

DATE: October 26, 1988

TO: Abbe Wolfsheimer, Councilmember, District 1
FROM: City Attorney
SUBJECT: Expenditure of Public Funds by Economic
Development Corporation to Promote Ballot
Initiatives

This is in response to your memorandum of September 8, 1988 to John Witt, City Attorney, containing several questions regarding a report published by the San Diego Economic Development Corporation in August 1988 regarding the "Quality of Life" Initiative, which has been designated Proposition "J" by the County Registrar on the November 8, 1988 ballot. You attach a copy of a newspaper article about the report, but no other documents.

You ask this office to investigate the matter and render a formal opinion on the following issues:

1. Can a City-funded agency legally take political positions and/or lobby in favor of ballot propositions under municipal or state election law?
2. Can the EDC do so by law or by its charter or must it limit its activities to economic development?
3. If the EDC is permitted to engage in political activities, may it do so on taxpayers' time and at taxpayers' expense?
4. If EDC is not permitted to do so, what remedies or sanctions are available to the City Council, i.e. a budget cut, or recovery of any unauthorized funds expended?

BACKGROUND FACTS

The facts were determined from a review of the documents identified below:

1. Articles of Incorporation of Economic Development Corporation, San Diego County, as amended May 12, 1966.
2. Bylaws of Economic Development Corporation, San Diego County, as amended May 15, 1984.
3. Agreement between The City of San Diego and San Diego Economic Development Corporation, filed in the office of the City Clerk as Document RR-271508 on July 25, 1988, and City Council Resolution R-271508 authorizing execution of this agreement.

4. San Diego Economic Development Corporation 1987 Annual Report.
5. San Diego Economic Corporation Budget Fiscal Year 1987.
6. Independent Auditor's Report dated July 28, 1988, prepared by Deloitte, Haskins & Sells and Financial Statements for the Years Ended June 30, 1988 and 1987 regarding Economic Development Corporation/San Diego County.
7. Excerpt from 1986-1987 Economic Development Corporation Chairman's Speech at 1987 Annual Meeting.
8. Agendas and Excerpts from Minutes of Economic Development Corporation Board of Directors' Meeting relating to the "growth issue."
9. Report entitled "Impact of Quality of Life Initiative on the City of San Diego's Economy" prepared by San Diego Economic Development Corporation, August 1988.

The San Diego Economic Development Corporation (EDC) is a nonprofit corporation organized under the General Nonprofit Corporation Law of the State of California (codified at

Corporations Code section 5000 et seq.). The primary purpose of EDC is:

to further the economic development of the greater San Diego, California area and to promote and assist the development of business, including small business concerns in said area. The primary objective of this corporation shall be benefit to the community as measured by increased employment, payroll, business volume and corresponding factors. (Article II(a) of EDC's Articles of Incorporation, as amended May 12, 1966, attached as Exhibit A)

EDC is funded by The City of San Diego ("City"), County of San Diego, private contributions and other miscellaneous revenue sources. (EDC Budget for FY 1989, attached as Exhibit B). For fiscal year 1989, City contributes \$435,000 of EDC's \$960,000 budget.

EDC and City for several years have entered into an agreement annually to memorialize their expectations of the activities of EDC. The most recent agreement between City and EDC was executed in July 1988 (City Clerk Document No. RR-271508, as authorized by Council Resolution No. R-271508, dated July 25, 1988; Agreement attached as Exhibit C). Prior agreements between City and EDC contained substantially the same language.

Paragraph I(a) through I(f) (page 2) of the City/EDC agreement sets forth the specific activities which EDC is authorized to conduct under the agreement. This paragraph specifically states that the listed activities are not to be exclusive. The activities which City prohibits EDC from conducting are set forth in the "General Terms and Conditions" portion of the City/EDC agreement (paragraph 11, page 5), which is incorporated by reference at paragraph VII, page 6 of the specific terms of the agreement. In relevant part, paragraph 11 reads as follows:

Organization EDC agrees to the following prohibitions:

- a. Organization EDC shall not use directly or indirectly any of the funds received from City under this Agreement for the following purposes:
 - 1) ...
 - 2) ...
 - 3) for any political ... activities whatever.

