



1400 K Street, Suite 400 • Sacramento, California 95814
Phone: 916.658.8200 Fax: 916.658.8240
www.cacities.org

TO: L. Allen Songstadt
Robert Ming
Doug Chotkevys
Bob Dunek
Lacy Kelly

FROM: Chris McKenzie, Executive Director

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SUBJECT: Response to Questions About the State League, Orange County Division
and Proposed Association of California Cities—Orange County

This memo answers the questions you raised with Jim Ridenour, League President, and me on October 8 about the relationship that could possibly be established between the state League/Orange County Division and the proposed new Association of Cities – Orange County. These responses represent my best efforts to answer the questions without having discussed them with the League board of directors which has final discretion over these matters. In my judgment, the board will be reluctant to take any steps that would potentially weaken the state League at a time when it has just achieved perhaps its most significant local control victory since its founding in 1898—the passage of Proposition 22 by a 61% - 39% margin.

I think it is important to remember that while the divisions and the state League have very intertwined and complimentary purposes, the divisions exist to build a stronger, more representative, and more effective state League—not the other way around. The purpose of the new association seems more about building a stronger county-based organization to deal with county and some statewide issues—sometimes even in competition with the state League. This will inevitably be viewed by some as a threat to enhancing the state League’s effectiveness in the years to come. Our members, the governor and the state legislature expect the state League to be the place where consensus on city policy is built. Having separate organizations with different positions undermines that goal.

With that in mind, here are the answers to the questions we discussed. We are preparing a similar communication to all cities in the county.

1. May the New Association Serve as the Orange County Division? No, it may not since the Division is legally part of the state League and operates under the bylaws of the state League. The officers and directors of the new association, however, may serve

concurrently as the officers and directors of the Orange County Division if they come from cities that are members of both the state League and the new association. The officers would act in two separate fiduciary capacities, however, and would have to hold legally separate meetings. The meetings could be held consecutively in the same location, with one meeting being adjourned before the next is called to order, but only members of the state League could participate in the Division meetings.

2. Can the State League Contract With the New Association to Provide the Same Services It Provides to the Orange County Division?¹ Yes, in theory the state League board could agree to provide such services under contract for a fee. It currently has such a contract to provide staff services to the Institute for Local Government (ILG), a separate non-profit 501 (c) (3) eligible research arm of the League and CSAC. Whether the state League board would agree to such a contract would be a matter completely within the sole discretion of the state League board. Unlike the ILG, the new association would potentially have policy goals that are at odds with the state League (i.e., this is one of the purposes of the new association—to allow for the adoption of policy positions at odds with the state League).

3. Can the State League Contract With the New Association to Provide Services to the Orange County Division? Yes, the state League could enter into such a contract, but it would be a matter completely within the discretion of the state League board. The services provided to the state League/Division, however, could only be for the exclusive benefit of cities in Orange County that are members of the state League. The state League board would likely consider that the new association would potentially have policy goals that are at odds with the state League (i.e., this is one of the purposes of the new association—to allow for the adoption of policy positions at odds with the state League).

4. Is it Possible for Cities to Be Division Members Only? No. Under the state League bylaws, membership in the Division requires membership in the state League. Cities that are not members of the state League and the Division could not participate as voting members in Division programs and activities, such as voting on Division positions and resolutions on matters, serving as a Division officer, serving on a state League or Division policy committee, etc. With the approval of the state League board, however, cities could make payments to the Division as “sponsors” or “supporters” comparable to private corporate sponsors and could receive limited non-voting benefits such as attendance at Division events and meetings. Whether the state League board would be willing to consider such a status would be entirely within its discretion. I anticipate it would have serious concerns about creating a precedent in other areas of the state.

¹ Since 1996 the League has administered payroll for the Division. While the Division board of directors makes all financial decisions, in 2005 the state League also began to provide accounting services for which it is reimbursed. Since 2006 the state League has provided legal services, human resources services, officers' and directors' liability insurance, and general administrative support without cost to the Division and the cities of the county. All employees of the Division are state League employees, but the cost of their services is borne by the members of the Orange County Division of the state League.

