

N.D.A.G. Letter to Bye (Dec. 24, 1987)

December 24, 1987

Mr. Kermit E. Bye
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Dear Mr. Bye:

Thank you for your letter of October 30, 1987, in which you request my opinion regarding whether the board of directors and officers of the Myron G. Nelson Fund, Inc. (MGN), may avail themselves of the provisions of the North Dakota Century Code that afford protection to state employees from civil litigation claims. In response to your question, I will discuss the applicability of N.D.C.C. § 26.1-21-10.1 (providing that the Attorney General shall defend employees of the state) and N.D.C.C. § 32-12.1-15(2) (limiting the liability of state employees).

N.D.C.C. § 26.1-21-10.1(2) states, in part, as follows:

2. The state of North Dakota shall defend any employee of the state in connection with any civil claim or demand, whether groundless or otherwise, arising out of an alleged act or omission occurring heretofore or hereafter during the employee's period of employment if the employee provides complete disclosure and cooperation in the defense of the claim or demand, and if the actions complained of were within the scope of the employee's employment.

N.D.C.C. § 26.1-21-10.1(1)(a) defines "employee of the state" as "all present or former officers or employees of the state or any of its agencies, departments, boards, or commissions, or persons acting on behalf of such agencies, departments, boards, or commissions in an official capacity, temporarily or permanently, with or without compensation. The term does not include an independent contractor."

N.D.C.C. § 32-12.1-15(2) states as follows:

2. No employee of the state may be held liable in the employee's personal capacity for actions or omissions occurring within the scope of the employee's employment unless such actions or omissions constitute reckless or grossly negligent conduct, malfeasance, or willful or wanton misconduct.

N.D.C.C. ch. 32-12.1 does not define "employee of the state." However, inasmuch as N.D.C.C. § 26.1-21-10.1(l)(a) (defining "employee of the state") and N.D.C.C.

§ 32-12.1-15(2) (which uses the term "employee of the state") both originated in House Bill No. 1446 in the 1987 Legislative Assembly, it is my opinion that the term "employee of the state" set forth in N.D.C.C. § 26.1-21-10.1(1)(a) is controlling for purposes of N.D.C.C. § 32-12.1-15(2). Thus, the dispositive issue in determining whether the directors and officers of MGN may avail themselves of the protections offered by N.D.C.C. §§ 26.1-21-10.1 and 32-12.1-15(2) is whether MGN is an agency, department, board, or commission of the state.

The language "agencies, departments, boards, or commissions" is obviously intended to include any entity that is, in actuality, the alter ego of the state regardless of the descriptive name attached to that entity. The issue of whether an entity associated with a state is, in actuality, the alter ego of the state has arisen in cases where the defendant entity attempts to avail itself of the protection against suit afforded states by the Eleventh Amendment of the U.S. Constitution. In Blake v. Kline, 612 F.2d 718, 722 (5th Cir. 1979), the Fifth Circuit adopted the following criteria in determining whether an agency, commission, or board which is related to the state should be regarded as the sovereign's alter ego for Eleventh Amendment purposes:

- [1] Local law and decisions defining the status and nature of the agency involved in its relation to the sovereign are factors to be considered, but only one of a number that are of significance. Among the others, no one of which is conclusive, perhaps the most important is [2] whether, in the event plaintiff prevails, the payment of the judgment will have to be made out of the state treasury; significant here also is whether the agency has the funds or the power to satisfy the judgment. Other relevant factors are [3] whether the agency is performing a governmental or proprietary function; [4] whether it has been separately incorporated; [5] the degree of autonomy over its operations; [6] whether it has the power to sue and be sued and to enter into contracts; [7] whether its property is immune from state taxation, and [8] whether the sovereign has immunized itself from responsibility for the agency's operations.

See also Ainsworth Aristocrat International Pty. v. Tourism Co., 818 F.2d 1034, 1037 (1st Cir. 1987); Hall v. Medical College of Ohio at Toledo, 742 F.2d 299, 302 (6th Cir. 1984).

I will discuss the Myron G. Nelson Fund within the framework of these eight factors to determine whether the corporation is, in fact, the alter ego of the state and, therefore, entitled to the statutory protections discussed above. Initially, I will discuss the statutory provisions defining the status and nature of the Myron G. Nelson Fund and its relationship with the state. This discussion will essentially address factors one, four, five, and six set forth above.

MGN is a corporation which derives its existence and authority from N.D.C.C. ch. 10-30.2. A review of N.D.C.C. ch. 10-30.2 indicates that MGN is generally designed to function

outside the political processes of state government. However, MGN is not entirely independent of state involvement.

Pursuant to N.D.C.C. § 10-30.2-02, the state's Industrial Commission appointed the initial incorporators of MGN. Upon fulfillment of this responsibility, however, the Industrial Commission is given no statutory authority over the corporation.

The powers of MGN are set forth in N.D.C.C. § 10-30.2-03. It is stated that "the corporation shall have the powers and privileges conferred upon domestic corporations under the business corporation act, to the extent not limited by this chapter." A review of N.D.C.C. ch. 10-30.2 indicates several nuances that could be considered limitations on the corporation. However, these nuances are extremely inconsequential to the substantive existence of the corporation and as a result, MGN will substantially function like any corporation organized under the North Dakota Business Corporation Act.