Also relevant to this inquiry are provisions of the City/EDC agreement pertaining to management of EDC's finances. Article II, paragraph 1, of the agreement reads: "Said City funds may be commingled with other funds to be received by EDC for its operations."

The article continues:

City funds may be used for staffing, advertising/publicity, general operations, promotional activities including travel and meetings, research activities and other reasonable and appropriate costs related to the program activities and purpose."

In contrast to the above-cited language permitting "commingling" of City funds and funds from other sources, paragraph 2 of the General Terms and Conditions portion of the Agreement states: "A separate accounting of the expenditure of funds received from the City shall be maintained in the accounting records and financial reports."

According to Daniel Pegg, President of EDC, and Paul Devermann, Vice President of EDC, in a meeting held in City Attorney offices on September 15, 1988, the City has never required a separate accounting of City funds under the terms of paragraph 2 of the General Terms and Conditions. Rather, the City has consistently permitted commingling of funds as stated in the Specific Terms cited above. This information was confirmed by the City's contract administrator for the agreement, Stephan A. West, Deputy Director for Economic Development of the City's Property Department.

It should also be noted that under the terms of the

Agreement, the City appoints two representatives to serve on the EDC Board (General Terms and Conditions, paragraph 13, page 6). The two current City representatives are Yasuo Sasaki, Vice President of Sanyo Industries of America, and Herbert G. Klein, Editor in Chief of Copley Newspapers.

At the September 15th meeting, Messieurs Pegg and Devermann confirmed that EDC issued a report on the "Quality of Life" Initiative Measure in August 1988. A copy of this report is attached as Exhibit D. This is the third report published by EDC on growth issues since publication of the SANDAG Report on Growth No. R-83 dated September 11, 1987. The first EDC report on growth was issued in September 1987; the second in April 1988; the third (the one in question) in August 1988. EDC's Board of

Directors authorized each of these reports. It is EDC's position that each of these reports treats the growth issue only as it affects economic development. The August 1988 report does not treat either the City Council approved ballot measure (Proposition H) nor the County growth measures on the upcoming ballot because, in EDC's view, these measures will not affect the economic development of the community. The August 1988 report has been disseminated to approximately 10 or 12 persons or entities, including this office and the media. Messieurs Pegg and Devermann also pointed out that in prior years, EDC has taken positions on the proposed unitary tax, border-related issues, and growth issues to the extent they affect economic development.

LEGAL ANALYSIS

General Rule Regarding Use of Public Funds For Political Purposes

The legal question underlying the four questions posed is to what extent public funds may be used for political purposes. The general rule in California is that public funds may not be used to promote the passage of a ballot measure in the absence of clear and explicit legislative authority. *Stanson v. Mott*, 17 Cal.3d 206 (1976). In that case, a taxpayer challenged the authorization by the Director of the State Department of Parks and Recreation of \$5,000 in public funds to promote the passage of a bond for future acquisition of park land and facilities. The California Supreme Court found that the director had no clear statutory authority to spend public monies for election campaign purposes, although there was statutory authority to spend public money for informational purposes, that is, to provide the public with a fair presentation of facts pertaining to the bond issue. In the *Stanson* case, the Court found that if the questioned agency publication were not merely informative but promotional in nature, then the expenditure of public funds for dissemination

would have been improper. 17 Cal.3d at 222-23.

Constitutional Questions

The Stanson case was decided purely on statutory grounds. The constitutional issue was discussed briefly but not decided by the Stanson court. 17 Cal.3d 206 at 217. Research reveals no California case that decides on constitutional grounds the issues presented by the instant situation. However, there have been cases in other jurisdictions that have done so. The results are inconclusive. See, for example, Mountain States Legal Foundation

v. Denver School District, 459 F. Supp. 357 (D. Colo. 1978), which prohibited on constitutional grounds a school district from authorizing the expenditure of public funds to defeat a proposed constitutional amendment; and, Alabama Libertarian Party v. City of Birmingham, F. Supp. , 1988 W.L. 92111 (N.D. Ala. September 6, 1988), which upheld on constitutional grounds a city's use of public funds to pay for advertisements in newspaper and radio and to distribute leaflets and brochures for two ballot measures. These cases demonstrate that the law is unsettled in this area, especially as it relates to the constitutional questions.

