

# **Frequently Asked Questions (FAQ) – TxCDBG Conflict of Interest Provisions**

December 6, 2017

## **I. Background and Types of Conflicts of Interest (COI)**

### A. What is a conflict of interest (COI)?

In general, a conflict of interest occurs when one's private interest and public duties overlap, resulting in a real or perceived lack of independence or impartiality.

To address such concerns, the Texas Department of Agriculture (TDA) and the U.S. Department of Housing and Urban Development (HUD) have developed policies to reduce conflicts of interest. Broadly speaking, a conflict of interest policy prohibits any employee, agent, elected official, or officer or their family or business associates from obtaining a financial interest or personal benefit from any TxCDBG assisted activity. TDA encourages Grant Recipients to avoid all conflicts of interest, real or apparent.

### B. How can a community evaluate whether a conflict of interest violation will or has occurred?

#### a. There are two sets of conflict of interest rules that exist:

- i. Rules for COI related to procurement of goods, supplies/equipment and services; or
- ii. Rules for non-procurement COI (all others activities such as real estate acquisition, provision of assistance with CDBG funds to individuals, businesses, etc.).

#### b. Once a determination of whether the conflict is a procurement and/or non-procurement COI, use the appropriate guidance below.

## **II. Procurement of goods or services COI (2 CFR 200.318(c) and 2 CFR 200.319(a))**

### A. To what type of activities does procurement COI apply?

It applies to the procurement of:

- Supplies
- Equipment
- Construction
- Services

### B. What is the regulation governing procurement conflict of interest?

Generally, the regulation at 2 CFR 200.318 prohibits an employee, officer or agent of the grantee/subgrantee or recipient/subrecipient from participating in the selection, or in the award or administration of a contract supported by Federal funds if a conflict of interest, real or apparent, would be involved. In addition, under 2 CFR 200.319(a), all procurement transactions must be conducted in a manner providing full and open competition. Therefore, contractors that develop or draft specifications,

requirements, statements of work, or invitations for bids or requests for proposals must be excluded from competing for such procurements.

C. When would such a conflict arise?

A procurement conflict of interest would arise when:

- 1) The employee, officer or agent,
- 2) Any member of his immediate family,
- 3) His or her partner, or
- 4) An organization which employs, or is about to employ, any of the above, has a financial or other interest in the firm selected for an award.

D. The COI procurement regulation applies to the Grant Recipient's employees, officers, and agents. How can these terms be distinguished? What about independent contractors?

The main difference between employee, agents and/or independent contractors is the degree of control the principal has over the duties of any of these three types of workers. It is important to distinguish between the various relationships to determine whether the COI policy is applicable.

Note: employees, officers, and agents of subrecipients, such as benefitting utilities and benefitting businesses, must comply with the same COI policies as those of the Grant Recipient.

An "employee" is a person who is in the paid service of a governmental unit by competent authority, and who performs tasks the details of which the governmental unit has the legal right to control.

An "agent" is a person or entity that has been authorized to act on behalf of another person or entity (i.e. an agent is authorized to act on behalf of the principal). With respect to the TxCDBG Program only, grant administrators and engineering consultants are considered agents of the Grant Recipient once they are procured. An existing business relationship does not necessarily constitute agency, but authorization to act on behalf of the Grant Recipient in one capacity for a specific CDBG project triggers COI rules and precludes the individual or entity from participating in another capacity on the same TxCDBG project.

An "independent contractor" is a person providing services or goods not as an employee, subject to the management of the person or entity, but as a freelancer, answerable only for the results of the contract. If the recipient of the services or goods does not control what the worker does and how the worker does his/her job, does not manage the business aspects of the worker's expenses and benefits, or have a contract for employment or benefits, the worker is likely to be an independent contractor. Independent contractors may contract for more than one component of a project without triggering COI concerns.

See examples Part IV.

E. What are the steps to determine whether a procurement conflict of interest has occurred or may occur?

1. Is the selection of the contractor for the procurement of goods, supplies, equipment, construction, or services? If no, evaluate whether non-procurement COI applies (see Non-Procurement COI below).
2. Who is involved with the award, selection, or administration of the TxCDBG grant?
  - a. Are they considered an employee, officer, or agent of the Grant Recipient? If the person is considered an employee, officer, or agent, continue with question 3.

