

Office of Government Ethics

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Letter to a Designated Agency Ethics Official dated June 2, 1992

This responds to your request for an informal opinion concerning an application of 5 U.S.C. app. § 502 and its implementing regulation at 5 C.F.R. part 2636 (56 Fed. Reg. 1721-1730, Jan. 17, 1991). You have asked whether [an employee] [of your agency] may continue to receive income from the [particular health care] practice he established prior to becoming a Government official. [The agency does not deal with health care issues].

As I understand the facts as you have described them, upon joining the Department in 1988 as a noncareer member of the Senior Executive Service, [the employee] transferred the operation of his practice to another [practitioner in his field] pursuant to a renewable one-year contract. The contract stipulates that [the employee] would "employ" the [practitioner], whose duties involve providing "professional [health care] services to [the employee's] patients." [The employee] retained the right to control, direct and supervise the duties of the [practitioner] he hired. All patients remained [the employee's] "patients of record," and [the employee] retained the right to approve his employee's time of vacation. In return, [the employee] agreed to provide an office, supplies, equipment, and other appropriate facilities and services. The contract states that the [practitioner] hired by [the employee] will receive 35% of the practice's adjusted gross receipts or \$20 per hour, whichever is greater.

In 1991, [the employee] entered a second contract with a different [practitioner] to provide services to his patients as manager of his practice. This contract also requires [the employee] to provide an office, supplies, equipment, staff support and other such appropriate facilities and services. In this case, the [practitioner] will be paid \$600 per week or 30% of the adjusted gross income of the practice, whichever is greater. The contract states that all patients treated at [the employee's] office are considered to be [the employee's] patients. Additionally, the contract permits [the employee] to provide services to his patients directly, provided that his income does "not exceed such amount as may be permitted by 5 C.F.R. 2634.501(b)."

5 U.S.C. app. § 502[a] prohibits a covered noncareer employee from receiving compensation for (1) practicing a profession that involves a fiduciary relationship or (2) affiliating with or being employed to perform professional duties by an entity which provides professional services involving a fiduciary relationship. The provision further prohibits a covered noncareer employee from permitting the use of his name by such an entity.

In this case, there is no disagreement that [the employee] is a covered noncareer employee within the meaning of the statute and that [his type of health care services] is a profession which involves a fiduciary relationship. In your view, the issue to be decided is whether the income received by [the employee] for services provided by the [practitioners] he hired is "compensation" as [that term is used in] section 502(a)(1). You suggest that, in [the employee's] case, the income he receives is essentially a return on his investment in the physical assets of his practice and is not "compensation" as [used] in 5 U.S.C. app. § 502 or [as defined in] its implementing regulation.

The term "compensation" is defined in the prohibition's implementing regulation to include "wages, salaries, honoraria, commissions, professional fees and any other form of compensation for services" other than salary and benefits paid by the United States. 5 C.F.R. § 2636.303(b). Specifically excluded from the definition is "income from investment activities where the individual services are not a material factor in the production of income" as well as "actual and necessary expenses incurred by the employee in connection with an outside activity." *Id.* at §§ 2636.303(b)(4) and (6). Compensation for services rendered in satisfaction of a contractual obligation entered prior to January 1, 1991, is also not considered "compensation" within the meaning of the regulation.

The regulation makes clear that the prohibition on receipt of compensation applies not only in cases where the employee is providing professional services, but also where he is affiliated with an entity that provides professional services involving a fiduciary relationship. *Id.* at § 2636.305(a)(1)(ii). In the latter case, the prohibition is not merely on being affiliated with such an entity, but is on receiving compensation for the affiliation. Where an employee is compensated by an entity because of his affiliation with the entity, he has received "compensation" for his services, i.e., his affiliation.

Moreover, the regulation clearly indicates that a covered employee may not allow the use of his name by any entity that provides professional services involving a fiduciary relationship, whether or not the employee receives compensation for permitting the use of his name. *Id.* at § 2636.305(a)(2). Thus, a covered employee could not permit someone to simply manage or operate a profession involving a fiduciary relationship on the employee's behalf, while retaining the employee's name as a business identifier.