Nevertheless, the law is clear in California that unless there is explicit statutory language authorizing it, expenditure of public funds for campaign electioneering is prohibited.

Lobbying vs. Campaigning

The first question presented specifically asks whether a partially city funded agency can "lobby" in favor of a ballot proposition. As pointed out in the cases, "lobbying" is a separate and distinct concept from "campaigning."

The Stanson court carefully distinguishes between the terms election "campaigning" and legislative "lobbying" as follows:

California statutes draw a clear distinction between the two matters; while various provisions authorize public expenditures for appropriate legislative lobbying activities... no similar provision sanctions the use of public funds in election campaigns.

More fundamentally, while public agency "lobbying" efforts undeniably involve the use of public funds to promote causes which some members of the public may not support, one of the primary functions of elected and appointed executive officials is, of course, to devise legislative proposals to attempt to implement the current administration's policies. Since the legislative process contemplates that interested parties will attend legislative hearings to explain the potential benefits or detriments of proposed

legislation, public agency lobbying, within the limits authorized by statute ... in no way undermines or distorts the legislative process. By contrast, the use of the public treasury to mount an election cam-paign which attempts to influence the resolution of

issues which our Constitution leave to the "free election" of the people ... does present a serious threat to the integrity of the electoral process.

Stanson v. Mott, 17 Cal.3d at 218.

A California Court of Appeal case from the Third District, Miller v. Miller, 87 Cal.App.3d 762 (1978), clarifies the distinction between lobbying and campaigning made in Stanson. Citing the above-quoted language, the court in Miller stated that the real issue in Stanson was "not the objective of the promotional activity but the audience to which it was directed." 87 Cal. App.3d at 768. In Miller, plaintiffs had challenged the promotion by the California Commission on the Status of Women of ERA ratification by legislatures of other states on the grounds that this activity was "election campaigning" as opposed to "legislative lobbying" and therefore improper. The court concluded that the activities of the commission were in the realm of "election campaigning" and therefore a prohibited public expenditure, absent clear legislative authority. The Miller court then found no clear statutory authority for the commission to marshal public support for the passage of the ERA.

In its discussion, the Miller court especially notes that local governmental agencies are expressly authorized by Government Code section 50023 to engage in legislative lobbying, however, they found no such statutory authority for "election campaigning." Therefore, in California at least, the courts find that local governmental agencies may expend public funds to engage in legislative lobbying, but not election campaigning.

Use of Public Funds by Private

Nonprofit Corporation

Although both the Stanson and Miller courts dealt with public agencies, the principles enunciated in these cases appear to apply to private entities partially funded by a governmental entity such as the City, at least to the extent public monies are involved. Careful examination of these two cases reveals that they discuss the propriety of expenditure of public funds. The question is not whether a public agency does the spending, only whether public, as opposed to private, funds are spent. Although there is no case treating the issue, the plain meaning of the terms in Stanson and Miller must control. Therefore, partially

public funded nonprofit agencies should have to abide by the same rule as public entities with respect to expenditures of public monies for political purposes.

Legality of Lobbying and Taking Political Positions by City Funded Agency

Next, we apply the above rules to the first question. That question asks whether a City-funded agency (presumably EDC) can legally take political positions and/or lobby in favor of ballot propositions under municipal or state election law. To answer the question, it is assumed that public funds are used to "take" the position or engage in lobbying. Absent any "separate accounting," it must be assumed that some public monies were used in the preparation of the report. The question does not arise if only private monies are used.

Essentially, state and local election laws do not answer the question, but the principles in Stanson and Miller do. First, there is nothing in the law to prohibit a partially public-funded private entity from merely taking or stating its positions on any political issue or candidate. These types of entities, as well as individuals, businesses, and government officials, in their individual as well as official capacities, have first amendment rights to declare their position on candidates and issues. Second, absent a local law or agreement prohibiting the conduct, under Stanson and Miller a partially city-funded private entity such as EDC may engage in "legislative lobbying," even if it uses public funds to do so. This does not answer the underlying question of whether the EDC report of August 1988 constitutes a "lobbying" effort, or is in the realm of "election campaigning." That issue is treated under the discussion of question number three (3), below.

