IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT, DIVISION EIGHT

JAMES D. MCGEE, Plaintiff and Appellant, v. **TORRANCE UNIFIED SCHOOL DISTRICT, and BARNHART-BALFOUR BEATTY, INC., dba BALFOUR BEATTY CONSTRUCTION, *et al.*,** Defendants and Respondents,	Court of Appeal No. B252570 (Super. Ct. No. YC068686)

Appeal From a Judgment
Of The Superior Court, County of Los Angeles
Hon. Stuart M. Rice, Judge

APPELLANT'S SUPPLEMENTAL REPLY BRIEF

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APPELLANT'S SUPPLEMENTAL REPLY BRIEF

Pursuant to the Court's Order dated October 21, 2014 Appellant James D. McGee (Taxpayer or Appellant) respectfully submits this Supplemental Reply Brief in reply to the Supplemental Briefs of Respondents Torrance Unified School District (District) and Barnhart-Balfour Beatty, Inc., dba Balfour Beatty Construction (Contractor). District and Contractor are collectively referred to herein as Respondents. Because Respondents' supplemental briefs are substantively identical in argument and content Taxpayer's Supplemental Reply Brief will primarily cite to District's Supplemental Brief as RSB. [1]

I. ARGUMENT

A. Respondents Incorrectly Assert the *Howard* Decision Disposes of All Legal Issues and Causes of Action Raised in Taxpayer's Pleadings

Respondents incorrectly assert "[t]his case is on all fours with the *Howard* decision and simply retreads the same issues that were already decided by the Fourth Appellate District" in *Los Alamitos Unified School District v. Howard Contracting, Inc.* (2014) 229 Cal.App.4th 1222, 178 Cal.Rptr.3d 355 ("*Howard*"). (RSB p. 1.) Respondents erroneously urge this Court "should follow *Howard* and affirm the trial court's judgment in full." (RSB p.2.)

Respondents fail to acknowledge the trial court's judgment here related to legal issues and causes of action raised in Taxpayer's pleadings which were never addressed by the *Howard* Court. The only similarity of issues between

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[1] Other terms not defined herein have the same definition as in Appellant's Opening Brief.

Howard and this case is whether Education Code section 17417 applies and requires competitive bidding of the leaseback contract. [2] The *Howard* Court did not consider the following issues raised in Taxpayer's First Amended Complaint (FAC) which is the subject of this Appeal:

First Cause of Action: the Lease-Leaseback Contracts at issue in this action are sham leases en tered into as a subterfuge to claim the right to undertake school construction in the manner authorized by Education Code sections 17400-17429. (Volume 1 of Appellant's Appendix, page 7, paragraph 20 through page 9, paragraph 26 (designated "1 AA 7:¶20-9:¶26").) Taxpayer's Opening Brief and Reply Brief provide sufficient authority for this Court over rule the trial court's sustaining of Respondents' demurrers to this cause of action.

Second Cause of Action: District's Board of Education breached the fiduciary duty imposed upon them by their position, oath of office, and/or applicable California law. (1 AA 9:¶27-10:¶31.) Taxpayer's Opening Brief and Reply Brief provide sufficient authority for this Court over rule the trial court's sustaining of Respondents' demurrers to this cause of action.

Fourth Cause of Action: Government Code section 1090 and/or common law conflict of interest principals preclude Contractor from being awarded the Lease-Leaseback Contracts. This conflict of interest arose from Contractor's prior professional consulting contract with District involving the Project which is the subject of the Lease-Leaseback Contracts. (1 AA 16:¶42-17:¶47.) Taxpayer's Opening Brief and Reply Brief provide sufficient authority for this Court over rule the trial court's sustaining of Respondents' demurrers to this cause of action.

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[2] All references are to the Education Code unless otherwise specified.

Fifth Cause of Action: the Lease-Leaseback Contracts at issue in this action do not constitute a genuine financing arrangement as required by Education Code sections 17400-17429. (1 AA 17:¶48-18:¶51.) Taxpayer's Opening Brief and Reply Brief provide sufficient authority for this Court over rule the trial court's sustaining of Respondents' demurrers to this cause of action.

