A G E N D A
CITY OF SEASIDE
CITY COUNCIL

SPECIAL MEETING
VIRTUAL ONLY
Thursday, March 25, 2021
5:00 PM

This meeting is compliant with Governor Newsom's Executive Order N-29-20 which allows local legislative bodies to hold public meetings electronically only, without a physical location for public participation, accessible only telephonically or otherwise electronically (video conferencing) to all members of the public seeking to observe and address the local legislative body, in order to avoid public gatherings, and until further notice.

This meeting can be watched via the City of Seaside You Tube channel
https://www.youtube.com/channel/UC1Cu7854Ohtjpr_XV1tDvRg

REMOTE PUBLIC COMMENTS To make a public comment, the following options are available:

- Before the Meeting via Email: Written comments can be emailed to CityClerk@ci.seaside.ca.us Include the following subject line: "Public Comment Item # (insert the agenda item number relevant to your comment). Written comments must be received by 5:00 p.m. on the day of the meeting. All submitted comments will be provided to the City Council or the Board for consideration, compiled as part of the record, and may be read into the record.

In an effort to ensure the virtual process closely follows our normal process, public comment will be accepted in writing during the meeting, but may not be read into the record during the meeting, but will be included as part of the final administrative record.

VIRTUAL MEETING ACCESS
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https://www.youtube.com/channel/UC1Cu7854Ohtjpr_XV1tDvRg
Or by joining the Zoom webinar link https://us02web.zoom.us/j/81936832059
Or call in phone number: 669-900-9128
Zoom Meeting Id 819 3683 2059

1. CALL TO ORDER

2. ROLL CALL – ESTABLISHMENT OF QUORUM

Ian N. Oglesby	Mayor
David R. Pacheco	Mayor Pro Tem
Jason Campbell	Council Member
Jon Wizard	Council Member
Alexis Garcia-Arrazola	Council Member

3. PLEDGE OF ALLEGIANCE

4. PUBLIC COMMENT

Members of the public wishing to address the Board on matters within the jurisdiction of the City of Seaside, but not on this agenda, may do so during the Public Comment period for up to three (3) minutes. Public Comments on specific agenda items are heard under that item. For the public record, please state your name.

5. STUDY SESSION

A. AFFORDABLE HOUSING STRATEGIES STUDY SESSION

RECOMMENDATION: Discuss strategies to advance the construction of affordable housing.

6. ADJOURNMENT

Next Regularly Scheduled Meeting:
Thursday, April 1, 2021
7:00 PM

The City of Seaside is committed to providing accessible facilities and accommodating people with disabilities in all of its services programs and activities. If special considerations are needed by any person to fully participate in this meeting, contact the City Clerk at 899-6707 no fewer than two business days prior to the meeting to allow reasonable arrangements. Agendas are posted at: http://www.ci.seaside.ca.us/129/City-Council-Committee-Agendas

Agenda-related writings or documents provided during public meetings are available for public inspection during the meeting or from the office of the City Clerk. This agenda is posted in compliance with California Governor Newsom's Executive Orders N-29-20 and N-33-20.

CITY OF SEASIDE
STAFF REPORT

Item No.: 5.A.

TO: City Council

FROM: Craig Malin, City Manager

BY: Craig Malin, City Manager

DATE: March 25, 2021

SUBJECT: AFFORDABLE HOUSING STRATEGIES STUDY SESSION

RECOMMENDATION

Discuss strategies to advance the construction of affordable housing.

BACKGROUND

The lack of affordable housing is a crisis in California, and Seaside is part of that crisis. Potential solutions to the crisis include affordable housing built by the private sector, promotion of accessory dwelling units, intensification of allowable density via up-zoning, affordable housing built by nonprofits, affordable housing built by local governments, use of public land for affordable housing, modular construction, co-housing and building code revisions promoting affordable housing.

At the March 25 Study Session, City Council members will discuss philosophies and strategies Seaside should employ to increase the availability of affordable housing in the community, potentially including creation of an aligned nonprofit to undertake planning, construction and leasing and / or sale of affordable housing.

FISCAL IMPACT

No fiscal impact to hold Study Session.

ATTACHMENTS

1. League of California Cities: Creating and Operating Nonprofit Organizations

Reviewed for Submission to the City Council by:

Craig Malin, City Manager

Creating and Operating Nonprofit Organizations

Wednesday, September 3, 2014 General Session; 1:00 – 2:45 p.m.

Shahiedah S. Coates, Jenkins & Hogin

2014 League of California Cities Annual Conference – City Attorneys' Track
Los Angeles Convention Center, Los Angeles

Notes:

Supplementing Public Services with Nonprofit Corporations:

A Survey of Key Legal Issues

Shahiedah S. Coates[1]

Introduction

Public services are often provided or supported by nonprofit corporations, a trend on the upswing. These partnerships take many forms. A municipality may create a nonprofit and delegate to it authority to perform government services and activities, enter into a collaborative relationship with a nonprofit with a close community connection to inform governmental policy development, or retain a nonprofit corporation to perform services as a contractor or coordinated service provider. Cities may provide grants to nonprofit corporations, may pay for products and services received, or may receive funds raised by nonprofits such as “friends of” parks, libraries and zoos.