Authority from Corporations Code or Articles of Incorporation

The next question presented is whether EDC has authority by law or by its "charter" to take political positions or engage in lobbying, or, on the contrary, must it limit its activities to economic development. This question assumes that the term "economic development" excludes lobbying or taking political positions.

First, there is no law authorizing the creation of EDC except general state law governing the formation of nonprofit corporations. This law allows formations of corporations for any public or charitable purpose. Corporations Code section 5111. Assuming there is no tax question involved (and there is none raised here), there is nothing in the Corporations Code to prevent this type of corporation from lobbying or taking

political positions on an issue.

Therefore, it is necessary to determine whether EDC's Articles of Incorporation (the equivalent of a charter) authorize it to lobby or take political positions on an issue. The purposes for which EDC was formed as set forth in its articles are stated in full in the background facts above. The purposes are very broad, and include among other things: "to engage in all lawful activities ... usually and normally engaged in by a corporation of this nature." (Article II(b)).

The purposes also include:

to possess and exercise all of the powers conferred by law upon nonprofit corporations and to have all other powers and to do all other acts necessary or incidental to the administration of the affairs and for carrying out the purposes of this corporation..." (Article II(c)).

The primary objective of the corporation is to benefit: "the community as measured by increased employment, payroll, business volume and corresponding factors." (Article II(a)).

The above-cited language is an extremely broad grant of power to the corporation by its articles. By no stretch of the imagination can this be interpreted to preclude lobbying or taking political positions on issues that may affect "employment, payroll, business volume and corresponding factors."

Therefore, in response to the second question, neither the corporation code under which EDC was organized nor its own articles of incorporation prohibit EDC from lobbying or taking a political stand on an issue related to its purposes.

Was the EDC Report Purely Informational,
as Opposed to Promotional?

The third question raised asks whether EDC may use taxpayer monies to pay for political activities. The question does not specify what type of political activity is involved. As discussed above, "political activity" may range from merely stating a position on an issue to lobbying a legislative body to engaging in election campaigning on a ballot measure.

Two factors potentially limit EDC's ability to engage in some political activities if it is using City money to do so: the above-discussed doctrine on the expenditure of public funds for election campaigning and the agreement between the City and EDC.

The principles involved in determining whether an expenditure of public funds for political purposes is proper or not was discussed at length above. Essentially, under those principles, EDC may not properly use the City's (or, for that matter, other

public entity's) funds for either promoting or opposing the "Quality of Life" measure. Whether the August 1988 report constitutes a purely informational, as opposed to promotional, report is a factual question and can be decided only after consideration of several factors outlined by the court in *Stanson v. Mott*, supra.

The Court, by way of dictum in *Stanson v. Mott*, supra, 17 Cal.3d 206, indicated what types of activities it considered improper campaign expenditures, as opposed to proper informational activities:

The use of public funds to purchase such items as bumper stickers, posters, advertising "floats" or television and radio "spots" unquestionably constitutes improper campaign activity citation as does the dissemination, at public expense, of campaign literature prepared by private proponents or opponents of a ballot measure citations. On the other hand, it is generally accepted that a public agency pursues a proper "informational" role when it simply gives a "fair presentation of the facts" in response to a citizen's request for information citation, or, when requested by a public or private organization, it authorizes an agency employee to present the department's view of a ballot proposal at a meeting of such organization citations. 17 Cal. 3d at 221.

The *Stanson* court further noted prior cases involving close questions of informational as opposed to promotional brochures. In so noting, the court stated:

public agencies may generally publish a "fair presentation of the facts" relevant to an election matter, ... but publicly financed brochures or newspaper advertisements which have purported to contain any relevant information, and which have refrained from exhorting voters to "Vote Yes" have, nevertheless, been found to constitute improper campaign literature citation ... The determination of the

propriety or impropriety of the expenditure depends on a careful consideration of such factors as the style, tenor and timing of the publication, no hard and fast rule governs each case." 17 Cal.3d at 222.

