents of The Texas A&M University System. The following month, November of 2003, Mr. Jones became a partner in the firm. He practices in Austin in the governmental relations section of the firm. He does not practice in the intellectual property section of the firm that is centered in Houston and Dallas, nor direct the legal services of the intellectual property section. Further, he has never performed legal services for or on behalf of TAMUS in any regard.

The firm continued to provide legal services on a number of intellectual property matters from November 2003 through June 2004. The firm did not notify TAMUS of Mr. Jones' partnership status, although it became generally known via media and other informal sources, because apparently, his membership was not considered relevant to any conflict issues, given his totally different practice area, lack of influence and direction over the contract with TAMUS, and lack of benefit other than as a general partner of the overall firm. The services received by TAMUS were performed to the satisfaction of TAMUS. Billings for that period of time totaling over $18,000 have been provided to TAMUS with the expectation that they would be paid in accordance with the terms of the contract.

Prior Opinion re Contracting with Outside Counsel

State agencies possess authority to contract for outside legal services.[1] Contracts between state agencies and private counsel must be approved by the Attorney General's Office.[2] Requirements for competitive procurement of such services are established by that office.[3] In accordance with those requirements, TAMUS published a Request for Proposals in the Texas Register. Numerous firms responded to the RFP and many of them were awarded contracts for legal services. The contract under discussion was approved by the Attorney General's Office on September 25, 2003.

In 1993 The Texas A&M University System sought an opinion from the Attorney General concerning conflict of interest principles as applied to a contract with a law firm in which a member of the board became a shareholder after the execution of the agreement. On September 1, 1992, Mr. Ross Margraves became a shareholder in the law firm of Winstead, Sechrest & Minick (WSM). For two years prior to that date, WSM had been providing legal services to the A&M System under a contract for outside counsel services related to a pending lawsuit. The attorney at WSM who was providing the services was part of its Dallas office, whereas Mr. Margraves officed in Houston. The legal services were in the area of intellectual property which was not an area in which Mr. Margraves practiced. The case was a complex dispute involving intellectual property and contract rights and had been ongoing for more than two years. WSM and Margraves had agreed that he would be completely shielded from any connection to the

[1] Tex. Gov. Code sec. 2254.153
[2] Tex. Gov. Code sec. 402.0212
[3] Tex. Gov. Code sec. 2254.154

case and would not receive any proceeds from the contract with the A&M System. WSM had provided services after September 1, 1992 up through October 12, 1992 when it was notified of the potential conflict issue. Mr. Margraves and the firm agreed that he would receive no salary from the firm for that time period in order to cure any conflict issues.

Despite all of those measures intended to protect the public interest, in L. O. No. 093-012 the Attorney General cited the strict Meyers rule and found that the firm could not continue to provide legal services to the System. In addition, no payment could be made for the services that had been rendered after September 1, 1992. The A.G. acknowledged that this would result in the loss of valuable legal advice and knowledge for which the System had been paying for two years, but declared there could be no other result under the common law of Texas.

The facts of the present situation are virtually identical to those presented in L.O. No. 093-012. We continue to be of the opinion that the common law of Texas does not support that opinion. In order to conclude that a contract is void under these circumstances, a court would have to find that the contract is against public policy.

> As a general rule, if a contract is not immoral in itself or in conflict with any express law, *it will not be contrary to public policy. Indeed, in doubtful cases a presumption exists in* favor of the validity of the transaction. Thus, in those cases in which public policy has not been settled by recognized principles, a contract will be in violation of public policy only if the injury to the public is clearly apparent. Where there is a claim that a contract contravenes public policy and is unenforceable, review should be approached with caution and only where the cases fall within the purposes for judicial intervention.[4] *(Citations omitted)*

There is no statutory provision in state law that addresses this situation. Therefore, reference to common law as expressed by the courts of the state is necessary.

Regrettably, the Attorney General has consistently held that the standard for deciding whether a conflict of interest exists is an absolute test founded upon dicta contained in a single case from a single court of appeals.

In light of the facts in this case, and of the potential harm that may befall both the state and future members of governing boards of state institutions of higher education, we assert that public policy does not demand that an agreement be voided if an individual who has *any amount* of interest in a contractual relationship created prior to the time he or she became a member of the governing board.

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[4] TXJUR, CONTRACTS § 143

Conflicts of Interest and Governing Bodies

Texas common law on conflicts of interest for members of governing bodies imposes an overly strict standard that may not be applicable to current checks and balances and reviews. In Attorney General Opinion JM-671 (1987)[5], the Attorney General found that Texas A&M University could not enter into an agreement with a company that was a wholly owned subsidiary of a corporation that was owned in part by a member of the Board of Regents. The actual interest owned by the Regent would have totaled no more than 1% of the ultimate value. The opinion cites and reaffirms the seminal Texas case on conflicts of interest for members of public bodies, Meyers v. Walker, 276 S.W. 305 (Tex. Civ. App.—Eastland 1925, *no writ*). In that case the Court of Appeals stated the rule as follows:

> If a public official directly or indirectly has a pecuniary interest in a contract, no matter how honest he may be, and although he may not be influenced by the interest, such a contract so made is violative of the spirit and letter of our law, and is against public policy. Meyers v. Walker, at 307.