Recent phenomena, such as economic recessions, the State of California’s “realignment” shift of responsibility of various programs to local governments, and restrictions on the ability of local governments to raise revenue, force cities to “do more with less.” Cities may find that creating or partnering with nonprofit corporations allows them to do just that. For instance, nonprofit corporations may be created to maintain a city landmark (such as the Lomita Railroad Museum Foundation and the Angels Flight Railway Foundation), provide financial support and/or management of public spaces (such as parks, libraries or zoos), or serve as a conduit for grants of government funds to other nonprofit corporations (such as the Harbor Community Benefit Foundation). Just as many cities outsource legal, law enforcement, or engineering services, they may consider outsourcing certain programs and activities to nonprofit corporations.[2]

Municipal-nonprofit partnerships are prevalent nationally, and an increasing proportion of government programs are managed or supported in some capacity by nonprofit corporations. A recent study of city budgets in North Carolina found that of the nonprofits funded by cities, 31 percent related to recreation, arts, and culture; 18 percent to economic development (such as chambers of commerce and business incubators); and 12 percent to public safety services.[3]

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[1] Ms. Coates is an attorney at Jenkins & Hogin, LLP, where she serves as an Assistant City Attorney to the cities of West Hollywood, Rolling Hills, and Malibu. Ms. Coates earned her J.D. from Harvard Law School and Masters in Business Administration from Woodbury University, and possesses a certificate in grantwriting from California State University, Dominguez Hills. Countless hours of pro bono work over the years have contributed to her knowledge of issues related to nonprofit organizations, particularly related to formation and qualification for tax-exempt status.

[2] However, labor agreements may limit the ability of a city to outsource certain jobs, even to a nonprofit corporation.

[3] Gordon P. Whitaker and James C. Drennan, *Local Government and Nonprofit Organizations*, COUNTY AND MUNICIPAL GOVERNMENT IN NORTH CAROLINA, UNC-Chapel Hill School of Government (2007), available at http://www.sogpubs.unc.edu/cmg/cmg11.pdf

"Private groups participate in the management of half of the seventeen hundred parks in New York City," including Central Park, and "business improvement districts manage the entire area between the White House and the Capitol" in Washington, D.C.[4] Hundreds of BIDs exist throughout the State of California and there are close to 40 in the City of Los Angeles alone.[5]

This paper discusses the unique legal issues involved in the provision (or support) of public services through nonprofit corporations in California. Section I outlines the fairly simple process of forming a nonprofit corporation in California. Section II reviews reasons that cities commonly cite as motivation for forming or partnering with nonprofit corporations. One of the most common reasons is the perception that a private entity has greater flexibility than a government agency because it is not considered a "local agency" under California law. However, Section III outlines three important laws that may apply to nonprofit corporations: the Brown Act, Public Records Act and Political Reform Act. Section IV concludes with a discussion regarding the extent to which a city may want to retain oversight and/or control over its nonprofit corporation.

I. Process of Forming a California Nonprofit Corporation

Nonprofit corporations are exempt from federal income taxation pursuant to 26 U.S.C. 501(c), but are not automatically exempt from taxation under state law. A nonprofit corporation must apply for exemption from state tax after obtaining tax-exempt status from the IRS. It is important to note that not all nonprofit corporations are eligible for 501(c)(3) status, even if they support a government activity. For instance, chambers of commerce and business leagues are 501(c)(6) organizations, social clubs are 501(c)(7) organizations, and civic leagues whose membership is limited to employees of a particular municipality are 501(c)(4) organizations. 501(c)(3) organizations are formed for charitable purposes, which includes "lessening the burdens of government." [6] To qualify for exemption as an organization that "lessens the burden of government," the government must consider the activities to be the government's responsibility, and the activities of the organization must actually "lessen" the burden of a government agency. Affordable housing development corporations, volunteer fire companies, and economic development corporations are examples of organizations likely to satisfy the test.

Nonprofit corporations are formed according to procedures set forth in state law, which prescribe a fairly simple process. Articles of incorporation must be filed with the Secretary of State and contain the information required by the California Nonprofit Corporation Law.[7] Cities

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[4] Michael Murray, *Private Management of Public Spaces: Nonprofit Organizations and Urban Parks*, 34 HARV. ENV. L. REV. 179, 180 (2010).
[5] City of Los Angeles, Office of the City Clerk, "A Quick Guide to Business Improvement Districts: BIDS 101," available at http://clerk.lacity.org/stellent/groups/Departments/@CLERK_BID_Contributor/documents/Contributor_Web_Content/LACITYP_025722.pdf
[6] Income Tax Regulations, 26 C.F.R. §1.501(c)(3)(d)(2).
[7] Corp. Code §§ 5000 *et seq.*

"are authorized to establish, fund, and operate nonprofit organizations."[8] If the corporation is created by an elected legislative body to exercise delegated authority, an additional copy of the articles must be filed with the Secretary of State for forwarding to the Controller.[9] If the corporation is created for a limited duration, the articles must provide for termination, otherwise the corporation's existence continues in perpetuity.[10] A nonprofit corporation's activities are governed by its bylaws[11] and any other adopted policies, and guided by its adopted mission.

By its nature, a mission statement limits a nonprofit corporation's scope of activity and target audience, and provides a baseline for performance evaluation. One of the first questions that should be asked before a city forms a nonprofit corporation is whether a nonprofit corporation already exists that is willing and able to assist with the desired program or activity. Partnering with an existing organization will save considerable resources and lead time involved in forming a corporation and awaiting federal and state determinations of tax-exempt status. Also, an existing organization may already have developed an effective fundraising model, obviating the need to create one for a newly formed nonprofit. Where partnering with an existing organization is not an option, the city may consider forming a new nonprofit corporation.

II. <u>Incentives to Utilize Nonprofit Corporations</u>

Nonprofit corporations are relied upon to provide or assist with public activities for a number of reasons. Commonly-cited motivations include the need or desire to: 1) fund expansion of public services or programs with alternative revenue sources; 2) shift liabilities from the city to a private entity; 3) engage a non-governmental neutral intermediary or independent contractor; and 4) operate outside of the restrictions applicable to government agencies. Each motivation is discussed in greater detail below.