For instance, since a grant administrator coordinates the TxCDBG project including engineering, the grant administrator cannot have a partner or ownership or immediate family member associated with the engineering firm that will be awarded the contract.

- b. If not considered an employee, officer, or agent, then there is no conflict of interest. Proceed to question 4 regarding competition requirements.
3. Will the employee, officer, or agent, or any of their business or familial relations receive a financial or personal gain if the firm is selected for an award of the TxCDBG contract?
  - a. If yes, then a conflict of interest violation will occur and costs will be disallowed if the contract is awarded.
  - b. If no, go to Question 4
4. Did the firm being considered for a contract help “develop or draft specifications, requirements, statements of work, or invitations for bids or requests for proposals”?
  - a. If no, then competition has been free and open and no conflict has occurred.
  - b. If yes, the firm is excluded from competing for such procurement.

F. If there is a conflict of interest, can the community ask for an exception?

No, federal policy does not allow for exceptions for procurement COI.

G. Besides preventing conflict of interest, what is also required of our Grant Recipients regarding their own procurement policies and conflict of interest?

All grant recipients must maintain written standards of conduct covering conflicts of interest governing the actions of its employees engaged in the selection, award and administration of contracts.

### **III. Non-Procurement COI (24 CFR 570.489(h))**

A. To what types of activities does non-procurement COI apply?

Non-procurement COI occurs in those situations not associated with the purchase of goods and services. For instance, non-procurement COI might occur in such activities as real estate acquisition, provision of assistance with CDBG funds to individuals, businesses, etc.

B. What is the regulation governing non-procurement conflict of interest?

1. Any person who is an employee, agent, consultant, officer or elected or appointed official of a recipient or subrecipient who:
  - Exercises any functions or responsibility with respect to CDBG activities
  - Is in a position to participate in the decision making process
  - Or gains inside information with regard to such activities...
2. Is prohibited from:
  - Obtaining a financial interest or benefit from a CDBG activity
  - Having a financial interest in any contract with respect to a CDBG activity or its proceeds, either for themselves or those with whom they have business or immediate family ties;

- During their tenure or for one year thereafter.

What does this mean?

Similar to procurement conflict of interest, this means those employees, agents, consultants, officers, or elected/appointed officials (or anyone in whom they have business or immediate family ties) – basically any people who have inside information regarding a CDBG project – may not obtain a financial interest or benefit from a CDBG project.

C. Can a Grant Recipient request an exception from TDA for non-procurement COI?

Yes, a Grant Recipient can request an exception from TDA. Exceptions may be granted on a case-by-case basis for non-procurement COI using the process outlined below.

1. Determine that there is a potential for a COI if an action is taken;
2. Publicly disclose the nature of the conflict and schedule a public hearing.
  - Just giving notice at a general city council/commissioner's court meeting without a published agenda item on the topic is not sufficient. Best practice is to give public notice and schedule a public hearing to specifically discuss the potential COI.
3. Discuss with the Grant Recipient's attorney and receive an opinion that the conflict will not violate State or local law.
4. Request an exception from TDA.
  - Submit documentation of the conflict and how the conflict was publicly disclosed;
  - Submit the attorney's opinion letter;
  - Either the attorney's letter or a letter from the Grant Recipient must evaluate each ground for allowing an exception (See factors for allowing an exception described in E. below);
  - TDA will make a determination whether the exception will serve to further the purposes of the CDBG program after considering the cumulative effect of all factors.

D. What if the COI occurred before it was disclosed to the public?

If the COI was not publicly disclosed and a conflict of interest has occurred, no exception may be granted after the fact. Costs may be disallowed.

E. What factors are considered in determining whether to grant an exception?

1. Allowing the exception would provide a significant cost benefit or essential expertise to the project;
2. An opportunity was provided for open competitive bidding or negotiation;
3. The person affected is a member of a group of low or moderate income persons and the exception will allow such person to receive the same interests as the group;
4. The person affected has withdrawn from his or her functions or responsibilities, or the decision making process with respect to the assisted activity;
5. Was the interest or benefit present before the affected person was in the "conflicting" position;
6. Undue hardship to recipient or person affected when weighed against public interest served by avoiding the prohibited conflict;
7. Any other relevant considerations.