Various statutes have been enacted that permit certain officials to recuse themselves from transactions in order to cure a conflict. At the time that JM-671 was issued, no such statute existed for contracts entered into by an institution of higher education.[6]

In JM-817 (1987), the Attorney General found that Stephen F. Austin State University could not contract for the purchase of goods from a company that employed the spouse of a member of the SFA Board of Regents. The fact that the board did not involve itself directly in any of the purchases was not considered to be sufficient to outweigh the conflict issue. Nor was the fact that university officials would be the ones who actually executed purchase orders or agreements, since any authority they had was delegated to them from the Board of Regents. The opinion states, in part:

> A subordinate officer or employee has authority to contract for the university only because the board has adopted a rule, regulation or order delegating such power. . . [Citations omitted.] The board may resume exercising that authority itself by repealing the rule, regulation, or order delegating it. The employee who approves the contract is accountable to the board for his decisions about the contract and for his job performance generally. If a dispute with the contractor arises, the board will very likely participate in resolving it. Thus, the board cannot divest itself of the responsibility for the contract with the firm, even though subordinate officers or employees may purchase products without regental approval.

In L.O. 97-072, the A.G. found that the Texas Department of Criminal Justice could not enter into a contract with a construction contractor because a member of the TDCJ board was a 40% owner in an insurance company that provided performance

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[5] Attached as Exhibit C

[6] It was argued, albeit unsuccessfully, that Article 6252-9b, sec. 6, V.T.C.S. (now §572.058, Tex. Govt. Code) abrogated the *Meyers* rule and created the necessary statutory recusal process for contracts that come before the Board of Regents. The A.G. rejected this argument and opined that Article 6252-9b did not apply to contracts because it did not "include any language indicating that [it] was intended to apply to contracts, nor does its legislative history suggest an intent to modify the Meyers v. Walker rule."

bonds and casualty insurance to the contractor. The opinion noted that, "If the insurance client secures the contract, its volume of business and payroll will increase and the board member's insurance company will make more money because the costs of the insurance it provides are directly affected by the size of the client's payroll." This, in combination with the strict Meyers rule, was sufficient to support an opinion finding that a conflict of interest precluded the TDCJ board from entering into the agreement with the contractor.

Pre-Meyers Decisions Are Not Supportive of the Attorney General's Strict Opinions

The standard applied by the Attorney General's Office and the few courts that have spoken on the subject is an absolute one. As was seen in the S.F.A. opinion (JM-817), even a miniscule interest in a contract (0.2%) was enough to render a transaction void. The rule purportedly supported by Meyers v. Walker is far more broad than that opinion will support.

The case was decided in 1925 by the Eastland Court of Appeals. It arose after the mayor and a city commissioner of Lamesa took a trip to Philadelphia at the expense of a prospective paving contractor (Panhandle Construction Company) which, along with other companies, had a bid pending before the city at the time. There was conflicting evidence concerning whether an agreement was actually reached between the officials and Panhandle for the contractor to pay the expenses. Following the trip, the city awarded the contract to Panhandle. At some time after the contract was signed several city officials were replaced and the new city government ratified the original contract. The plaintiffs sought to enjoin the city from paying Panhandle for its work under the contract. The plaintiffs argued that because the contract was null and void and against public policy it could not have been ratified. They contended that the fact that the officials accepted the trip from Panhandle before awarding the contract was sufficient by itself to render void any subsequent contract between the city and Panhandle. They also alleged that the officials and Panhandle had violated Article 376 of the Penal Code.[7] The trial court disagreed and instructed the jury to return a verdict for the defendants.

The Court of Appeals reversed the trial court and remanded the case for another trial because there was sufficient evidence presented at trial to support submission of the case to a jury. The author of the opinion states that he felt the case should have

[7] "If any officer of any county in this state, or of any city or town therein, shall become in any manner pecuniarily interested in any contracts made by such county, city or town, through its agents or otherwise, for the construction or repair of any bridge, road, street, alley or house, or any other work undertaken by such county, city or town, or shall become interested in any bid or proposal for such work or in the purchase or sale of anything made for or on account of such county, city or town, or who shall contract for or receive any money or property, or the representative of either, or any emolument or advantage whatsoever in consideration of such bid, proposal, contract, purchase or sale, he shall be fined in a sum of not less than fifty nor more than five hundred dollars."

been rendered rather than remanded, but that he did not desire "to go to the extent of dissenting." He states,

> The writer has grave doubts that this cause should be remanded, for the reason, when this contract was made by admission of city, the vice existed, and the interest would be presumed. The fact the Panhandle Construction Company denied making such agreement would not alter or change the matter, because the city commission who first entered into this contract did so with the understanding that the bidder would reimburse the expenses of the inspection trip, and to that extent the officials manifestly would be interested. At 308.