Seventh Cause of Action: Based on the allegations of his FAC Taxpayer sought a judicial declaration that the Lease-Leaseback Contracts between Contractor and District are ultra vires, illegal, void and/or unenforceable. (1 AA 19:¶56-20:¶59.) Taxpayer's Opening Brief and Reply Brief provide sufficient authority for this Court over rule the trial court's sustaining of Respondents' demurrers to this cause of action.

1. The Howard Court Was Not Presented with the Same Conflict of Interest Scenario as Is Present Here

Respondents cite to Section VI of Appellant Howard's Opening Brief (AMJN 42-44) and incorrectly assert the *Howard* Court "considered the very same arguments raised by the parties to the instant appeal" relative to "conflicts of interest of public officials." (RSB p.1). Appellant Howard's conflict of interest arguments were based on alleged gifts contractors in that case gave to school district officials. Relying on Education Code Section 35230's prohibition on the giving of gifts to school board members for the purpose of influencing their contracting decisions Appellant Howard asserted:

> "Because contractors donate millions of dollars to school boards in campaign contributions and often get contracts, there is clearly the appearance of a conflict of interest which would preclude these sale leaseback contracts. For this reason, the lease leaseback contracts between the SCHOOL DISTRICT and the contractor are ultra vires, void and unenforceable." (AMJN

p.44.)

Here Taxpayer's conflict of interest argument is not premised on gifts or Education Code Section 35230 as was the case in *Howard*.. There is no mention of gifts what so ever in Taxpayer's pleadings or briefs. Instead, Taxpayer's claim of conflict of interest arises from Contractor's prior consulting contract with District for pre-construction services relative to the same project for which Contractor was awarded the subsequent lease-leaseback contracts to construct. Taxpayer's claim of conflict of interest is premised on *Hub City Solid Waste Services, Inc. v. City of Compton* (2010) 186 Cal.App.4th 1114 (*Hub*); *California Housing Finance Agency v. Hanover/California Management and Accounting Center, Inc.* (2007) 148 Cal.App.4th 682 (*CHFA*) and *Schaefer v. Berinstein* (1956) 140 Cal.App.2d 278 (*Schaefer*) and their application of the common law and Government Code 1090 prohibition on a public entity's contracts being awarded to consultants/advisors of the public entity who have a financial interest in those contracts.

In *Schaefer* the Second District Court of Appeal upheld the application of common law conflict of interest prohibition codified in Government Code, Section 1090 et seq., to an independent contractor (a specially retained outside counsel) working for a public entity when the Court stated at page 291 "A person merely in an advisory position to a city is affected by the conflicts of interest rule... [because he] was an officer and agent of the city... in a position to advise the city council as to what action should be taken."

Subsequently in *Hub* the Second District Court of Appeal again upheld the application the conflict of interest prohibition codified in Government Code, Section 1090 to an independent contractor (a waste management

consultant) working for a public entity. Citing to *CHFA* the *Hub* Court stated:

> "A person in an advisory position to a city may fall within the scope of section 1090. In particular, independent contractors whose official capacities carry the potential to exert considerable influence over the contracting decisions of a public agency may not have personal interests in that agency's contracts." *Id.*, at 1124-1125 citing to *CHFA* at p. 693.

The above cases state that conflict of interest prohibitions are broadly construed and will be found where the independent contractor has merely the opportunity to use their position to advance their financial interest. They do not have to actually act for their benefit or for the public entity's detriment for there to be a cause of action for conflict of interest. They just have to participate in the making of a contract that they have a financial interest in.

Participation in the making of a contract is defined broadly as any act involving preliminary discussions, negotiations, compromises, reasoning, planning, drawing of plans and specifications, and solicitation for bids. *Millbrae Assn. for Residential Survival v. City of Millbrae* (1968) 262 Cal.App.2d 222, 237; see also *Stigall v. City of Taft* (1962) 58 Cal.2d 565, 569.