The question is whether the August 1988 report issued by the

EDC on the Quality of Life Initiative is purely informational or rather promotional in nature in light of the above factors in Stanson.

The EDC report in question is attached hereto as Exhibit D. On the surface it appears to be a "purely informational" report about the projected effects on San Diego's economy and employment if the "Quality of Life" (Proposition J) initiative measure passes in November. The EDC report does not contain any clear exhortation to "Vote Yes" or "Vote No" on Proposition J or on any other measure on the November ballot. However, it does spell out in fairly strong language what EDC considers will be the consequences if Proposition J passes. For example, at page 1, paragraph 6, of the Executive Summary, the report reads: "This referring to the projected effect of Proposition J to increase unemployment rate and reduce population growth is an unacceptable tradeoff. EDC concurs with San Diego Association of Governments (SANDAG) that this level of economic disruption will likely be so damaging that the local economy may never recover."

Page 2, paragraph 4 of the Executive Summary reads: "The Quality of Life Initiative does not meet these effective growth management criteria and in fact causes more harm than good because it ignores sound economic planning."

In its conclusion, page 10, paragraph 6, the EDC report states: "In addition to causing unemployment, the QLI will also reduce City revenues. The city and its residents will be confronted with the need to eliminate essential, and currently over-taxed, public services as a result of the lost revenues."

Although not specifically exhortations to "Vote No" on Proposition J, these excerpts leave no question in the reader's mind about what position EDC wants the reader to take on Proposition J. To that extent, the report is in the nature of "campaign electioneering." But the bulk of the report clearly is informational and, although the accuracy of the statistics and information cannot be judged in this document, it purports to provide relevant facts about Proposition J and its consequences if adopted in November.

Although a close question, it appears under the Stanson criteria that the EDC report is in the nature of a prohibited campaign electioneering document, because it is not purely informational. The standard in Stanson is strict. A document must be purely informational, or it will not pass legal muster. Since the EDC report contains no statement about the projected advantages of the measure if adopted, nor does it contain any statement about the competing measure (Proposition H), the report is easily attacked as not containing a fair presentation of the

facts. To pass the Stanson test, at a minimum the report would need to contain some balanced view of the pros and cons of the measure and its competing measure.

There is no serious question here about to whom the EDC report is directed. Although the report has received limited distribution to date, the intended audience is clearly the voter, not the legislative assembly, since the measure is on the ballot, not a bill before the legislature. Therefore, preparation and publication of the EDC report was a violation of the Stanson principles, if public monies were used, and unless EDC has clear statutory authority for campaign electioneering. We are quick to stress, however, that this conclusion is based on the assumption that public monies were used since there has been no "separate accounting."

Perusal of the Corporations Code reveals no clear authority for EDC to use public funds for publication of "electioneering" reports. There is nothing in the City's Charter or Municipal Code which would authorize EDC to do so. Therefore, if EDC used public monies to issue its report, to do so was in violation of Stanson principles.

Agreement Between City and EDC

In the agreement between EDC and City, EDC is specifically charged with expanding "the region's industrial base through the development of primary sector employment opportunities which will result in general economic growth, economic diversification, and capital formation."

The agreement specifically authorizes EDC to conduct the following activities:

- a. Concerted promotional and marketing efforts such as nationwide advertising, direct mailings, personal contracts, executive tours of San Diego, etc. to attract business and industry to San Diego.
- b. Encouragement and assistance to local businesses/industries to relocate and expand within the region.
- c. Development and dissemination of data and responses to inquiries pertaining to industrial operations and opportunities in San Diego.
- d. Liaison and coordination between prospective private sector employers and public agencies, the City in particular, as appropriate.
- e. Promotion to prospective employers of the services of PIC/RETC in providing job training and referral of low-income and unemployed persons. A written plan for implementing this provision shall be

prepared by EDC and approved by the City.

- f. Active promotion of a positive business environment within the San Diego region.

