CLIENT NEWS BRIEF

State's Top Court Rules that Contractors Can be Prosecuted for Conflict of Interest

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The California Supreme Court has ruled that an independent contractor can be criminally liable for a conflict of interest under California Government Code section 1090, expanding the universe of penalties a contractor can face for violating the statute and reversing a prior appellate court ruling that exempted contractors from criminal liability for such conflicts.

The Court's decision in *People v. Superior Court (Sahlolbei)* (June 26, 2017, No. S232639) ___ Cal.5th ___ only applies to independent contractors who have been entrusted with entering into transactions on behalf of the public agency. But due to an expansion of government and public contracting in which regular employees and even consultants can have control over the public purse, the decision has broad implications for all California public agencies.

Section 1090 prohibits public officers and employees from making contracts in which they have a financial interest when acting in their official capacities. Generally, any contract made in violation of section 1090 is void and cannot be enforced. Criminal penalties for a willful violation include a fine of up to $1,000 or imprisonment, and a lifetime ban on holding public office.

Hossain Sahlolbei worked as a surgeon at a Riverside County hospital and served on the hospital's executive committee, both in an independent contractor capacity. Sahlolbei negotiated a $36,000 per month contract with an anesthesiologist at the committee's behest plus $10,000 for moving expenses. He then pressured the hospital to hire the anesthesiologist for $48,000 a month, with $40,000 for moving expenses. Sahlolbei instructed the anesthesiologist to deposit his paychecks into Sahlolbei's bank account, and the surgeon paid the anesthesiologist $36,000 a month and pocketed the rest. He was later charged with violating section 1090.

In reversing the appellate court's judgment dismissing the charge, the Supreme Court held that independent contractors are not categorically excluded from prosecution under section 1090 and that an independent contractor who has been retained or appointed by a public agency and whose actual duties include engaging in or advising on public contracting is charged with acting on the agency's behalf. This makes such contractors fully subject to the statute. The Supreme Court found that Sahlolbei violated section 1090 because there was evidence that hospital leadership asked him to assist in identifying doctors to recruit to the hospital, which he actually did and directly profited from.

As the Supreme Court provided in a hypothetical, a stationery supplier that sells paper to a public agency would ordinarily not be liable under section 1090 if it advised the agency to buy pens from its subsidiary, because the supplier was not engaging in a transaction on the agency's behalf. However, a person who was initially hired by an agency as an officer or employee with contracting responsibilities and then rehired as an independent contractor to perform the same duties would be subject to section 1090.

The Court also expressly reversed the Second District Court of Appeal decision


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in *People v. Christiansen* (2013) 216 Cal.App.4th 1181 (*Christiansen*), reasoning that the Legislature intended for section 1090 to apply to certain contractors in both the civil and criminal liability contexts. In *Christiansen*, a school district's planning and facilities director, who served the district as an independent contractor, was prosecuted for violating section 1090 after she advised the school district to hire her consulting company for facilities management services, among other self-dealings. The appellate court held that prior courts' expansion of the statutory term "employees" to apply to independent contractors made them civilly but not criminally liable under section 1090. The Supreme Court disagreed with that conclusion.

Since *Christiansen*, California courts have applied civil liability under section 1090 to independent contractors in a series of "lease-leaseback" cases involving companies that provided "preconstruction" consulting services to school districts that later hired them as lease-leaseback contractors. (See 2017 Client News Brief No. 32, 2016 Client News Brief No. 29 and 2015 Client News Brief No. 30.) The Supreme Court decision in *Sahlolbei* raises the possibility that such contractors can now be either or both civilly and criminally liable under section 1090.

The Supreme Court limited its decision by refusing to express a view on whether an independent contractor can be held criminally liable under section 1090 for conduct that occurred during the time frame between the decisions in *Christiansen* and *Sahlolbei*.

Public agencies should be aware that independent contractors, including consultants, cannot "change hats" to obscure their participation in public contracting. In reviewing any transaction between an independent contractor and a public agency for a conflict, the focus should be on the substance, not the form, of the transaction. Transactions in which a public agency hires a consultant to perform work about which the consultant previously advised the public agency as well as those in which a public agency hires a former employee as a consultant when both roles include similar work are particularly prone to conflicts of interest and should be carefully evaluated for legality prior to any engagement.

If you have any questions about this decision or conflict of interest law in general, please contact the authors of this Client News Brief or an attorney at one of our nine offices located statewide. You can also visit our website, follow us on Facebook or Twitter or download our Client News Brief App.