N.D.C.C. § 10-30.2-03 specifies additional powers of the corporation as follows:

1. Make contracts and execute all instruments necessary for the exercise of its powers and functions.
2. Coordinate and cooperate with state agencies and the state's political subdivisions, colleges, universities, and other academic and research sources, both private and public, agencies and organizations of the federal government, and all public or private entities.
3. Receive appropriations from the legislative assembly and other public moneys, as well as contributions from other public agencies, private individuals, companies, and other contributors.
4. Review cooperative funding agreements with federal and state loan and grant programs and commercially funded projects.
5. Administer an industrial development revenue bond guarantee program as provided in chapter 6-09.2.

These enumerated powers obviously create the potential for substantial interplay between state agencies and institutions and the corporation. Even so, the corporation is clearly independent and autonomous from any existing state agency.

It must also be noted that N.D.C.C. § 10-30.2-05 provides that there must be representation on the corporation's board of directors from the Economic Development Commission (a state agency), investors, and the business sectors of the North Dakota economy. This section further provides that "the business sector and investors must constitute a majority of the board."

The other area where there exists state involvement concerns the capitalization of the corporation.

10-30.2-04. CAPITALIZATION--PAYMENT OF DIVIDENDS. The funds deposited in the industrial development revenue bond fund pursuant to former section 6-09.2-06 and all accumulated earnings from the investment of the fund must be used by the Bank of North Dakota to purchase shares of the corporation upon the issuance of the certificate of incorporation. Beginning on July 1, 1987, the Bank of North Dakota may purchase annually shares of the corporation in an amount to be determined by the industrial commission. In determining the annual investment to be made in the corporation by the Bank of North Dakota, the industrial commission shall consider the level of private investment in the corporation, and attempt to match the private investment on a dollar-for-dollar basis. The corporation may issue shares to other public and private entities or persons when authorized by the board of directors.

Depending on the number of shares owned, the Bank of North Dakota may or may not be able to control the policies and operations of the corporation.

The above discussion of the status and nature of the Myron G. Nelson Fund and its relationship with the state can be summarized by several conclusory statements. First, MGN is a creature of the Legislature. Although MGN will generally function like any other corporation formed under North Dakota law, it is subject to several minor limitations. Second, the Bank of North Dakota will invest public funds to capitalize the corporation and, as a result, may be able to exert control over MGN by virtue of its shareholder status. Third, the Economic Development Commission will be represented on the corporation's board of directors. Fourth, there is the possibility of substantial interplay between MGN and other state entities. Fifth, MGN remains subject to future legislative enactments, including legislative appropriations to the corporation, that may increase or decrease the level of state involvement with the corporation. Finally, MGN is clearly autonomous and independent from any existing state entity.

The second factor set forth above is whether any judgment in favor of a plaintiff will have to be paid from the state treasury. This is closely interrelated with the eighth factor and, accordingly, I will consolidate my discussion of these points. N.D.C.C. § 10-30.2-14 provides that "the state of North Dakota is not liable for any damage incurred by an investor in the corporation." Although this declaration of immunity is limited to one particular cause of action, it is consistent with the general theme of N.D.C.C. ch. 10-30.2 that the corporation is a distinct and independent corporate body. This declaration of state immunity suggests that MGN is not an alter ego of the state.

The third factor set forth above is whether MGN will be performing a proprietary or governmental function. A finding that an entity performs governmental functions is indicative that the body is merely an arm of the state. Governmental functions are those that have been customarily performed by governments for the purpose of governing its

people. See Illinois Trust and Savings Bank v. City of Arkansas City, 76 F. 271, 282 (8th Cir. 1896). On the other hand, proprietary functions generally further some commercial purpose for the benefit of the public but do not constitute traditional governmental functions. *Id.* Although MGN might engage in some economic development activities that could be classified as governmental functions, it primarily acts in a proprietary capacity for the benefit of its shareholders. The corporation's primarily proprietary nature indicates that it is not an alter ego of the state.

Finally, I will discuss the seventh factor relative to the taxable status of MGN. There is no indication anywhere in the North Dakota Century Code that MGN is immune from taxation -- property or income. Indeed, N.D.C.C. § 10-30.1-05 provides that MGN can make investments in venture capital corporations created under chapter 10-30.1, but that MGN is not entitled to any credits against its income tax for any such investments. Evidently, the Legislature intended that MGN is to be a taxpaying corporation. As a result, it is my opinion that consideration of this factor preponderates in favor of a finding that MGN is not acting as an alter ego of the state.

Having said all this, it is apparent that there are several countervailing considerations that could lead to differing conclusions. However, I believe the better argument is that MGN is not an alter ego of the state and, therefore, is not entitled to the statutory and constitutional protections against civil litigation afforded the state and its employees. The overriding consideration supporting my opinion is the independence and autonomy of MGN. MGN is responsible to its shareholders, not the state of North Dakota. I do not consider the Bank of North Dakota's investment in the corporation, made in its proprietary capacity, as affecting MGN's autonomy. In addition to its independence from the state, the remaining factors discussed above support the conclusion that MGN does not function as the alter ego of the state.

In summary, it is my opinion that the term "employee of the state" as used in N.D.C.C. § 26.1-21-10.1 and N.D.C.C. § 32-12.1-15 would not include directors and officers of the Myron G. Nelson Fund, Inc. Therefore, I would suggest that the directors of the corporation explore the possibility of obtaining adequate liability insurance.

Sincerely,

Nicholas J. Spaeth

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