#### IV. COI Examples

##### **Example 1:**

County X sought a contractor to complete some drainage improvements by sealed competitive bids.

- The project will be funded with CDBG funds.
- ABC Corp. is the engineering firm which will administer the project.
- XYZ Constructors, Inc. was the low bidder for the job and has been selected for the award of this contract.

The principals of both the engineering firm and the construction company are brothers-in-law.

Q: Can County X award the contract to XYZ Constructors, Inc.?

A. No. This is a “procurement of construction services” by County X covered by *2 CFR § 200.318*.

It is a conflict of interest for an agent (ABC Corp.) of the grantee to administer a contract supported by federal funds if a member of his “immediate family” has a financial interest in the company selected for the award (XYZ Constructors).

Accordingly, it would be a conflict of interest for ABC Corp. to administer a construction contract funded with CDBG money, since the principle’s brother-in-law is the principle of XYZ Constructors, Inc.

Q. Can the County be granted an exception?

A. No, no exceptions are allowed for procurement COI.

##### **Example 2:**

Texas Water WSC, a water supply corporation, has a contract with the vendor, Water Works, Inc. to operate its water treatment plant. Several years into the contract, the water treatment plant is in need of repairs and the City of Drought, Texas on behalf of the water supply corporation applies for TxCDBG funding to repair the plant.

Q: Can Water Works, Inc. bid for this construction contract without violating conflict of interest or competition regulations or should such action be disallowed?

A. It depends. Under this fact scenario, Water Works, Inc. is operating as an independent contractor to the WSC and not as an agent. Therefore, under first part of the procurement conflict of interest analysis, Water Works, Inc. can compete for this construction contract. However, if Water Works, Inc. assists in the preparation of the application for TxCDBG funding in any manner such as providing specifications for the repair, Water Works, Inc. is prohibited from competing for this contract.

### **Example 3:**

The City of Agrarian applied for economic development funding under TDA's Texas Capital Fund (TCF) as part of an economic incentive package used to attract a new manufacturing business to this rural community. When the business moves to Agrarian, they will be adding a large manufacturing facility as well as remodeling the current building site. The funds from TDA will be used to upgrade the road leading to the plant. Using private funding, the company has hired an engineer to oversee the building of the new manufacturing facility.

Q: Can the engineer of the facility then compete for the design of the road?

A: This scenario involves the procurement of services therefore, procurement COI analysis. With economic development projects (those that use Texas Capital Fund funding), the benefitting business is considered a subrecipient to the City of Agrarian. Since the engineer is acting as the agent of the company (subrecipient of funding) when overseeing this economic development project as well as gaining insider information, the same engineer cannot be selected to design the construction of the road.

### **Example 4:**

Mr. Smith was employed by County X as its grant administrator. Mr. Smith over a 4 year period also formed a company and was its executive director. Mr. Smith awarded several CDBG contracts to this company. He collected a salary from the county as a grant administrator and also collected a salary as the executive director of his company, which was paid using CDBG funds.

Q: Did Mr. Smith violate conflict of interest regulations?

A: Yes. In fact, the fact scenario above was an actual case investigated by the U.S. Office of Inspector General. In that case, the defendant, a former CDBG grant administrator, was sentenced to 36 months' probation and ordered to pay restitution to HUD in the amount of \$116,064.

### **Example 5:**

The City of Bluebonnet plans to apply for CDBG funds to reconstruct Oak Street. The Mayor of Bluebonnet owns two rental homes located in the project area.

Q: Is this a conflict of interest?

A: Yes. The Mayor will benefit from the CDBG-funded improvements, therefore a conflict exists between the public duties of the Mayor and her private interest in her properties. Because the conflict is based on benefit as a property owner and not on a purchasing or contracting opportunity, this is considered a non-procurement conflict of interest.

Q: May CDBG funds be used for this project?

A: The City may request that TDA grant an exception to the prohibition on conflict of interest, based on the best interest of the community. Such an exception may be granted for non-procurement conflicts.

The city should complete the exception request as described in Part III above prior to taking any action on the project.