A. Expanding Services and Programs with Alternative Revenue Sources

1. Private Donations

Because nonprofit corporations are primarily funded by private donations and grants, they provide an opportunity to expand public services without placing an additional strain on public funds. Although donors receive the same financial benefit from giving to a government agency as to a nonprofit corporation (and either donation effectively results in subsidization),[12] nonprofit corporations are generally more effective than government agencies at attracting

[8] Municipal Law Handbook, section 1.85, League of California Cities (2013); Corp. Code §§ 5065, 5120.
[9] Corp. Code § 5120(e).
[10] Corp. Code § 5120(c).
[11] Corp. Code §§ 5150 - 5153.
[12] Charitable donations to a governmental unit are tax-deductible under section 170(c)(1) of the Internal Revenue Code if made for a public purpose.

donations and volunteers.[13] One theory suggests that nonprofit corporations are more attractive to donors because they have lower monitoring costs and have financial incentives inapplicable to government agencies.[14] Some people may assume that private entities are more efficient than the government and are therefore more willing to subsidize their work. Alternatively, some people may feel that they are "captive" contributors to government through taxation and are unwilling to voluntarily contribute more.

Also, nonprofits are in the business of raising funds and can be adept at doing so. They have access to sources that facilitate large fundraising campaigns such as Charitybuzz.com (an online auction broker of luxurious items for charities) and GuideStar (an information service that provides financial reports and other records that contribute to the perception that nonprofits are more transparent or accountable than government agencies), while governments typically neither engage in direct solicitation nor participate in broad fundraising efforts. As a result, the general public simply may not be aware that they can make tax-exempt donations to government agencies. One exception to this generality is the fairly common bequest of land to governments. For instance, the Los Angeles Griffith Park was transferred through bequest. Cities are advised to pay close attention to the terms and conditions contained in these land grants. Where a grant places a restriction on use of the land (i.e., the land can only be used for a park) and contains a right of reversion in the grantor or grantor's heirs, the government's interest in the property can be lost if the restrictions are not respected.[15]

2. Tax-Exempt Revenue Bonds

Tax-exempt revenue bonds may provide a substantial source of financing for eligible projects (such as capital improvement, economic development projects, and construction of public facilities) conducted by nonprofit corporations. Unlike bonds issued by a city, these revenue bonds are not subject to voter approval. Voters are not entitled to decide whether nonprofit corporation revenue bonds should be issued because debt service is derived from revenue sources such as parking fees, admission charges, and lease payments, and does not constitute a general obligation of the public. However, the community receives public benefits from the project. Today, we take for granted that nonprofit corporations have access to tax-exempt revenue bonds, but the scheme was not always favored.[16]

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[13] See Michael Murray, *Private Management of Public Spaces: Nonprofit Organizations and Urban Parks*, 34 HARV. ENV. L. REV. 179, 180 (2010).

[14] *Id.* at 202-203 ("responsibility to, or dependence on, contributors… incentivizes behavior that attracts donors.").

[15] *See, e.g., Walton v. City of Red Bluff* (1991) 2 Cal.App.4th 117, in which property granted to the city for the purpose of maintaining a library, subject to reversion reverted to the grantor's heirs because the city failed to maintain a library; and *City of Palm Springs v. Living Desert Reserve* (1999) 70 Cal.App.4th 613, 622, in which the court found that conveyance of property to the city for use as a desert wildlife preserve subject to a reversionary interest did not place the property into the public trust, but "must be construed as granting to the City a fee simple subject to a condition subsequent, and assigning [grantor] a power of termination."

[16] *See, e.g.,* Hart H. Spiegel, *Financing Private Ventures with Tax-Exempt Bonds: a Developing 'Truckhole' in the Tax Law*, 17 STAN. L. REV. 224, 227 (1965). The article laments that IRS policy, culminating with Revenue

The Bergeson-Peace Infrastructure and Economic Development Bank Act[17] authorizes the California Infrastructure and Economic Development Bank ("I-bank") to serve as a conduit issuer of tax-exempt and taxable bonds on behalf of 501(c)(3) organizations pursuing eligible projects. Bond proceeds must create public benefits in the community where the project is located by enhancing the economic, social, or cultural quality of life for local residents, and be used for a project consistent with any existing local or regional comprehensive plan. [18] In recent years, the I-bank has issued revenue bonds on behalf of 501(c)(3) organizations such as the RAND Corporation, Youth Services Center of Riverside, San Francisco Ballet Association, Santa Barbara Center for Performing Arts, and Salvation Army.

3. Special Assessments (BIDs)

Business improvement districts ("BIDs") are authorized by state law,[19] created by ordinance subject to public hearing and majority protest, and provide a mechanism for revenue generation through special assessments for "activities" and "improvements" such as newsletters, private security and escorts, information booths, banners, holiday lights, street cleaning and maintenance, and promoting tourism and economic development. Special assessments must be commensurate with the benefits businesses receive from the BID's activities,[20] must be periodically renewed by city council,[21] and provide a reliable source of funding as an alternative to general municipal funds or sporadic private donations.

Often, cities do not administer the activities and improvements funded by BID assessments, but contract with nonprofit corporations created for the sole purpose of bearing that responsibility. Assessment funds received by the city are transferred to the nonprofit corporation, and a contract specifying the terms of the arrangement is entered into by the city and

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Ruling 63-20, results in "erosion of the tax base" by expanding "private" access to tax-exempt financing, and questions the legitimacy of the public benefit of such projects. ("Typically, a private "nonprofit" corporation is organized. Its revenue bonds are issued to obtain funds with which to build the aluminum mill, garage, or other facility, which is then leased to private interests. The proceeds from the long-term lease of the facility are pledged to amortize the bonds. At the end of thirty to forty years the facility belongs to the city. A package of this sort presented to the city council has great appeal. The city invests nothing and becomes the owner of a project, without cost, after thirty or forty years. Its own credit is not pledged on the bonds. It has all to gain and nothing to lose.") at 227.

[17] Gov. Code §§ 63043 – 63047.

[18] *See* Gov. Code §§ 63043 – 63047 and501(c)(3) Revenue Bond Program description available at www.ibank.ca.gov/501c3_bonds.htm. I-bank applications must contain a project description including, among other things, a comprehensive summary of all public benefits of the project and description of any past, present or potential controversy connected with the project or its financing. California Infrastructure and Economic Development Bank Policies and Procedures for Conduit Revenue Bond Financing for Economic Development Facilities (updated August 24, 2010), section II.B.