Here as their provider of preconstruction services and advice Contractor was likewise in a position to advise and provide considerable influence upon District's school board and staff as to what actions they should take relative to the Project design, materials, work scope, schedule and sequence of the Lease Leaseback Contract. Even if Contractor did not use its position as District's preconstruction service provider to advance Contractor's financial interest in the subsequent Lease Leaseback Contracts, its ability to do so created a potential for conflict of interest that should have precluded Contractor from being considered for an award of the Lease Leaseback Contracts.

The *Howard* Court never considered the foregoing cases or the facts upon which Taxpayer's conflict of interest allegations are based. Therefore, contrary to Respondents' assertion, the *Howard* Court did not consider "the very same arguments raised by the parties to the instant appeal" relative to "conflicts of interest of public officials."

B. Respondents Incorrectly Assert 17417 Has No Application Here Because 17406 Exclusively Covers the Sublease Potion of the Lease-Leaseback Transaction

In Section A of RSB Respondents assert 17406 exclusively covers the sublease potion of the lease-leaseback transaction by including language which "expressly requires that the lessee "shall" construct school facilities on the site and that title to the site and the school facilities shall vest in the District at the end of the term." (RSB p. 2.) Respondents posit the strawman "[i]f Section 17406 was not meant to exempt the sublease from competitive bidding, then there would be no reason for the statute to contain all these provisions about construction work and terms."

Taxpayer asserts 17406 requirement quoted by Respondents' RSB at page 2 that "lessee therein . . . construct on the demised premises, or provide for the construction thereon . . ., a building . . . for the use of the school district during the term thereon . . . " is present to ensure that a school district's leasing out of its property to a third party without competitive bidding is allowed only if that site lease is for the purpose of enabling that third to construct on the leased site/premises facilities that the third party will be leased back to the school district. (AOB p. 2, fn1; p. 25 and ARB pp. 24-25.) Otherwise 17472 would apply to require the school only lease its property out to the third party that offers to pay the school district the highest rent.

Despite Respondents' assertion to the contrary, the language used by the Legislature in 17406 clearly applies only to the site lease portion of the lease leaseback transaction when 17406 is read in context of and harmonized with the other provisions of Article 2. The confusion posited by Respondents' only exists when one tries to apply Respondents' strained and constrained interpretation of 17406 in a vacuum.

Respondents' strained and constrained interpretation of 17406 and 17417 lead to mischief and absurdity. Taxpayer's proposed interpretation is consistent with common sense and promotes sound public policy. Taxpayer's reasoned interpretation of 17406 and 17417 should be adopted under the following authority:

> "If a statute's language permits more than one reasonable interpretation, we may consider 'a variety of extrinsic aids, including the ostensible objects to be achieved, the evils to be remedied, the legislative history, public policy, contemporaneous administrative construction, and the statutory scheme of which the statute is a part.' [Citation.] After considering these extrinsic aids, we 'must select the construction that comports most closely with the apparent intent of the Legislature, with a view to promoting rather than defeating the general purpose of the statute, and avoid an interpretation that would lead to absurd consequences.' [Citation.]" *State ex rel. Dockstader v. Hamby* (2008) 162 Cal.App. 4th 480, 488 citing to *Wilcox v. Birtwhistle* (1999) 21 Cal.4th 973, 977-978

C. Respondents Incorrectly Assert 17417's Competitive Bidding Requirements Apply to Agreements Entered Into Under 17407

In Section B of RSB Respondents assert the *Howard* Court's interpretation of 17406 (exempting both the site lease and facilities leaseback agreements from competitive bidding) does not render 17417 a nullity because 17417's competitive bidding requirements applies agreements entered into by

a school district pursuant to Section 17407. (RSB 4-5.) Respondents' RSB fails to overcome Taxpayer's assertion 17417 can not apply to leases under 17407 because, inter alia, 17407 and 17417 contain terms which are incongruous. (ARB pp. 11-14.)

