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## Lease-Leasebacks Are Exempt from Competitive Bidding, Court of Appeal Confirms

Pointing to the “plain, unambiguous, and explicit” language of the statute, the California Court of Appeal has confirmed that Education Code section 17406 exempts school districts from obtaining competitive bids when entering into lease-leaseback agreements to improve school property. (*Los Alamitos Unified School Dist. v. Howard Contracting, Inc.* (9/17/14, No. 6049194).)

In this case, the Los Alamitos Unified School District (“District”) entered into a lease-leaseback agreement with a third-party contractor for a construction project involving upgrades and improvements to its high school track and athletic field. The agreement was authorized by the District’s governing board and the District sought court validation of the agreement, as authorized by Code of Civil Procedure section 860. Another contractor, Howard Contracting Inc. (“Howard”), filed an objection, claiming the lease-leaseback agreement was “unconstitutional, unconscionable, illegal and a theft of public funds” because the District did not obtain competitive bids for the project.

Affirming a trial court’s judgment in the District’s favor, the Court of Appeal rejected Howard’s argument that California’s public contract law requiring competitive bidding applies to the construction delivery method known as “lease lease-back,” an alternative means of construction that permits a school district to lease property for a minimum rental value of one dollar per year to a contractor who is responsible for construction of a building or buildings on the property to be used by the district during the lease term, with title to the building(s) vesting in the district at the expiration of the term (or earlier if the agreement so provides). Instead, the court observed that the “great weight of authority” supported the District’s contention that the specific language of section 17406 exempted lease-leaseback agreements from the competitive bidding that would otherwise apply to a public works contract.

The Court of Appeal pointed to a 1973 interpretation of an earlier version of section 17406 by the California Attorney General stating that “the Legislature excluded a [lease-leaseback] arrangement . . . from the notice and bid requirements. Because a school district is not required to obtain bids for [such] lease arrangements . . . , it may lease its property for the purpose of permitting the construction thereon of school buildings which the district will lease at such rental value as the governing board deems in the best interest of the district without reference to competitive bidding.”

The court also noted that the California Legislature, in 2004, sought to amend section 17406 to require that districts solicit competitive bids for lease-leaseback arrangements. However, the proposed legislation was vetoed by the Governor, who stated that the bill “imposes restrictions on lease-leaseback contracts that could limit competition, inadvertently limit schools’ flexibility, and drive higher administrative costs; thereby potentially increasing the overall cost of school facility construction.” According to the court, the unsuccessful attempt to amend section 17406 to delete reference to the language “without advertising for bids” implies that the section as it currently reads does not require competitive bidding.

Howard also unsuccessfully contended that Education Code section 17417, which contains a general requirement of competitive bidding for a “lease or agreement,” should take precedence over section 17406. According to the court, because section 17046 begins with the language “notwithstanding section 17417,” this shows that “section 17406 provides an exception to the more general section 17417.”

While it is uncertain whether this decision will be appealed to the California Supreme Court, the Court of Appeal’s published opinion provides judicial support for previous interpretations of section 17406, including that of the Attorney General, that districts are exempt from competitive bidding when entering into lease-leaseback agreements. F3 will provide updates on any subsequent developments in this case.

If you have any questions regarding this decision or any related matter, please call one of our six offices.

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