[19] In California, BIDS are most commonly formed pursuant to the Parking and Business Improvement Area Law of 1989 or the Property and Business Improvement District Law of 1994 (Streets & Highways Code §36500 et seq. and §36600 et seq., respectively).

[20] *See, e.g.*, Sts. & High. Code § 36536.

[21] Assessments levied under the 1989 Act must be renewed annually, while assessments under the 1994 Act may be approved for five-year periods

the nonprofit. The term of the contract should coincide with the term of the approved assessment, subject to renewal concurrent with the BID assessment. In the Los Angeles area, this model has been adopted for several BIDs in the City of West Hollywood[22] and Downtown Santa Monica.[23] Business owners in West Hollywood have voiced their approval of this model's ability to provide tailored services and programs to businesses and provide a catalyst for public-private collaboration.[24] For cities with BIDs whose primary activities are not traditionally within the purview of government agencies (such as concert, special event, or tourism planning and promotion), use of a nonprofit corporation may relieve the city of otherwise having to develop or retain in-house expertise.

B. Shifting Liabilities to a Private Entity

1. Affordable Housing

State law mandates that cities provide their "fair share" of affordable housing to meet regional housing needs.[25] However, cities are not required to assume the liabilities incident to developing and managing affordable housing to satisfy this statutory requirement, which could be substantial. Instead, cities may offer density bonuses and other incentives to developers,[26] may cooperate with projects that qualify for federal and state low income housing tax credits ("LIHTC"), and may administer affordable housing programs through a separate nonprofit corporation. Cities may wish to avoid directly serving as affordable housing developer/property manager for the reasons illustrated below.

In California, the Tax Credit Allocation Committee administers the federal and state LIHTC programs. Those programs require that eligible tenants have an equal opportunity to apply for an affordable unit, which is oftentimes accomplished through a lottery. A city may facilitate the lottery process, in which interested persons complete a lottery or waitlist application, are evaluated by city staff for income eligibility, and eligible applicants are sorted in a random order used to determine the order in which applicants will be invited to submit rental applications. Rental applications are ultimately evaluated by the property manager. Imagine that an applicant files a claim with the California Department of Fair Employment and Housing ("DFEH") alleging that they were denied housing on the basis of an unlawful discrimination. If the city is not the property manager, its obligations in responding to such a claim and the scope of its potential liability are greatly reduced.[27]

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[22] http://thesunsetstrip.com/info/about-sunset-strip-business-association-ssba
[23] http://www.downtownsm.com/
[24] Most recently in a joint presentation by business owner Nic Adler and Mayor John D'Amico at the May 2014 California Contract Cities Association 55th Annual Municipal Seminar.
[25] Gov. Code § 65584.
[26] Authorized by Gov. Code § 65915 – 65918.
[27] See Attachment 1 for a sample list of questions from DFEH in its investigation of a claim alleging discrimination on the basis of a disability in connection with a LIHTC lottery.

Beyond housing discrimination complaints that could lead to federal litigation, cities may wish to avoid the potential political backlash of exercising basic landlord rights such as evictions, inspections, and retaining a portion of a tenant's security deposit where appropriate. Tenants may attempt to use council meetings as the venue to voice their discontent. Elected officials may feel political pressure to take (or avoid) actions that affect registered voters, particularly during election season. These factors add an undesirable layer of complexity to the landlord-tenant relationship, which by its nature is often fraught with difficulties.

As separate entities, nonprofit housing corporations have the potential to insulate cities from the challenges discussed above and others, while allowing the city to retain some level of influence over the provision of affordable housing within its boundaries. Further, some sources of grant funds may only be available to non-governmental organizations. As separate entities, housing corporations may benefit from being governed by a diverse board of directors representing public officials, public employees, business and community leaders, developers, and affordable unit residents, can greatly contribute to creative productivity.

Many cities, including the City of West Hollywood, whose Community Housing Corporation has developed 14 apartment communities ,[28] counties, and groups of cities utilize nonprofit corporations to provide affordable housing.

2. Construction of Public Facilities (Lease-backs)

Construction of public facilities and infrastructure often involves long-term and greatly expensive projects that lend themselves to a lease, lease-back arrangement. The lease-back arrangement typically involves a government agency leasing undeveloped land to a developer who bears responsibility for constructing a public facility that, when completed, is leased back to the government agency. The California Attorney General has described the lease-back as "commonly used to finance the construction of public facilities through the aegis of a nonprofit corporation, thus avoiding the debt limitation provisions of the California Constitution applicable to the state and local governments."[29] It is a "classic medium" that has "been approved in cases such as *Dean v. Kuchel* (1950) 35 Cal.2d 444; *City of Los Angeles v. Offner* (1942) 19 Cal.2d 483 and *County of Los Angeles v. Nesvig* (1965) 231 Cal.App.2d 603,"[30] and used for construction of stadiums, sports arenas, theaters, and even rubbish incinerators.

Sections 5.235 and 5.236 of the Municipal Law Handbook discuss lease-back agreements and provide an outline of requirements.[31] In addition, a lease-back agreement whose term exceeds five years must receive prior authorization by an ordinance subject to referendum.[32]

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[28] West Hollywood Community Housing Corporation, "What We Do," available at http://www.whchc.org/index.php?option=com_content&view=article&id=160&Itemid=78
[29] 70 Ops.Cal.Atty.Gen. 57 (1987), n. 2.
[30] 70 Ops.Cal.Atty.Gen. 57 (1987).
[31] "1) Rent must be abated when a city does not occupy or have beneficial use of the property.

