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Timothy N. Schott
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From: Pamela D. Griebel 
Assistant Attorney General

Date: October 10, 2008

Re: City of Fort Dodge – conflict of interest issues

You have each requested informal advice regarding conflict of interest issues surrounding the procurement of engineering services by the City of Fort Dodge. Your request was initially directed to Christie J. Scase in her capacity as the assistant attorney general assigned to represent the Auditor of State. Ms. Scase has now left our office, but her research and analysis is reflected in this memorandum.

County Attorney Schott's inquiries relate to potential conflicts arising from the fact that the city's mayor, Terry Lutz, is an officer and shareholder of McClure Engineering Co. of Fort Dodge. The Auditor of State's office echoes the questions presented by the county attorney regarding the ability of the city to contract with McClure Engineering Co. while Mr. Lutz serves as a city officer. In addition, the Auditor's office asks us to address the potential conflict of interest and competitive bidding issues arising from the fact that a second engineering firm, MER Engineering, Inc., continued to contract to provide engineering services during an extended period of time while Eldon Rossow, a director and officer of that firm, was serving as interim city engineer under contract with the city.

Conflict principles governing city officers and employees:

Iowa Code section 362.5 establishes a broad general prohibition upon city officers and employees contracting with the city. "A city officer or employee shall

not have an interest, direct or indirect, in any contract or job of work or material or the profits thereof or services to be furnished or performed for the officer's or employee's city." Iowa Code § 362.5 (2007). The prohibition is, however, subject to a number of exceptions, including the following:

The provisions of this section do not apply to:

* * *

4. Contracts made by a city, upon competitive bid in writing, publicly invited and opened.

5. Contracts in which a city officer or employee has an interest solely by reason of employment, or a stock interest of the kind described in subsection 9, or both, if the contracts are made by competitive bid in writing, publicly invited and opened, or if the remuneration of employment will not be directly affected as a result of the contract and the duties of employment do not directly involve the procurement or preparation of any part of the contract. The competitive bid qualification of this subsection does not apply to a contract for professional services not customarily awarded by competitive bid.

* * *

7. A contract in which a city officer or employee has an interest if the contract was made before the time the officer or employee was elected or appointed, but the contract may not be renewed.

* * *

9. A contract with a corporation in which a city officer or employee has an interest by reason of stockholdings when less than five percent of the outstanding stock of the corporation is owned or controlled directly or indirectly by the officer or employee or the spouse or immediate family of such officer or employee.

Iowa Code § 362.5(4), (5), (7), (9). "The exceptions listed in section 362.5 are the only lawful means by which a city officer or employee may do business with that city." 1994 Iowa Op. Att'yGen. 11 (#93-4-8(L)) [1993 WL 137167]. In the absence of an applicable exception, "the general prohibition in section 362.5 against city officers or employees having a direct or indirect interest in contracts with a city applies even if they abstain from awarding the contracts." 1994 Iowa Op. Att'yGen. 119 (#94-7-4) [1994 WL 470450].

"Statutory conflict-of-interest provisions reveal legislative intent to engender public confidence in the operation of government. The principle underlying this policy is that a government employee or official cannot serve two masters at the same

time, and the public interest should not be entrusted to an official with interests in conflict with the public interest.” T & K Roofing Co., Inc. v. Iowa Dept. of Education, 593 N.W.2d 159, 163 (Iowa 1999) (citations omitted). As this office has previously observed, the following well-settled principles arise from Iowa case law to guide the conflict of interest analysis: “that the applicable laws have a practical focus, that they demand complete loyalty to the public, that they encompass situations in which the mere possibility of conflict exists, and that they seek to promote confidence in the integrity and impartiality of public officers.” Id., citing Bluffs Development Corp. v. Bd. of Adjustment, 499 N.W.2d 12, 15 (Iowa 1993); Borlin v. City of Council Bluffs, 338 N.W.2d 146, 150 (Iowa 1983); Wilson v. Iowa City, 165 N.W.2d 813, 822-23 (Iowa 1969); Bay v. Davidson, 133 Iowa 688, 111 N.W. 25, 26 (1907); also 10A McQuillan, *Law of Municipal Corporations* § 341, at 916-17 (1990); 63A Am.Jur.2d *Public Officers and Employees* § 322, at 989-99 (1984).