Although broad, these activities do not clearly contemplate EDC issuing reports on the impact of ballot measures. Additionally, the agreement specifically prohibits EDC from using City monies to engage in any political activity whatever (see above-cited facts). The agreement, however, nowhere defines the term "political activity." For purposes of this analysis, it seems appropriate to at least include in the definition the terms "lobbying" and "campaign electioneering" as defined in the Stanson case, *supra*.

The issue would then be whether the August 1988 EDC report constitutes "political activity" prohibited by the agreement? Having just concluded that the EDC report would likely be found to be a "campaign electioneering" type of report under Stanson, it is unnecessary to iterate that same analysis here. On balance, preparation and dissemination of the EDC report appears to be in the nature of political activity, in violation of the strict terms of the agreement with the City, if it was prepared and distributed with City funds.

However, the strict terms of the agreement may have been altered by the conduct of the parties over the years. Apparently EDC has published several reports over the years on campaign issues similar to their August 1988 report, according to Messieurs Pegg and Devermann. These reports were issued with the

knowledge of the City and despite the language in prior agreements prohibiting EDC from using City funds for "political activity." Assuming these facts are true, then the express terms of the agreement may well be modified by the conduct of the parties to exclude this type of EDC report from the term "political activity"; and, therefore, the City would be estopped from asserting that publication of this report was a violation of the agreement.

Remedies of City

The fourth question presented asks what remedies City has if EDC wrongfully expended City funds to publish the August 1988 report.

The remedies of the City are set forth in relevant part in paragraph 14 of the "General Terms and Conditions" of the City/EDC agreement, as follows: "The City may withhold funds from the contracting Organization EDC and terminate its entire obligation upon notice to the Organization EDC if the Organization EDC violates any of the terms of the agreement, or for other good cause shown not related to a violation of the

terms of the agreement."

Because of the ambiguity of the term "political activity" in the agreement arising from the past conduct of the parties over issuance of prior EDC reports, there is no clear violation of this agreement by EDC in publishing the August 1988 report. Therefore, termination of the agreement does not appear justified. Additionally, since the City allows EDC to commingle its City funds with other monies, both public and private, it would be difficult if not impossible to determine what, if any, public monies were spent on this report. Hence, it would be difficult to assess how much money, if any, to withhold from the organization.

Lastly, although the Council could find that EDC's issuance of the report was a potential misuse of public funds and therefore "good cause" to terminate the agreement under paragraph 14, the fact that City has allowed EDC to commingle private and public funds both by express language and by conduct over the years, it would be difficult to assess what amount of money, if any, could be withheld from EDC's payments.

In its future agreements, Council may wish to require strict accounting of public fund expenditures so that it may avail itself of the "withholding of funds" remedy in the event of a breach.

Conclusion

California case law prohibits the use of public funds for political purposes unless clearly and explicitly authorized by statute. The rule applies to both public agencies and partially publicly funded nonprofit corporations to the extent those corporations use public monies for their activities.

There is explicit statutory authority for public agencies to engage in "lobbying" a legislative body, but not for "campaign electioneering" on ballot measures. Under California corporation law and its Articles of Incorporation, EDC, a partially publicly funded nonprofit corporation, may engage in lobbying or campaign electioneering as long as it does not use public funds to do so.

The EDC report of August 1988 on the "Quality of Life" Initiative measure (Proposition J) appears to be in the nature of a "promotional" document, and is not "purely informational." Therefore, it would violate the principles enumerated in *Stanson v. Mott*, 17 Cal.3d 206 (1976), prohibiting use of public funds for political purposes unless there is a "separate accounting" showing no public funds expended on the report. Publication of the EDC report has the potential to be in violation of the agreement between EDC and City. However, based on the parties' prior conduct interpreting their agreement and because the August

1988 EDC report is not clearly a political document, it is not recommended that the Council either terminate the agreement with EDC or withhold monies from EDC, which are the two contractual remedies provided.

JOHN W. WITT, City Attorney

By

Cristie C. McGuire

Deputy City Attorney

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Attachments

cc Stephan A. West,

Property Department

Daniel Pegg, EDC

Paul Devermann, EDC

ML-88-93