Recall 17407 expressly applies to leases of real property not owned by a school district [3] and 17417 references a lease of "real property belonging to the district." Moreover, 17407 contains its own express requirements for two weeks of advertising for competitive bids which conflict with the express requirements for three weeks of advertising for competitive bidding in section 17417. (ARB 11-12.)

By its express terms 17417 is the section in Article 2 that prescribes the specific requirements for the contract by which a school district pays money to a third party to leaseback the facilities constructed by that third party on district owned property. 17417 requires the leaseback contract be awarded only to the third party who, by way of sealed competitive bids, offers to charge the district the least to construct on district owned property the facilities specified by the district in their plans and specifications which have been approved by DSA prior receiving said bids.

Respondents unsuccessfully attempt to counter the Taxpayer's analysis and argument at ARB pp.14-17 that 17417 cannot be used with 17407 because the two statutes expressly specify different minimum lengths of time notices inviting bids must be published and held open. Two weeks for 17407 and three weeks for 17417. Respondents' assertion (RSB p.5) that 17417 only

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[3] That 17407 is clear from its language requires title to the site vest in the district at the end of the lease term. Specifically "[t]he instrument shall provide that the title to the building and site shall vest in the district at the expiration of the lease,...

requires solicitation of bids for two weeks just as in 17407 is contrary to the express language of 17417 which 17417 states:

> "The resolution **shall fix a time, not less than three weeks** thereafter **for a public meeting** of the governing board to be held at its regular place of meeting, **at which sealed proposals to enter a lease or agreement with the school district will be received** from any person, firm, or corporation, and considered by the governing board [emphasis added].

17417 goes on to state:

> At the time and place fixed in the resolution for the meeting of the governing body, all sealed proposals which have been received shall, in public session, be opened, examined, and declared by the board. Of the proposals submitted which conform to all terms and conditions specified in the resolution of intention to enter a lease or agreement and which are made by responsible bidders, the proposal which calls for the lowest rental shall be finally accepted, or the board shall reject all bids.

The sophistry and confusion of meeting notice periods and bid solicitation periods offered by Respondents at RSB p. 5 must be recognized and rejected by the Court. Further, Respondents' reference to 17418 is a red herring since that statute authorizes districts to enter into contracts with non-profit public benefit corporations who then have to likewise engage in competitive bidding.

In this case Taxpayer challenges the leaseback contract between District and Contractor on the grounds it does not comply with all of the requirements prescribed by 17417, namely proper solicitation of sealed bids and the award of the leaseback contract by which District is going to pay tens of millions of bond funded dollars paid by taxpayers only to the lowest responsible bidder. Such a process is required by Article 2 to ensure bond proceeds are not wasted and cannot be misdirected through fraud, favoritism and/or corruption.

D. Respondents Incorrectly Assert The Howard Court Properly Relied on the 1973 Attorney General Opinion Holding that Lease-Leaseback Agreements Are Not Subject to Competitive Bidding

In Section C of RSB Respondents attempt to excuse the 1973 Attorney General Opinion (56 Ops.Atty.Gen. 571 (1973)'s failure to expressly recognize or consider the existence of the contemporaneous predecessor of section 17417 as noted by Taxpayer in ARB pp. 14-16 by stating:

> "The Attorney General could not have analyzed the statute in a vacuum, and must have considered the entirety of the lease-leaseback law when rendering the opinion." (RSB p.6.)

and

> "Clearly, the Attorney General could not have made such a pronouncement without considering all the relevant statutes, including the predecessor of section 17417, and comparing them to each other." (RSB p.5-6.)

Respondents' wishful thinking does not change the fact the Attorney General never acknowledges or discusses 15712 which, at the time of the Attorney General opinion, was the predecessor of section 17417. Moreover, the Attorney General does acknowledge how incongruous its conclusion is with the surrounding lease-leaseback statutes requiring competitive bidding as well as California's long tradition of requiring competitive bidding to determine the amount of public funds to be paid by a public entity for construction projects. *Id.*, at 580. The Attorney General opinion expressly stated its reservation about its conclusion because "[c]onsiderations of wisdom, expediency, or policy suggest a contrary conclusion..." *Id.*, at 580-581. (See ARB 14-16.)