5. Is it Possible for the New Association to Become a Chapter or Affiliate of the State League? Unlike some other organizations, the state League does not have chapters under its bylaws. To do so would require an amendment to the bylaws; this could not be effective until January 1, 2012. The League's affiliate status is typically reserved for statewide associations serving city officials, such as the California Redevelopment Association, but the new association could request affiliate status.

6. What Other Factors Should Be Considered About the New Association? The organizers and cities of Orange County should consider a number of factors in moving forward with the new organization, including:

- Compliance Oversight. If there is no contract with the state League to provide accounting and other oversight, what safeguards will exist to ensure compliance with all state and federal laws and best accounting practices?
- Liability. If the association sustains a financial or legal loss, will city members be responsible for paying any of the cost associated with that loss? What insurance coverages will be secured?
- Purpose of Association. If the association can't lobby, what advocacy purpose does it serve?
- Audit and Accounting. Will the association follow generally accepted accounting principles for nonprofit associations and have an annual audit?
- Staffing. Will the new association be able to attract and manage competent staff and offer a competitive compensation package?
- Continuity. Is it possible to sustain the association beyond its first year or two of existence?
- Duplication of Services. Will the new association duplicate any services provided by the Division or the state League?
- Are Their Other Options? The new association is being considered due to concern about the loss of cities in the membership of the state League/Division and a desire to adopt positions at odds with the state League. Are their other options, such as reducing dues or increasing dues on the remaining cities that would allow maintenance of services at the Division until cities return to membership?
- Policy Influence. Will the new association give Orange County cities a stronger or weaker voice in state policy matters?
- Impact on the State League. Will the formation of the new association discourage membership in the state League by Orange County cities, weakening the impact of the state League's efforts to "restore and protect local control for cities," the mission of the state League.

I trust this addresses the issues we discussed on October 8. Please let me know if you have any further questions.

c. League Executive Committee

Questions Answered About AOCC-OC

Compliance Oversight. If there is no contract with the state League to provide accounting and other oversight, what safeguards will exist to ensure compliance with all state and federal laws and best accounting practices?

The AOCC-OC will contract with a Certified Public Accountant that specializes in 501(c)3 nonprofits. This is a common practice among nonprofits, and should not cost the organization much more than it pays now, given the relatively small operating budget. The AOCC-OC will also conduct audits in compliance with IRS tax-exempt requirements. This is a new expense that the AOCC-OC expects to bear, but it is not cost prohibitive.

In addition, under the Division structure, the League does not permit access to full financial reports to anyone but internal “management.” The Board merely receives income and expense schedules. Under AOCC-OC, as is common and best practice for all 501(c)3 organizations, the Board will have receive full Profit & Loss, Balance Sheet, and Income and Expense Reports, for review and approval from a Certified Public Accountant.

• **Liability. If the association sustains a financial or legal loss, will city members be responsible for paying any of the cost associated with that loss? What insurance coverages will be secured?**

The association will be a separate nonprofit corporation that will provide liability protection for its members and will follow industry standard corporate formalities which prevent courts from looking through the corporation structure and applying liability to its members. Best Practices for nonprofits includes the securing of Liability and Directors and Officers Insurance. The AOCC-OC, like all reputable nonprofits, will secure these insurance policies to protect its Board, staff and members. This is a new expense that AOCC-OC expects to bear, but it is not cost prohibitive.

• **Purpose of Association. If the association can't lobby, what advocacy purpose does it serve?**

501(c)3 nonprofits are permitted to engage in advocacy activities at up to 20% of their budget and resources. The current organization does not approach that level of time and resource commitment. Since the AOCC-OC services are designed to replicate services previously offered under the Division structure, the AOCC-OC will not be in danger of extended beyond that limited amount. If it desires to become more active, the AOCC-OC will poll its members to investigate forming a PAC or other options.

- **Audit and Accounting.** Will the association follow generally accepted accounting principles for nonprofit associations and have an annual audit?

All nonprofits, particularly 501 category nonprofits, are required to follow GAAP (Generally Accepted Accounting Principles). Certified Public Accountants that specialize in 501 category nonprofits ensure that GAAP is followed. At this time, an audit is required once every two years. The AOCC-OC will comply with this best practice.

- **Staffing.** Will the new association be able to attract and manage competent staff and offer a competitive compensation package?