The lease-back arrangement has oft been upheld against legal challenges. In one of the most notable cases, *Los Angeles County v. Nesvig,*[33] the court upheld the County's lease, lease-back arrangement crafted to facilitate construction of the theater and forum now known as the Music Center in downtown Los Angeles. The arrangement involved a County lease of land to a private entity responsible for construction, and a lease-back of the constructed facility to the County for 30 years, with a concurrent sublease authorizing a non-profit organization to manage and operate the Music Center on behalf of the County. The arrangement was challenged as violating the constitutional debt limit. The court held:

> "if the lease or other agreement is entered into in good faith and creates no immediate indebtedness for the aggregate installments therein provided for but, on the contrary, confines liability to each installment as it falls due and each year's payment is for the consideration actually furnished that year, no violence is done to the constitutional provision." However, the arrangement is invalid if it creates a "full and complete liability upon" execution of a single instrument or "is actually a conditional sales contract in which the 'rentals' are installment payments on the purchase price."[34]

C. Engaging a Non-Government Organization

Particularly where activities involve sensitive political issues or a community mistrusting of government agencies, it may make sense to engage an independent nonprofit organization with strong community ties as a neutral intermediary. This approach proved successful when the Housing Authority of the County of Los Angeles ("Authority") engaged the Advancement Project to conduct an in-depth assessment of the needs of the housing developments in the Watts community in preparation for revitalization of one of the most violent areas in Los Angeles. The Advancement Project is a California-based nonprofit civil rights organization that concentrates on issues related to inequality in access to public services in minority and disadvantaged communities. As a non-government organization with strong credibility in and ties to the community, the Advancement Project was able to gain greater access to information than the Authority likely could have. The Advancement Project produced a community assessment and recommended violence reduction strategies, which are being implemented through an ongoing collaboration including the Los Angeles Police Department and the Authority, and confirmed by a 2011 inter-agency agreement. According to the Advancement Project, the resulting Community Safety Partnership has reduced violent crime in Watts by more than 50 percent, notably decreased youth gang membership and activity, reduced homicide rates, and laid the

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2) The obligation of a city to make payments must be on an annual basis and subject to appropriation (i.e., if the city council does not budget the funds for payment, payment is not due). Acceleration of rental payments in the event of non-appropriation or in the event of default is not allowed because to do otherwise would violate the debt limitation of Cal Const art XVI, §18. A covenant to appropriate annually is common. Further, acceleration of payments in the event of default is not a valid provision of a financing lease.

3) Fair market rent should be paid for the property, taking into consideration the nature and use of the property and any option to purchase."

[32] Gov. Code § 54240 *et seq.*

[33] (1965) 231 Cal.App.2d 603.

[34] *Los Angeles County v. Nesvig* (1965) 231 Cal.App.2d 603, 609-619 (quoting an extensive list of cases).

groundwork for future investment in the community that may be conducted by the Authority and/or others.[35]

Cities with limited resources often outsource certain activities to independent contractors. In some cases, nonprofit corporations may be available to serve as independent contractors. For instance, the Institute for Building Technology and Safety ("IBTS") is a 501(c)(3) nonprofit corporation that performs a variety of municipal services, such as administrative services and communications, financial services, planning and zoning, public works, engineering and floodplain management, code enforcement, permit issuance and inspections, and emergency preparedness. One of IBTS's more vocal clients is the City of Central, Louisiana, whose arrangement with IBTS includes the corporations' pledge to return excess income to the city if expenses are less than the contract award, among other benefits.[36]

D. Operating Outside of the Restrictions Applicable to Government Agencies

Likely the most cited reason that government agencies perform certain activities through nonprofit corporations is the presumption that private entities are exempt from the regulations applicable to public agencies. Cities are "government actors" that must avoid restraining the public's freedom of speech and expression, and must avoid discriminating on the basis of a protected characteristic. They must adhere to the debt limit contained in the California Constitution, the open meeting requirements of the Brown Act, the disclosure requirements of the Public Records Act, and the reporting requirements of the Political Reform Act. Cities generally must receive voter approval to raise revenue through taxes, special assessments, and bonds. Finally, labor agreements, fiscal policies, and other regulations may increase operational costs and reduce flexibility in ways inapplicable to private organizations.[37] However, as Section III explains, nonprofit corporations can be subject to many of the same restrictions as cities, depending on their structure and operations.

III. Nonprofit Corporations are Sometimes Treated as Government Agencies

While nonprofit corporations are generally exempt from the legal restrictions applicable to cities, nonprofit corporations serving a governmental function may be subject to laws applicable to cities in very fact-specific circumstances. Generally, when statutory requirements apply to a government entity, it cannot avoid the statutory requirements by delegating administrative responsibilities to a nonprofit corporation.[38] Even if a nonprofit corporation is not

[35] http://www.advancementprojectca.org/?q=Community-Safety-Partnership-Los-Angeles
[36] Recently discussed in a joint presentation at the September 2013 International City/County Management Association ("ICMA") conference. The conference power point is available at http://www.ibts.org/services/municipal-services.html
[37] But see section III for a discussion on when the laws applicable to cities may apply to nonprofit corporations.
[38] *See, e.g.*, 81 Ops.Cal.Atty.Gen.281 (1998) (finding that a nonprofit created by a redevelopment agency generally must comply with the same laws and regulations as the agency itself, including open meeting laws, acquisition and relocation requirements, and public bidding and prevailing wage statutes).

legally required to comply with the Brown Act, Public Records Act, and Political Reform Act, it may wish to voluntarily opt in to the extent practicable.

A. Brown Act

The governing board of a nonprofit corporation may be a "legislative body" subject to the Ralph M. Brown Act. Government Code section 54952(c) provides that a "legislative body" includes:

> "(c) (1) A board, commission, committee, or other multimember body that governs a private corporation, limited liability company, or other entity that either:
>
> (A) Is created by the elected legislative body in order to exercise authority that may lawfully be delegated by the elected governing body to a private corporation, limited liability company, or other entity.
>
> (B) Receives funds from a local agency and the membership of whose governing body includes a member of the legislative body of the local agency appointed to that governing body as a full voting member by the legislative body of the local agency."