Contrary to Respondents' assertion, Taxpayer does not discount the overall importance and persuasiveness of Attorney General opinions in general to Courts. (RSB p.7.) However, the foregoing does not change the fact that Courts generally give little deference to Attorney General opinions that appear to misinterpret the law as is the case here. (ARB 14-15.)

Further, Respondents' citation to the 1986 Legislative amendments to add the phrase "without advertising for bids" (RSB p. 11) (as well as the Legislatures addition of the phrase "Notwithstanding 17417") actually supports Taxpayer's interpretation of 17406 and 17417. Under Respondents' logic such amendments were enacted by the Legislature, in response to the 1973 Attorney General opinion, attempting to clarify that site leases under 17406 do not need to be competitively bid whereas facilities leaseback agreements under 17417 do need to be competitively bid. It makes sense site leases would not need competitive bidding since the third party is paying a de minimis sum to the school district and that facilities leaseback agreements would need competitive bidding since school districts are paying millions of dollars to the third party to construct school facilities. (AOB p. 23, 29.)

E. Respondents Make Too Much of AB 1486 and Misconstrue the Governor's Related Veto Message

In Section D of RSB Respondents continue to make too much of AB 1486 and misconstrue the then Governor's veto message as well as Taxpayer's arguments relative thereto. Taxpayer reiterates his prior arguments why the former Governor's veto message is not evidence of the Legislative intent Respondents contend it is. What is more, AB 1486 and the Governor's related veto message do nothing to change 17417 which is the gravamen of Taxpayer's argument. The interpretation of 17406 and 17417 asserted by Respondents does not necessarily follow from either AB 1486 or the

Governor's veto message relative thereto.

F. Respondents Continue to Misinterpret "Notwithstanding 17417" and Misapply the Klajic and Summer H Cases

In Section E of RSB Respondents continue to misinterpret the phrase "Notwithstanding 17417" and misapply the Klajic and Summer H cases. Taxpayer reiterates his prior arguments why Respondents' interpretation of the foregoing are flawed.

G. Respondents Incorrectly Discount the State Allocation Board Report

While the SAB Report may have been part of the record on appeal in the *Howard* case, it was not briefed by either party and it was not referenced by that Court. Here the analysis and opinions of the SAB Report provide a substantial basis for the arguments advanced by Taxpayer. Respondents' ad hominem dismissal of the analysis and opinions in the SAB Report as "the uninformed musings of a staff attorney" (RSB p.8) fails to acknowledge and give due respect to a California state administrative agency attorney who in good faith was attempting to summarize, analyze and bring to their agency's attention valid concerns and objections to the manner in which the lease leaseback process has been applied over the last 10 years.

Assuming for the sake of argument that the SAB Report should not be given as much weight as an Attorney General Opinion does not negate the analysis and opinions contained therein which should be carefully considered by this Court as it makes its own determination of the issues and requested interpretations before it. Taxpayer respectfully requests this Court expressly address the analysis and opinions contained in the SAB Report as part of its ultimate opinion in this matter.

II. CONCLUSION

Based on the foregoing Taxpayer requests this Court reverse the Superior Court's sustaining of District's and Contractor's Demurrers to and subsequent dismissal of Taxpayer's First Amended Complaint and remand this matter to the Superior Court with direction to allow Taxpayer's action to proceed.

Dated: November 10, 2014

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By: 

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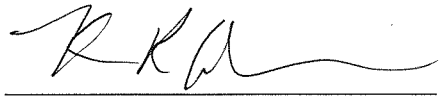
CERTIFICATE OF COMPLIANCE

Pursuant to rule 8.204(c) of the California Rules of Court, I hereby certify that this brief exclusive of the cover, table of contents and table of authorities contains 3478 words, including footnotes. In making this certification, I have relied on the word count of the computer program used to prepare this brief.

Executed on November 10, 2014, at San Diego, California.



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