The Board of the Division has made it clear to Division staff that should they be able to reach critical mass to move to the AOCC-OC structure, they would like the current Division staff to move over to the new organization with a competitive compensation package.

- **Continuity.** Is it possible to sustain the association beyond its first year or two of existence?

The AOCC-OC is more sustainable than the Division structure for three reasons.

1- The current Division structure has been proven unsustainable due to the requirement for cities to pay two sets of dues. For those cities that have dropped membership for this reason and are only interested in local services, the AOCC-OC structure is more sustainable than the current Division structure which requires payment of both sets of dues.

2- The local organization has, in the last 3.5 years, provided a host of "Value Added Services." The AOCC-OC will continue to provide these and new value added services, and will remain "member-centric," polling its member base to determine what services are needed and wanted. This will further increase sustainability.

3- Lastly, the new 501(c)3 structure allows the AOCC-OC to pursue grants and tax-deductible donations, further increasing financial sustainability.

- **Duplication of Services.** Will the new association duplicate any services provided by the Division or the state League?

No. The Division does not duplicate services of the League now, but compliments them. The AOCC-OC will continue to provide the same and expanded local services that add value to Orange County cities. See the attached "Value Added Performance of the Division," for information on value added services that do not duplicate state League benefits.

- **Are Their Other Options?** The new association is being considered due to concern about the loss of cities in the membership of the state League/Division and a desire to adopt positions at odds with the state League. Are there other options, such as reducing dues or increasing dues on the remaining cities that would allow maintenance of services at the Division until cities return to membership?

The Division Board has explored allowing some cities to pay less dues. The Board sees this as unfair to the full dues paying members and believes it sets a precedent that will ultimately undermine the sustainability of the organization. Regarding dues increases, Orange County cities have sent the clear message that they cannot and will not support a dues increase. The best option is to open the organizations funding base options, which is part of the benefit of moving to AOCC-OC. As mentioned previously, the Board expects new grants and sponsorships that become possible once the organizational structure is changed to a traditional 501(c)3.

- **Policy Influence.** Will the new association give Orange County cities a stronger or weaker voice in state policy matters?

On state policy matters, the AOCC-OC will give Orange County cities a stronger voice. On matters where the AOCC-OC and the State League agree, the AOCC-OC will add its name to the list of organizations supporting the State League, thereby increasing the voice of Orange County cities on state policy matters. Membership in the new association does not prevent members from also being members in the State League so many members will continue to be counted in State League number when determining State League influence. On matters where the AOCC-OC and the State League disagree, Orange County cities will have the ability to offer different approaches and ideas to state policy matters that may shape the discussion in ways that are more aligned with Orange County city interests. This option will no longer be available if the State League becomes a more traditional 501 nonprofit.

On local matters, the Division has had a strong voice and impact on Orange County issues and the Board expects this impact to be enhanced by moving to the new structure. The AOCC-OC will be viewed as speaking for Orange County cities because it is less influenced by positions taken by the State League, and because it is expected that the AOCC-OC will be able to bring back cities that have dropped the State League. This more unified voice will help the AOCC-OC have greater influence with the county and other local partnering agencies and nonprofits in Orange County.

- **Impact on the State League.** Will the formation of the new association discourage membership in the state League by Orange County cities, weakening the impact of the state League's efforts to "restore and protect local control for cities," the mission of the state League.

No. The OC Division has lost 1/3 of its members. These members have been lost to the League as well, and represent the largest cluster of dropped members of any Division in the state League. The AOCC-OC will have the same mission as the League - "To Restore and Protect Local Control," and when the two organizations align, the League potentially gets more Orange County cities to back up its voice under the AOCC-OC structure.

- **Cost to Operate Independently. Will it cost the AOCC-OC substantially more to maintain an independent 501(c)3 organization?**

No. While the AOCC-OC will incur some new costs necessary to operate in a professional and fiduciary manner, there are also a number of costs savings that will reduce expense in some areas. The new structure will also provide the AOCC-OC with greater transparency on expenses from functions currently handled by the State League and the ability to collaborate with Orange County partners to reduce those costs. Therefore, the new expenses will not be significant in the overall budget, and can be offset by the new funding opportunities created by the separate, 501(c)3 status.