Whether a nonprofit is "created" by the elected legislative body of a government agency is a question of law.[39] "To 'create' means, among other things, 'to bring into existence,' or 'to produce or bring about by a course of action or behavior.'"[40] A property owners association created by a city to perform administrative functions related to a business improvement district funded by assessments is a "legislative body" subject to the Brown Act.[41] In *Epstein v. Hollywood Entertainment Dist. II Business Improvement District*, the District argued that its board was not subject to the Brown Act because, among other things, the District provided only "supplemental" services to the city.[42] Calling it "backwards" to focus on the "supplemental" nature of the services, the court clarified that application of the Brown Act turns not on "the *kinds of services*, so much as the *nature of the source of funding* to be used for them."[43]

A nonprofit corporation formed to provide programming for a cable television channel set aside for educational use by a cable operator pursuant to its franchise agreement with a city and designated by the city to provide the programming services is subject to the Brown Act.[44] A nonprofit entity created by a community redevelopment agency, and delegated authority of the agency, is subject to the Brown Act.[45] Although the Brown Act may apply, a nonprofit

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[39] *Epstein v. Hollywood Entertainment Dist. II Business Improvement Dist.* (2001) 87 Cal.App.4th 862, 876.
[40] *Californians Aware v. Joint Labor/Management Benefits Com.* (2011) 200 Cal.App.4th 972, 979-980 (quoting 92 Ops.Cal.Atty.Gen. 102, 107 (2009)).
[41] *Epstein v. Hollywood Entertainment Dist. II Business Improvement Dist.* (2001) 87 Cal.App.4th 862.
[42] *Id.* at 874.
[43] *Id.* (emphasis in original).
[44] 85 Ops.Cal.Atty.Gen. 55 (2002).
[45] 81 Ops.Cal.Atty.Gen. 281 (1998).

corporation's board may not be authorized to meet in closed session with the city attorney of its creating city. For instance, the Brown Act does not authorize a nonprofit created by a redevelopment agency and delegated authority to negotiate settlement of eminent domain disputes to meet in closed session with the redevelopment agency's legal counsel unless the nonprofit is a party to the dispute.[46]

A private pre-existing corporation does not become subject to the Brown Act by simply entering into a contractual arrangement to exercise authority that a government entity could exercise.[47] Further, a nonprofit corporation is not subject to the Brown Act merely because it receives public funds.[48] For instance, the DWP nonprofits discussed in Section IV(A) below are not subject to the Brown Act because, although funded by the city, their boards do not include a member of the legislative body of the city.[49]

B. Public Records Act

As a private corporation, a nonprofit is generally not subject to the Public Records Act; [50] however, "entities that are legislative bodies of a local agency pursuant to subdivisions (c) and (d) of Section 54952 [of the Brown Act]"[51] must comply with the Public Records Act.[52] ***To emphasize, not all nonprofits subject to the Brown Act are subject to the Public Records Act—only those subject to the Brown Act under subdivision (c) or (d) of Section 54952 of the Government Code.*** Nonprofit corporations that voluntarily subject themselves to the Brown Act do not consequently become subject to the Public Records Act. Meeting agendas and other writings distributed to a majority of a board subject to the Brown Act in connection with a matter subject to discussion or consideration at an open meeting are public records.[53]

C. Political Reform Act

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[46] *Shapiro v. Board of Directors of the Centre City Development Corporation*, 134 Cal.App.4th 170, 182 (2005) ("we look to the content of section 54956.9 to determine whether a meeting between the legislative body of one local agency and the legal counsel of another local agency falls within the narrow category of closed-session meetings permitted by section 54956.9. Doing so, we conclude that nowhere in the plain text of section 54956.9 is the practice authorized.").

[47] *Epstein v. Hollywood Entertainment District II Business Improvement District*, 87 Cal.App.4th 862, 871 (2001) (citing *International Longshoremen's & Warehousemen's Union v. Los Angeles Export Terminal, Inc.*, 69 Cal.App.4th 287, 300, fn. 5).

[48] Cal. Attorney Gen. Office, The Brown Act: Open Meetings for Legislative Bodies (2003) pp. 5-6, available at http://caag.state.ca.us/publications/2003_Intro_BrownAct.pdf

[49] 87 Ops.Cal.Atty.Gen.19 (2004).

[50] *See, e.g.*, *Community Youth Athletic Center v. City of National City* (2013) 220 Cal.App.4th 1385 and *Consolidated Irrigation District v. Superior Court* (2012) 205 Cal.App.4th 697.

[51] Gov. Code § 6252 (a).

[52] 85 Ops.Cal.Atty.Gen.55 (2002) ("Our answer to the first question [applicability of the Brown Act] thus answers the second question [applicability of the Public Records Act].")

[53] Gov. Code § 54957.5(a).

The Political Reform Act contains two main requirements: covered agencies must adopt a conflict of interest policy and covered "public officials" must disclose their economic interests.[54] Nonprofit board members are frequently wealthy and well-connected individuals who may prefer to keep their financial information private, and certainly do not think of themselves as "public officials" subject to public scrutiny. However, board members may be required to file statements of economic interest (FPPC Form 700) if the nonprofit corporation satisfies the four-part "*Siegel* test." The requirements of the Political Reform Act cannot simply be ignored; violators may be subject to fines and criminal prosecution.[55]

The Political Reform Act defines "public official" as "every member, officer, employee or consultant of a state or local government agency."[56] The Fair Political Practices Commission ("FPPC") defines "member" to include "salaried or unsalaried members of committees, boards or commissions with decisionmaking authority," meaning that the committee, board or commission:

(i) may make a final governmental decision;
(ii) may compel a governmental decision;
(iii) may prevent a governmental decision either by reason of an exclusive power to initiate the decision or by reason of a veto that may not be overridden; or
(iv) makes substantive recommendations that are, and over an extended period of time have been, regularly approved without significant amendment or modification by another public official or governmental agency.[57]