To serve these purposes, statutes governing conflicts must be strictly interpreted and applied to protect the public interest and the integrity of government function. As our highest court explained in a leading modern era case addressing the subject:

We doubt if any rule of law has more longevity than that which condemns conflict between the public and private interests of government officials and employees nor any which has been more consistently and rigidly applied. The high standards which the public requires of its servants were set by common law and adopted later by statute. It is almost universally held that such statutes are merely declaratory of the common law. These rules, whether common law or statutory, are based on moral principles and public policy. The demand complete loyalty to the public and seek to avoid subjecting a public servant to the difficult, and often insoluble, task of deciding between public duty and private advantage.

Wilson v. Iowa City, 165 N.W.2d at 822. With these principles in mind, we turn to the specific facts underlying your inquiries.

Potential conflicts arising from contracts with McClure Engineering Co.:

We have the following understanding of the facts with regard the mayor, based upon the background information provided. Mayor Lutz was elected in 2005. He is an officer and the largest shareholder (49%) of McClure Engineering. For many years, McClure Engineering has performed engineering work for the City of Fort Dodge and the company regularly bids on engineering contracts with the city. The

mayor receives financial benefit from contracts with the city in the form of division of the company profits.

Shortly after he took office, Mayor Lutz requested and received advice from the city attorney regarding whether his service as mayor would create a conflict of interest which would interfere with or void contracts between the city and McClure Engineering. The mayor was advised that contracts which were in place prior to the mayor taking office were permitted to be completed. The city attorney concluded that future contracts between the city and McClure Engineering would present an impermissible conflict under Iowa Code 362.5, unless they fit within one of the enumerated exceptions to the general conflict rule. After examining the exceptions, he advised that McClure could be awarded engineering services contracts during Mayor Lutz's term pursuant to Code subsection 362.5(4), if the contracts were made "upon competitive bid in writing, publicly invited and opened" and the mayor took no part in the process on behalf of either the city or McClure. Given that professional services, including engineering services are generally not subject to traditional competitive bidding, the city attorney opined that a competitive qualification process would qualify for the exception

Against this background, County Attorney Schott has requested advice addressing Iowa Code sections 362.5(4), 362.5(5), and 26.4. Specifically, he asks:

1. Does the mayor's situation as the largest shareholder of his company disqualify him from the excepting language in paragraph (5) ". . . in which a city officer or employee has an interest solely by reason of employment."
2. Would the profit sharing arrangement of the mayor's company constitute "remuneration of employment," thus disqualifying him from the exception in the second half of paragraph (5)?
3. Do the competitive bid exceptions of either paragraph (4) or (5) allow for a competitive bid professional services contract based upon qualitative criteria, rather than the requirements of Chapter 26?
4. Recently enacted Iowa Code Section 26.4 exempts architectural and engineering design services from the competitive bidding requirements of Iowa Code Chapter 26. Does this exemption in any way change the conflict analysis under 362.5?

The Auditor of State's office asks also asks whether "a request for qualifications (RFQ) meets the intent and requirements of competitive bidding." The RFQ process is described in the Auditor's office request as a request for submission, and comparison of, qualitative information from a potential engineering firm. Pricing information is not requested or considered during the vendor selection process. Instead, compensation is determined by the successful firm negotiating a contract with the city with a not-to-exceed total price for professional services.

County Attorney Schott's first two questions relate to the applicability of the exception in subsection 362.5(5). He asks whether the mayor's stock ownership or receipt of profits from contracts with the city disqualify him from the exception. These facts disqualify the mayor from taking advantage of the exception set forth in this subsection. Subsection 5(5) allows contracts in which a city officer or employee has an interest *only if* the affected city officer or employee's interest arises "solely by reason of employment, or a stock interest of a kind described in subsection 9 [i.e. stockholding of less than five percent of outstanding stock], or both." Under the facts presented here, Mayor Lutz is far from being a mere employee and/or minor stockholder of McClure Engineering. He is the corporation's largest stockholder (owning 49% of outstanding shares), he receives a share of the profits deriving from contracts with the city, and he is identified as the president of the corporation on its most recent biennial report which was filed with the Iowa Secretary of State in April of this year. We agree with the City Attorney's characterization of subsection (5) as applying when a city officer or employee's interest in a contract is indirect and de minimus. Given the role Mayor Lutz has with the corporation, this subsection does not apply to contracts between the city and McClure Engineering.

