A QUICK LOOK INTO IMPORTANT ISSUES OF THE DAY

BY NICHOLAS BIRDSONG

Conflict of interest laws prohibit public officials and employees from exercising authority that substantially and directly affects a personal financial interest. Despite variation in how states define conflicts of interest, all agree on the basic idea that legislators with a conflict should disclose the nature of the interest and recuse themselves from participating in the matter.

But how can a legislator work with sprawling business interests affected by equally sprawling legislation or when unforeseen conflicts could lurk around every corner? Experiences that qualify lawmakers to craft good policy may come from the private sector, but with experience often comes financial ties. Should ethics rules prohibit some of the most qualified experts from working in government?

Blind trusts potentially cure conflicts of interest by transferring assets into a financial instrument controlled by an independent trustee, who may sell or transfer interests without knowledge of the beneficiary. The beneficiary becomes “blind” to the impact of official actions on private interests held in trust, thereby creating a shield against conflicts of interest.

Did You Know?

- No state requires public officials to use a blind trust while serving, but 12 states define blind trusts, which officials can use to avoid conflicts of interest.
- Expertise and occupations are typically considered when making legislative committee assignments, but this may increase the risk of conflicts of interest.
- Trusts aren’t just for ethics. Lottery winners may use one type of “blind trust” to stay anonymous.
Although 12 states define blind trust by statute or regulation, no state requires public officials to use a blind trust while serving. The laws and rules exist to provide a tool to protect public officials from a conflict of interest or the appearance of a conflict. If officials elect to place assets in a blind trust, they must follow requirements that vary substantially from state to state.

Some rules require trustees to be an institutional fiduciary like a bank. An official’s family members and business associates are often precluded from acting as trustee. However, some states specify no restrictions on who may manage a blind trust.

Definitions may require trust assets to be easily transferrable without the beneficiary’s knowledge. In Alaska, for example, a blind trust may not contain investments if their sale or transfer is public record or if the ownership interest is “with permanency that makes transfer improbable or impractical, including real estate, security interests in personal property, mortgages, and interests in closely held businesses.”

Communications between trustee and beneficiary may be limited to specified subject matters—such as when a public official needs assets from the trust or information relating to tax returns—and conducted only in writing. Most states prohibit beneficiaries from directing how funds may be invested, although some allow notifying a trustee that an asset placed in the trust should be sold to prevent a conflict.

While states may not define a blind trust, some have statutes or regulations that recognize their use in limiting required disclosures or shielding against conflicts of interest. Informal use of the federal definition (described below) is common.

More than half the states lack any statutory or regulatory mention of blind trusts. If using a blind trust shields an official from knowledge about its assets, however, it could still protect officials from disclosure or recusal requirements under certain ethics rules.

However, authoritative sources in two states otherwise silent on blind trusts disagreed. An advisory opinion from the Georgia secretary of state says assets would still need to be disclosed, regardless of whether they are held in a blind trust. In Ohio, an Ethics Commission advisory opinion said, “There is no provision in Ohio that recognizes or provides for the creation of ‘blind trusts.’ Consequently, the Ethics Law does not recognize a method by which blind trusts, and their assets, can be disclosed in a manner that is consistent with the purpose in creating a blind trust.”

Federal Action

The Ethics in Government Act of 1978 formalized the federal approach to blind trusts. Before that, the absence of statutory direction resulted in inconsistent or ineffective use of trusts.

Current law requires members of all branches of government to file financial reports within 30 days of assuming a federal position. Along with other required disclosures, filers must submit a copy of any blind trust instrument and a list of assets transferred to the trust. Assets placed in trust remain potential conflicts until the trustee notifies the beneficiary that an asset is removed or valued under $1,000.

Federal ethics law defines a “qualified blind trust” as a trust certified by an appropriate ethics authority in which a public official, public employee or family member has a beneficial interest. A qualified trustee must be an independent, disinterested and non-familial financial institution or other fiduciary. The trustee must have discretion in managing and controlling assets without notifying the beneficiary, free from sale or transfer restrictions unless approved by an appropriate ethics office.

Trustees and beneficiaries may communicate only in writing and as expressly permitted. Beneficiaries may request asset distributions, discuss general investment goals, notify trustees of subsequently applicable laws that prohibit holding certain assets, or request the sale of an initially placed asset that could create an apparent conflict. Trustees may communicate only to disclose summary trust information required for tax purposes or to notify the beneficiary when an asset initially transferred to the trust is disposed of or its value drops below $1,000.