In determining whether a nonprofit corporation is a "local government agency," the FPPC considers four criteria:

(i) Whether the impetus for formation of the corporation originated with a government agency;
(ii) Whether it is substantially funded by, or its primary source for funds is, a government agency;
(iii) Whether one of the principal purposes for which it is formed is to provide services or undertake obligations which public agencies are legally authorized to perform and which, in fact, they traditionally have performed; and
(iv) Whether the corporation is treated as a public entity by other statutory provisions.[58]

Over time, some general rules have developed. A nonprofit corporation may be subject to the Political Reform Act even if it does not satisfy all four criteria.[59] Chambers of commerce, visitor bureaus, and downtown business associations perform activities that benefit government

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[54] Gov. Code §§ 87200 – 87210.
[55] Gov. Code §§ 9100 – 91014.
[56] Gov. Code § 82048.
[57] Section 18701 of the Regulations of the FPPC, Title 2, Division 6, Cal. Code Regs., subdivision (a)(1). A comment to § 18701 advises: "In limited circumstances, the members of a nonprofit organization may be 'public officials.' (*In re Siegel* (1977) 3 FPPC Ops. 62.)."
[58] *In re Siegel* (1977) 3 FPPC Ops. 62.
[59] *In re Carter* (2002) FPPC Advice Letter A-02-202.

agencies, but are not necessarily traditionally performed by government agencies.[60] Tax-exempt status alone is not sufficient to find that the corporation is treated as a public entity.[61] However, a fact-specific analysis is required to determine whether any given nonprofit corporation is subject to the Political Reform Act. When in doubt, seek the advice of the FPPC.

In addition, a nonprofit corporation may be considered a "state actor" under federal law. For purposes of discrimination actions under 42 U.S.C. section 1983, a volunteer fire company is a "state actor" even if it is a private, nonprofit corporation,[62] because "[f]ire protection is a public function which amounts to state action even if the fire protection unit is composed of voluntary or unpaid members," and "most volunteer fire companies occupy town-owned land and buildings and utilize town-owned firefighting equipment."[63]

IV. Maintaining Oversight and Control

Cities are advised to maintain ongoing oversight and an appropriate level of control over the nonprofit corporations that they create. Proper oversight can deter questionable financial practices of the nonprofit and control may be necessary in certain contexts.

A. Oversight as a Deterrent to Bad Behavior

Two nonprofit organizations (the Joint Safety Institute [JSI] and Joint Training Institute [JTI]) were created several years ago through collective bargaining between the City of Los Angeles Department of Water and Power ("DWP") and its employees' labor union. The organizations were created to administer workforce training and safety programs, and are contractually entitled to annual contributions from the City. A fairly recent news article reported that the City had contributed a cumulative $40 million, some portion of which was spent by the nonprofits on questionable activities.[64] In response to the revelation, Los Angeles Mayor Eric Garcetti sought the financial records of the organizations, which they refused to disclose on grounds that they "are not city agencies and therefore not subject to open records laws."[65] Thus began the epic legal battle that continues today.

The City subpoenaed the nonprofit organizations' financial records, and the organizations moved to quash the subpoena.[66] In upholding the subpoena, the court found that while the operative agreements between the City and the organizations did not expressly subject them to a

[60] *Id.*
[61] *Id.*
[62] *Gibson v. Hurleyville Fire Co. No. 1*, 1 F.Supp.2d 329, 330 (S.D.N.Y., 1998).
[63] Survey of 1998 Nonprofit Case Law (January-June), 33 U.S.F. L. Rev. 231, 252 (Winter 1999).
[64] Jack Dolan and Emily Alpert Reyes, *DWP Union Boss Warns City Not to Withhold Payments to Nonprofits*, L.A. TIMES, June 17, 2014.
[65] *D'Arcy v. Galperin*, Los Angeles Superior Court Case No. BS146924, n. 9 ("The California Attorney General has stated that the JSI and JTI are not 'public agencies' subject to the open-meeting requirements of the Brown Act. 87 Cal.Ops.Atty.Gen. 19 (2004)." The ruling is subject to a stay while the Second District Court of Appeal reviews the lower court's judgment.
[66] *Id.*

City audit, a "broad construction" of the City's charter provision authorizing the Controller to audit the accounts of "every person charged in any way with the safe-keeping or disbursement of public money" provided sufficient authority. Relying on *People v. Johnson*,[67] which found that monies disbursed to a private entity remained "public funds" so long as the government continues to exercise supervision and control over the funds and their ultimate use, the court found that the grants remained "public funds" subject to audit under the City charter… "albeit barely."[68]

As a third prong of the trifecta effort to learn how City funds were spent, the City replaced its appointed members on the organizations' board of trustees. However, to avoid sharing information with the City's appointees, the organizations refused to recognize the validity of the appointments and to meet. On July 18, 2014, the Los Angeles Superior Court ordered the organizations to recognize the City's appointees, but declined to go so far as to order the board to meet.[69]

The unfortunate ordeal could have been avoided if the funding agreement included a provision authorizing the City to review the organizations' accounts.