The county attorney's third question and the question posed by the Auditor of State's office both seek guidance regarding whether solicitation of qualitative information from potential vendors and the selection of a vendor based upon responses to the RFQ constitutes competitive bidding in the context of the exceptions set forth in section 362.5. The conflict of interest exceptions in subsections 362.5(4) and (5) each refer to contracts made "upon competitive bid in writing, publically invited and opened." We do not believe that the qualitative selection process which is described constitutes a competitive bid procedure for purposes of section 362.5.

Although chapter 362 does not define what is meant by "competitive bid," the concept of competitive bidding as a method for awarding public contracts is not new or unique and the term has a well-established definition in the context of government contracting. When terms are not defined by statute, "we look to prior decisions of [the courts], similar statutes, dictionary definitions, and common usage." Iowa Association of School Bds. v. Iowa Dept. of Education, 739 N.W.2d 303, 309 (Iowa

2007), quoting Gardin v. Long Beach Mortgage Co., 661 N.W.2d 193, 197 (Iowa 2003). “In addition, ‘we consider the context of the provision[s] at issue and interpret the provision[s] consistent with the entire statute of which [they are] a part.’” Id., quoting State v. Kamber, 737 N.W.2d 297, 299 (Iowa 2007). Black’s Law Dictionary defines “bid” as “[a] buyer’s offer to pay a specified price for something that may or may not be for sale.” *Black’s Law Dictionary* 153 (7th ed. 1999). “Competitive bid” is defined as “a bid submitted in response to public notice of an intended sale or purchase.” Id. at 154.

The purpose and benefits of competitive bidding have frequently been addressed by our court. The requirements protect the public by securing “competition among bidders, the best results at the lowest price, and . . . forestall fraud, favoritism and corruption in the making of contracts.” Eleview Construction Co., Inc. v. North Scott Community Sch. Dist., 373 N.W.2d 138, 142 (Iowa 1985), quoting Istari Construction, Inc. v. City of Muscatine, 330 N.W.2d 798, 800 (Iowa 1983). “The paramount purpose of the competitive bidding statute is to protect the public as taxpayers . . .” Master Builders of Iowa, Inc. v. Polk County, 653 N.W.2d 382, 394 (Iowa 2002). The process is designed to “provide a [city] with the *best* results at the lowest possible price.” Id. at 395 (emphasis original). As described by the court and detailed in chapter 26, the competitive bidding process does not preclude the consideration of the qualifications of bidders within the bid review, but once qualified bidders are identified the contract award must be based on price. Iowa Code chapter 26 sets forth the current competitive bidding requirements for public construction projects. This statute requires a contract let under competitive bidding to be awarded to the “lowest responsive, responsible bidder.” Iowa Code §§ 26.9, 26.10 (2007).

Sound logic supports limiting the exceptions to the conflict of interest rule to contracts which follow this form of competitive bidding. The exceptions set forth in section 362.5 are designed to allow contracts to proceed, despite a potential conflict of interest, when the timing of the contract or process used to select the vendor provides assurance that the potential conflict will not impact selection of the vendor or when the potential benefit to the public official or employee is minimal. If an objective, price-based competitive bidding process is utilized, the danger of a city employee or officer with a conflicting interest having undue influence over the award process is virtually eliminated. The same is not true if contracts are awarded solely upon subjective qualification criteria. The RFQ process, as it is described in the State Auditor’s correspondence, bases the selection of a vendor upon comparison of qualitative information submitted by potential engineering firms, without consideration of pricing information. The city then negotiates a contract and the cost of the services with the successful firm. This process simply cannot fairly be classified as a competitive bid award process.

Finally, County Attorney Schott points to Code section 26.4, which exempts architectural and engineering design services from the competitive bidding requirements of Iowa Code Chapter 26 and asks whether this provision changes the conflict analysis under 362.5. We do not believe that it does. Section 26.4 removes engineering design services from the general requirement for competitive bidding, but does not preclude the use of competitive bidding for such services.

Subsection 362.5(4) provides a broad exception making the general conflict of interest prohibition inapplicable to all contracts which are made by the city “upon competitive bid in writing, publicly invited and opened,” regardless of the nature of interest a city officer or employee may have in the contract. Given the breadth of the exception, its terms must be strictly construed to protect the public. A contract which is awarded under an alternate process which does not include price-based competitive bidding, simply will not qualify for this exception. As we reasoned when applying a similar conflict provision to architectural services, “[i]n the absence of competitive bidding, the sale of these services by officials will be prohibited.” 1992 Iowa Op. Att’yGen. 192 (#92-12-2) [1992 WL 470390].

