

ADVISORY OPINION 94 - 67

December 15, 1994

- RE:
- 1) Must a public servant divest himself of his interest in a company which holds a state contract?
 - 2) May the public servant sell the stock of the company to a current employee, with the sale proceeds to be distributed over several years?
 - 3) May the public servant continue to be listed as a guarantor for the company on bank loan documents?
 - 4) Does the fact that the public servant's spouse is a member of a county board of education present any ethics considerations?
- DECISION:
- 1) Yes, except that a public servant may own up to five percent of any business which does business with the Commonwealth of Kentucky.
 - 2) Yes, provided the sale amount is fixed at the time of sale and is not dependent upon any event occurring after the transaction closing.
 - 3) No.
 - 4) No.

This opinion is in response to your November 29, 1994, request for an advisory opinion from the Executive Branch Ethics Commission (the "Commission"). This matter was reviewed at the December 15, 1994, meeting of the Commission, and the following opinion is issued.

You state the relevant facts as follows. You are considering candidacy for a state constitutional office and have questions concerning any possible conflict of interest with your present business, if you are elected. You are president of, and hold all shares outstanding in, a company which contracts with the state to audit, transport, and distribute food stamps in four counties. This bid contract, though issued by the Commonwealth, is under the auspices of the U. S. Department of Agriculture, Food and Nutrition Services. You wonder if the last sentence in KRS 11A.040(4) affects whether you must divest any interest in the company.

KRS 11A.040(4) states:

(4) No public servant shall knowingly himself or through any business in which he owns or controls an interest of more than five percent (5%), or by any other person for his use or benefit or on his account, undertake, execute, hold, or enjoy, in whole or in part, any contract, agreement, lease, sale, or purchase made, entered into, awarded, or granted by any state agency. This provision shall not apply to a contract, purchase, or good faith negotiation made pursuant to KRS Chapter 416 relating to eminent domain or to agreements which may directly or indirectly involve public funds disbursed through entitlement programs.

If you are elected to constitutional office and become a public servant, you must not have more than a five percent (5%) interest in any business which does business with the Commonwealth of Kentucky. Although you state the company's contract is under the auspices of the federal government, it is issued by the Commonwealth of Kentucky. The company and the Commonwealth are in a contractual relationship. The fact that the subject matter of the contract is funded through entitlement programs is irrelevant since the company is not receiving its contractual consideration due to any entitlement rights.

You may sell the stock of your company to a current employee, with the sale proceeds being disbursed over several years, provided the amount is set at the transfer of the ownership interest. If the amount were to remain flexible, or dependent in some way on future events such as accounts receivable or the profit margin on a

certain future date, you would have a conflict of interest.

You also ask whether a conflict of interest would exist if you sell your company to one of its current employees, yet remain as a personal guarantor on the company's loan documents with the bank. You state, "(b)ecause the company is reimbursed by the Commonwealth for operation of expenses in arrears, a line of credit to the company, secured by my personal guarantee is required. . . .(The prospective purchase/employee does not have the financial strength to maintain this line of credit)."

If you are listed as a personal guarantor on the company's bank loans, the risk of the company's nonpayment rests with you. What will happen if the company, which admittedly does not possess the same financial strength as you personally, defaults on the bank loans? You would then have to make the company's loan payments, and it is likely that your contract with the company ensures that you regain your interest in the company if this situation occurs. At that point, you would possess an interest in the company which exceeds the five percent maximum. Even if, for some reason, you would not regain your interest in the company in the case of default, you would have a vested interest in the company's success which poses a conflict of interest for you. Thus, you should not continue as a loan guarantor if the company is sold.

Finally, your spouse is a member of the local county school board and you wish to know if this poses any conflict of interest concerns for you. Currently, the Commission does not believe this relationship would present a conflict if you are elected. The school board, which does receive some funds from the state, is not a business which is owned or controlled by you or your spouse. However, a conflict would exist if the school board has a business or regulatory relationship with the state agency to which you are elected.