The opinion reflects the author's strong inclination as dicta to find a conflict existed sufficient to preclude sending the case back to a jury. Thus, the part of the decision that has been repeatedly cited by the Attorney General as authority for an absolute standard[8] is contained in dicta.

The actual holding of the case was that the trial court erred in removing the case from the jury because there was a disputed issue of fact concerning whether an agreement was reached concerning the expenses for the trip. The court did not rule on the issue of whether the contract was void *ab initio* or whether the city had the ability to ratify it at a later date. The court expresses its opinion that the contract could be void, but it never went so far as to hold that it was void.

It is important to note as well that in this case the city officials had already received a benefit from the contractor prior to execution of the paving contract. Such is not the case in the situation at hand. In addition, an examination of some of the authorities cited by the Meyers opinion in support of its absolute doctrine reveals that the facts of these cases vary markedly and none of them align with the facts presented in this opinion request. The Meyers opinion cites Texas Anchor Fence Co. v. City of San Antonio, 30 Tex. Civ. App. 561, 71 S. W. 301. In that case an alderman had paid off one of the city's creditors because the city did not have the funds to pay its bill. The alderman later presented the debt to the city for reimbursement. The court found that the debt could not be paid because the alderman was in violation of the Penal Code and a similar provision of the city charter. The case was not decided upon common law grounds.

The Meyers opinion also cites Knippa v. Stewart Iron Works (Tex. Civ. App.) 66 S. W. 322; 19 R. C. L. § 196, pp. 739, 897. In that case Knippa was a county commissioner who participated in awarding a contract for construction of a county building. Later, after the original contractor could not complete the job and a surety company stepped in and hired a second contractor, he loaned the new contractor $1,000 to be secured by the proceeds of the contract. The new contractor also abandoned the job and it was taken over by another. After the project was completed,

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[8] "If a public official directly or indirectly has a pecuniary interest in a contract, no matter how honest he may be, and although he may not be influenced by the interest, such a contract so made is violative of the spirit and letter of our law, and is against public policy." Meyers v. Walker, at 307.

Knippa presented his lien for payment by the county for the work of the second contractor. The county would not pay him and litigation ensued. The Court of Appeals ruled that he could not be paid by the county because he had violated his oath as a commissioner by his acquisition of a pecuniary interest in a county contract which he had approved in his official capacity. The court noted that Knippa had placed himself in a conflict or a potential conflict. The court did not say that a commissioner could never have any interest at all in a contract with the county. It said that when a commissioner took upon himself the role of a creditor of the county he violated public policy. In the case under discussion, the regent could not reasonably be said to have done anything to purposefully make himself a potential creditor or claimant against the interests of the A&M System. His acceptance of a partnership in a large law firm to practice in an area unrelated to any of the System's business is in no way comparable to purchasing a debt owed by the System.

The Meyers opinion also cites Graves & Houtchens v. Diamond Hill Independent School District (Tex. Civ. App.) 243 S. W. 638, as authority for finding that the contract with the paving company was invalid. However, that case does not involve a conflict of interest by a public official serving on a governing body. It concerned a contract between a school board and a law firm for lobbying services. The court found that the school board had no authority to employ counsel and spend public money for lobbying.

Meyers v. Walker as Authority

Meyers has been cited as authority in only three cases in Texas jurisprudence. In Hager v. State, ex rel. TeVault (Tex. Civ. App. 1969) 446 S.W.2d 43, the case involved a question of conflict when a city councilman whose recall was being demanded proceeded to vote on a resolution concerning the city's appeal from a writ of mandamus ordering it to hold the recall election. In Robinson v. Hays (Tex. Civ. App. 1932) 62 S.W.2d 1007, the issue was whether a candidate for re-election to a city council who was a party to an election contest could participate in his official capacity in determining the validity of the election. In City of Edinburg v. Ellis[9] (Tex. Com. App. 1933) 59 S.W.2d 99, a city council member had conspired with a vendor to overcharge the city for goods and services. Meyers was cited to support the principle that it is a general rule that municipal contracts in which officers or employees of the city have a personal pecuniary interest are void. In Hager and Robinson there was no question of contracts or pecuniary interest. Both cases involved official actions that conflicted with the personal interest of the official in holding the office.