I am not persuaded that the facts in this case establish that [the employee's] contractual arrangements concerning the operation of his practice amount to creation of an "investment" interest and that the compensation he received was a return on his investment in the physical assets of his practice. Both contracts demonstrate that [the employee] hired someone to conduct the practice on his behalf and that he retained full control over the operation of the practice, including such routine matters as the time and place his employee was required to provide the services, the length of his vacations, and the type and amount of supplies and equipment to be ordered. Both contracts indicate that all patients remained [the employee's] patients of record and that all relevant documents and records belonged to [the employee]. The second contract also specified that his [practitioner's] malpractice insurance must designate [the employee] as an additional named insured.

Because [the employee] continued personally and directly to control the operation of his practice while he was a covered noncareer employee, it is difficult to conclude that he was not "affiliated" with an entity providing professional services involving a fiduciary relationship. Moreover, the fact that he received money for the provision of these services and simply paid his employee an established percentage or salary compels the conclusion that he received "compensation" for his affiliation with the practice. On the other hand, there is no indication that the [practitioners] hired by [the employee] were merely leasing his office and equipment or that fees involved in this arrangement were based on an estimate of the fair market value of the lease of [the employee's] facilities and equipment, as you have suggested.

Additionally, although nothing in the materials you have provided demonstrates conclusively that [the employee] permitted the use of his name by the practice, it appears that he took no steps to see that his name was not used. I recommend that you

inquire further whether the [practitioners] he hired did, in fact, provide services under his name.

In this connection, both [the employee] and you on his behalf have argued that the statute at 5 U.S.C. app. § 502(a)(2) and the regulation at 5 C.F.R. § 2636.305(a)(2) force employees who provide professional services on a pro bono basis to violate state licensing procedures and professional ethics codes requiring that professional services be provided under the provider's individual name. In the absence of further information or evidence that there is any such licensing procedure or ethics code that applies to [the employee], I see no reason to address that argument. Also, I note that in your memorandum dated May 11, 1992, you cite the ABA Model Code of Professional Responsibility, Ethical Canon 2-11, as an example of a relevant code of professional ethics. However, in 1983, that Code was replaced by the Model Rules of Professional Conduct. I can find nothing in the Model Rules, and in particular in Rules 7.1-7.5 concerning Information About Legal Services, which is inconsistent with the requirements of the statute or the regulation. In fact, Rule 7.5(c) states that "the name of a lawyer holding a public office shall not be used in the name of a law firm, or in communications on its behalf, during any substantial period in which the lawyer is not actively and regularly practicing with the firm." ABA Model Rules of Professional Conduct Rule 7.5 (c)(1983).

[The employee] has also stated that any compensation for professional services he has received after January 1, 1991, is less than the actual and necessary expenses incurred by him in connection with his practice in 1991. While it is not entirely clear whether [the employee] is referring to compensation he received for services personally provided by him or compensation for affiliation with the practice, in either case the question of whether his compensation exceeded his expenses is a factual one to be determined after appropriate investigation.

The restrictions of 5 U.S.C. app. § 502 became effective on January 1, 1991, the day the implementing regulation was published. As the rule makes clear, the restrictions do not apply to compensation for services rendered before that date or those rendered in satisfaction of an obligation under a contract entered prior to January 1, 1992. Therefore, there is no restriction on the receipt of compensation by [the employee] pursuant to the terms of the contract dated July 12, 1988, during the one-year contract renewal period which presumably began on July 12, 1990. However,

receipt of compensation pursuant to any new contract or other contract renewal after January 1, 1991, would be prohibited. The appropriate penalties for violations are described in 5 C.F.R. § 2636.104. Unless [the employee] acted in good faith reliance on an advisory opinion properly issued under 5 U.S.C. § 2635.103, activities in which he engaged which are inconsistent with the statute and regulation should be referred to the Department of Justice for appropriate civil action.

Sincerely,

Stephen D. Potts
Director