B. Control May Have Legal Implications

In some instances, the city may need to retain a certain amount of control over the nonprofit to protect certain legal interests. For instance, in *Los Angeles County v. Nesvig*,[70] discussed in Section II(B)(2) above, the sublease operating contract incident to a lease-back arrangement was challenged as an unlawful delegation to a private entity of a government agency's power. The court described the following "general rule":

> "while a public body may not delegate its power of control over public affairs to a private group, it may delegate the performance of administrative functions to such groups if it retains ultimate control over administration so that it may safeguard the public interest." Thus, "there are two issues, whether the function is a proper one for delegation, and whether the manner of delegation retains the necessary, ultimate control over administration in the hands of the public entity."[71]

Whether sufficient control is retained largely depends on the facts of the case. For instance, failure to retain control of prices charged for facilities is fatal; however, retention of control over long-term and short-term subleases, admission prices, concessions, food and refreshment prices, and/or the operator's annual budget satisfies the rule.[72]

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[67] 209 Cal.App.4th 800 (2012) (misappropriation of public funds by a group home).
[68] *D'Arcy v. Galperin*, Los Angeles Superior Court Case No. BS146924. Because the ruling is based on an interpretation of the City charter, the court did not determine the nonprofits' argument that they are not subject to the Public Records Act or the Brown Act (n. 11).
[69] *James McDaniel et al. v. Brian D'Arcy et al*, Los Angeles Superior Court Case No. BC543782 (July 17, 2014 Tentative Ruling).
[70] (1965) 231 Cal.App.2d 603.
[71] *Id.* at 616-617 (internal citations omitted).
[72] *Id.*

Also, see the discussion in Section IV(A) regarding the impact of control on the "public" character of funds transferred to nonprofit corporations.

Conclusion

Cities have significant opportunities to expand and enhance public services through the use of nonprofit corporations. It is fairly easy to form a nonprofit corporation in California, and depending on the organization's purpose, achieving tax-exempt status may be straightforward as well. Nonprofit corporations may provide access to alternative funding sources, serve as a mechanism for cities to reduce liabilities incident to certain activities, act as neutral intermediaries or independent contractors, and may allow certain activities to be conducted outside of the restrictions applicable to cities. However, nonprofit corporations may be subject to laws applicable to cities such as the Brown Act, Public Records Act, and Political Reform Act, and an analysis should be performed prior to formation to ensure that the corporate structure is compatible with expectations. The questions that follow may assist in preliminary planning. After the appropriate structure is designed and the nonprofit is formed, cities are well-advised to maintain appropriate levels of oversight and control.

Preliminary Considerations for Creating Nonprofit Corporations

1. ***What is the "mission" of the activity or project, and what is its public benefit?***
2. ***Does the mission or project have the potential to attract a dedicated base of donors and volunteers (i.e., might the project have "friends" or attract a "working board" that can assume some responsibilities of city staff)?***
3. ***Can it be accomplished more efficiently by a private organization?***
4. ***Are any existing nonprofit organizations in the community capable of accomplishing or contributing to the mission? If so, what is the relationship between existing nonprofit(s) and the city/community?***
5. ***Would partnering with an existing nonprofit benefit the project in a unique way or relieve the city from costs involved in formation and management of a new nonprofit organization?***
6. ***Do any aspects of the project necessitate city control over program design and/or implementation?***
7. ***Does success of the project require that some or all activities occur outside of public scrutiny (i.e., would the purpose be frustrated if the organization were subject to the Brown Act and Public Records Act)?***
8. ***Does the project qualify for alternative funding, such as tax-exempt revenue bonds, BID assessments, or grants?***

9. ***If the city provides funding to the nonprofit, how will adequate control over and access to granted funds be accomplished?***
10. ***Do labor agreements or other constraints prevent shifting city responsibilities to a private entity?***

Attachment 1- Sample Inquiry from DFEH re: Housing Discrimination Claim response.

You must submit a response to the questions below <u>within twenty (20) days</u> of the date of this letter.

1. State the legal name of your business and any other name(s) under which you do or have done business in California.

2. State your business address. Please note that you are required to notify the DFEH in writing of any change of address and the effective date of such change while the complaint is under investigation and throughout any administrative adjudication. (California Code of Regulations, title 2, sections 7403 and 7411).

3. State type of legal business entity (i.e., corporation, partnership, limited partnership, sole proprietorship).

4. State the number of individuals you employ in California.

5. Does your company have a current contract(s) for the provisions of goods, services or public works with the State of California or receive federal funds? If so, name the awarding agency.

6. Identify and list the legal owners of the property named in the complaint by name, address, telephone number, and type of ownership.

7. Identify and list all other housing rental properties in California owned in whole or in part by each of the persons named above.

8. State the number of living units (individual apartments, houses, etc.) you or your company rent or lease to the public in California.

9. List all persons and/or firms involved in the management of the property named in the complaint by name, address, telephone number, job title, and management responsibility.

10. Are you a recipient of a state and/or federal low income housing tax credit for the property identified in the complaint?

11. Do you receive any HUD subsidies? If yes, please provide a detailed written explanation with documentation.

12. Provide relevant information or evidence that will assist us in determining the merits of the complaint.

13. Identify and list by name, title, address, and telephone number each individual who made the decision to deny complainant's accommodation request to be given priority for of the affordable units located at the property in the complaint.

14. State the reason[s] why the above decision maker took the above-mentioned actions.

15. Submit all communication records involving the complainant's accommodation requests and your actions upon those requests. If requests were verbal, provide a narrative of each request including dates and parties involved.

16. List all units address, unit number or other designations, home and work telephone numbers, and disabilities status of all the persons currently occupying each unit. Submit copies of the rental applications for all tenants listed. Indicate if rental is vacant.

17. For all persons who requested accommodations during the past 12 months, list the name, disability, address, home and work telephone numbers, date of request, reason for the request, and name of person who approved or denied each request and reasons for the approval or denial.

18. Describe in detail your policy and procedure for handling disabled tenant accommodation requests. Submit a copy of any written rules and policies. Explain how the policy was applied to the complainant.

19. Describe your rental policy or guidelines regarding people with disabilities. Submit a copy of your policy. Explain in detail how the policy was applied to the complainant.

20. Describe in detail your rental advertising procedures.

21. Describe in detail your rental procedures. Submit a copy of any written policy or procedures.

22. Describe in detail your criteria for selecting tenants. Submit a copy of any written policy or procedures.

23. For all persons who applied to rent during the last 12 months, list the name, address, telephone number, disability status, unit applied for [if known], and date of application. For each person indicate if accepted as tenants, and, if denied, indicate reason for denial.

24. Submit copies of the rental application of each current tenant. Indicate tenant's disability status.