In marked contrast to the small number of courts that have looked to Meyers for authority, the Office of the Attorney General has cited the case in over 40 opinions issued since 1978. No serious effort has been made to examine the roots of the case, or even what it actually stands for. In fact, the opposite is true: the office has expanded

[9] Meyers is mentioned in Delta Elec. Const. Co. v. San Antonio (Tex. Civ. App. 1969) 437 S.W.2d 602 but only as part of a quotation from City of Edinburg.

the rule it created to reach beyond the relationship between a board member and the public body.

Expansion and Outcomes of Meyers Doctrine

The TDCJ opinion (L.O. 97-072) took the Meyers absolute standard to a new level when it found a conflict existed because a company that had no contract with the agency *might* benefit *if* it underwrote insurance for the successful contractor. The result is a type of "second generation" conflict of interest: if a governing board member *may potentially* receive some amount of benefit because he or she has some interest in an entity that *may potentially* do business with an entity that is awarded a contract, there is a violation of public policy. Conceivably, this application of Meyers could make void all state agency contracts with entities that have an independent relationship with a firm or company in which a board member has any type of interest. For example, a contract for the purchase of office supplies could be found to be void if a board member owned an interest in a real estate firm that owned the building in which the office supply store is located. Such a tortuous result is manifestly unsupportable. Vendors and other contractors doing business with state agencies should not be required to run the risk of having their agreements voided at some future time because of unrelated or remotely related interests of present—and potential—members of a governing board.

An interest in a valid contract that inures to a member of a governing board after the contract is executed and without any action of the member should not be fatal to the contract. In the circumstances presented herein, there was no opportunity for the board member to have exerted any influence over the contracting process. He was neither a board member nor a partner in the law firm at the time it was executed. All of the firm's billings under the agreement are scrutinized, reviewed and approved at several levels (including the Attorney General's Office) for the purpose of ensuring that amounts are not overbilled or improperly paid. The regent has no input into the process of providing or paying for the legal services rendered under the agreement. The parties entered into the agreement in good faith and the firm continued providing services in good faith after the regent became a partner. There is not even a trace of evidence that he or the firm have received any benefit other than what was properly contracted for in the past.

The environment for public contracting has undergone dramatic changes since 1924. The state has taken great steps toward guarding the public interest in contracts made by public agencies. Contracts and the processes for obtaining goods and services are statutorily declared to be public information.[10] At the time the Meyers opinion was written, there were no Open Meetings or Public Information Acts in Texas. Public officials were not required to file annual financial disclosure reports as they are today.

[10] See Tex. Govt. Code §552.022

The position described in past Attorney General Opinions can be described as a "zero tolerance" standard. If applied in the context of modern business and professional practices the cure becomes worse than the disease. In addition, this zero tolerance has been applied in a manner that apparently renders legally executed agreements void upon the happening of an unrelated subsequent event.

When selecting nominees for state boards, governors seek out persons who are experienced and qualified to serve the needs of increasingly complex state institutions. Business acumen, financial knowledge, and professional experience are required in order for board members to govern in an increasingly complex financial environment of state government and higher education. Simultaneously, global and national commerce are becoming more integrated as business interests intersect in countless areas of influence.

Assuming, *arguendo*, that the public policy of Texas requires that contracts made prior to appointment of a board member be voided for no reason other than the fact that the member may benefit from their continued existence, there is a wide range of issues that arise as a consequence.

- Are state university systems responsible for monitoring the business interests of board members?

- Should board members be required to report all of their business interests to the institutions at all times?

- Does a board member have a legal duty to inquire about all of the university system's business arrangements before he or she makes an investment?

- Should contracts executed by universities contain a provision notifying the contracting party that the entire agreement is subject to being rendered void without notice or opportunity to cure if a member of the governing board acquires a pecuniary interest in the contractor, or in an entity that does business with the contractor?

- If the size of the interest is considered irrelevant, how far does the prohibition extend when a regent owns interests in companies that own interests in other companies at the national and multi-national level?

- If a board member acquires an interest through no act of his or her own, such as by means of an inheritance, does the strict application rule apply?

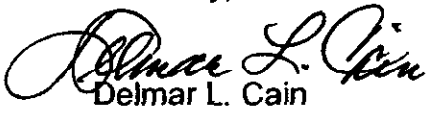
- Should the governor's office undertake to research and identify contracts that a state university system has in effect before naming an individual to fill a regent's position?

- What causes of action may contractors have against the state and state officials when an ongoing contract is voided by the appointment of a new member, or by the acquisition of any size of interest by a sitting member?

In summary, we are concerned that the past opinions of the Attorney General's office have created a standard that is not in the best interest of the state nor supported by any valid authority. Further, it disserves the interests of the public to invalidate agreements that are otherwise valid and have been performed in accordance with their agreed upon terms.

Your consideration of our request is greatly appreciated.

Sincerely,



Delmar L. Cain
General Counsel

xc: Members, Board of Regents
Chancellor Robert D. McTeer