Potential conflicts arising from contracts with MER:

The State Auditor’s office has also asked that we consider potential conflicts of interest and competitive bidding requirements pertaining to the city and its contractual relationships with an appointed engineer. The Auditor’s staff has provided the following information. Eldon Rossow is president and serves on the board of directors of MER Engineering, Inc. of Fort Dodge. According to amended articles of incorporation for the company, Mr. Rossow and one other individual are the sole shareholders and directors of the corporation. In January of 2004, MER Engineering, through correspondence from Eldon Rossow, submitted a proposal to provide professional engineering services to City of Fort Dodge. In March of 2004, an executive order was issued by the mayor appointing Mr. Rossow to act as a “temporary interim city engineer” for the city and the city entered into an agreement with MER Engineering for the corporation to provide licensed engineering services at agreed upon hourly rates, to assist the engineering department for a period not to exceed 90 days.

It is our understanding that Mr. Rossow continued to serve as the “interim city engineer” until a permanent city engineer was appointed in March of 2008. During this four year period, Mr. Rossow billed and was paid an average of approximately \$5,000 per month for services provided as the city engineer. Also during this time, MER Engineering was awarded additional contracts to perform project specific

engineering services for the city. Against this background, the Auditor's office asks: "does a conflict of interest exist if the City Engineer's firm performs engineering services pursuant to a contract competitively bid, and publicly invited?"

The outcome of this inquiry, like nearly all conflict of interest issues, is controlled by the specific facts and circumstances presented and can not be definitively resolved through advice or opinion from this office. Resolution of this issue is partially dependent upon whether Mr. Rossow's appointment as the interim city engineer made him an officer or employee of the city for purposes of section 362.5. If so, then the provisions of Code section 362.5 are applicable and it is possible MER Engineering could legitimately contract with the city if the contract was awarded through a price-based competitive bidding process as allowed by subsection 362.5(4).

We believe, however, that even if the terms of subsection 362.5(4) are technically applicable, the overall relationship between Mr. Rossow, his engineering firm, and the city was quite troubling. Regardless of whether Mr. Rossow was technically an employee or officer of the city, he was serving as the acting city engineer and performing services for the city for a four year period. From that position we assume that he had access to all relevant information about city projects and was responsible for advising the city when needed engineering services exceeded his current capacity and availability. Any attempt by MER to contract for these additional services seems fraught with the potential for organizational conflicts of interest. See Medco Behavioral Care Corp. of Iowa v. Iowa Dept. of Human Services, 553 N.W.2d 556, 563-66 (Iowa 1996) (discussing federal procurement rules regarding organizational conflicts).

As stated above, the principle underlying conflict of interest policies is recognition of the fact "that a government employee or official cannot serve two masters at the same time, and the public interest should not be entrusted to an official with interests in conflict with the public interest." T & K Roofing Co., Inc. v. Iowa Dept. of Education, 593 N.W.2d at 163. If Mr. Rossow was, on the one hand, advising the city whether it needed to contract for additional outside engineering services, or assisting with preparation of the project descriptions or terms for the engineering contract, or assessing the quality of the engineering work performed for the City by all vendors, and, on the other hand, acting on behalf of MER Engineering in competing for or providing those outside services or profiting from the contract work awarded to MER, then a conflict of interest did exist – regardless of whether his

position as interim city engineer is viewed as that of an employee or of an independent contractor.¹

Conclusion: We are hopeful that this advice will be useful to you as you work to resolve these conflict of interest issues. Please note, however, that the discussion set forth herein represents the analysis of Christy Scase and myself, and is not an opinion of the Attorney General.

¹ In addition to the conflict of interest concerns, there is a strong argument that the former interim city engineer was in violation of Iowa Code section 68B.2A(1)(c) by engaging in outside employment subject to his official control, inspection, review or audit. Section 2.08.090 of the Fort Dodge City Code (from the city code chapter entitled "City Officers") defines the duty of the city engineer to include superintending public property, streets, and improvements and construction and improvement of these assets. The fact scenario provided indicates Mr. Rossow was appointed by the Mayor to fill the city engineer position on a interim basis until a new engineer could be hired and that his firm received compensation for these services. If the MER firm was providing engineering services to the city while Mr. Rossow was acting city engineer and such services fell under the scope of his supervisory responsibility, section 68A.2A may have been implicated. Unlike the situation in T&K Roofing, Mr. Rossow was not a volunteer, unpaid consultant. He was instead a "person who serves or is employed by" the city. Iowa Code § 68B.2A(1).