Case No. S266344

SUPREME COURT OF THE STATE OF CALIFORNIA

STEPHEN K. DAVIS,
Plaintiff and Respondent,

v.

FRESNO UNIFIED SCHOOL DISTRICT, AND
HARRIS CONSTRUCTION CO., INC.
Defendants and Petitioners.

After a Published Decision By the Court of Appeal,
Fifth Appellate District
Case No. F079811

From the Superior Court,
County of Fresno
Case No. 12CECG03718
The Honorable Kimberly Gaab

ANSWERING BRIEF ON THE MERITS

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Respondent Stephen K. Davis ("Taxpayer") respectfully submits the following Answering Brief on the Merits in response to Petitioner Fresno Unified School District ("District")'s Opening Brief on the Merits (cited as "DOB") and Petitioner Harris Construction Co., Inc., ("Builder")'s Opening Brief on the Merits (cited as "BOB"). (District and Builder collectively "Petitioners".)

INTRODUCTION

Based on 50 years of precedent and sound public policy this Court should conclude a lease-leaseback arrangement in which construction is financed entirely through District's general obligation bond proceeds already on hand rather than by or through the builder is not a "contract" within the meaning of Government Code § 53511 and not subject to the limitations and immunities afforded by Government Code §§ 860-870 (the "Validation Statutes"). This was the conclusion in *Davis v. Fresno Unified Sch. Dist.*, (2020) 57 Cal.App.5th 911 ("*Davis II*") which is well reasoned and should be affirmed by this Court.

Here, this Court is being asked to conclude the opposite so Builder, a private party, can keep $36 million public dollars it illegally received from District by way of lease-leaseback construction contracts that were void ab initio for their failure to comply with applicable public contracting statutes and/or conflict of interest prohibitions.

The issue before this Court must be considered in light of the following public interest authorities and sound policies:

"No principle of law is better settled than that a party to an illegal contract cannot come into a court of law and ask to have

his illegal objects carried out;" *Lee On v. Long* (1951) 37 Cal.2d 499, 501.

California Constitution Article XI, Section 10(a) says a "local government body may not... pay a claim under an agreement made without authority of law." Further, California Constitution Article XVI, Section 6 says "The Legislature shall have no power to....authorize the making of any gift, of any public money or thing of value to any individual, municipal or other corporation whatever..."

For over 150 years in California, the rule has been public contracts executed without full compliance with all applicable legal requirements are: (1) void ab initio and unenforceable as being in excess of the agency's power; (2) estoppel to deny their validity cannot be asserted; and (3) quasi-contract recovery is not allowed. See, e.g., *Zottman v. San Francisco* (1862) 20 Cal. 96; *Reams v. Cooley* (1915) 171 Cal. 150; *Los Angeles Dredging Co. v. Long Beach* (1930) 210 Cal. 348; *Miller v. McKinnon* (1942) 20 Cal.2d 83, 87-88. It is equally well settled that money paid under a void contract may be recovered in a suit filed by a taxpayer on behalf of the governmental agency involved . *Id.* at 96. This Court noted "It may sometimes seem a hardship upon a contractor that all compensation for work done, etc., should be denied him; but it should be remembered that he, no less than the officers of the corporation, when he deals in a matter expressly provided for in the charter, is bound to see to it that the charter is complied with." *Id.* at 89. Further, contractors like Builder are presumed to know the laws relating to public contracting. *Id.* The

rational for the Court's strict application of this doctrine is that to hold otherwise would create a disincentive for contractors and public entities to follow the law. *Id.*

Likewise, public contracts which violate California's conflict of interest prohibitions are void from their inception. *Lexin v. Superior Court* (2010) 47 Cal.4th 1050, 1073, as modified (Apr. 22, 2010); *Thomson v. Call* (1985) 38 Cal.3d 633, 646 & fn. 15; *Stigall v. City of Taft* (1962) 58 Cal.2d 565, 568–569.

This Court recently summarized a key principal of law and public policy in California that applies to this case: "A void contract is without legal effect. (Rest.2d Contracts, § 7, com. a.) It binds no one and is a mere nullity. [citation omitted] Such a contract has no existence whatever. It has no legal entity for any purpose and neither action nor inaction of a party to it can validate it. As we said of a fraudulent real property transfer in First Nat. Bank of L.A. v. Maxwell (1899) 123 Cal. 360, 371, 55 P. 980, 'A void thing is as no thing.'" *Yvanova v. New Century Mortgage Corp.* (2016) 62 Cal.4th 919, 929.

Moreover, "the court has both the power and duty to ascertain the true facts in order that it may not unwittingly lend its assistance to the consummation or encouragement of what public policy forbids. It is immaterial that the parties, whether by inadvertence or consent, even at the trial do not raise the issue. The court may do so of its own motion when the testimony produces evidence of illegality. It is not too late to raise the issue ... even on appeal." *Fellom v. Adams* (1969) 274 Cal.App.2d 855,

863, quoting *Estate of Prieto* (1966) 243 Cal.App.2d 79, 85–86.

"[T]he purpose of requiring governmental entities to open the contracts process to public bidding is to eliminate favoritism, fraud and corruption; avoid misuse of public funds; and stimulate advantageous marketplace competition." *MCM Construction, Inc., v. City and County of San Francisco* (1998) 66 Cal.App. 4th 359, 369. To promote the foregoing public policies the letting of public contracts universally receive close judicial scrutiny and contracts awarded without strict compliance with bidding requirements will be set aside even where it is certain there was in fact no corruption or adverse effect on the bidding process and deviations would save the entity money. *Ghilotti Construction Co. v. District of Richmond*, (1996) 45 Cal. App. 4th 897, 907-908.

Respondents concede Builder provided no financing under the lease-leaseback construction contracts at issue and instead those contracts were entirely funded by District issued bonds sold one year before Builder was awarded the challenged contracts. Moreover, the bonds that funded construction of the Project were general obligation bonds paid for by ad valorem taxes levied on all taxable real property (and certain personal property) across the entire District rather than lease revenue bonds or tax increment bonds directly paid for from the Project. Taxpayer litigation concerning construction contracts funded by general obligation bonds does not interfere with the stream of revenue (ad valorem taxes) used to pay off those bonds and therefore those construction contracts are not subject to validation. What is more, Respondents' arbitrage arguments in favor of validation are

red herrings because the bonds that financed the Project, like all California tax exempt public finance, contained anti-arbitrage certifications, covenants and restrictions put in place at the time of their issuance to maintain their advertised tax exempt status for their duration even if there is taxpayer litigation involving subsequent contracts funded by those bonds. Based on the foregoing anti arbitrage protections subsequent contracts funded by those bonds deserve no protection under the Validation Statutes because such litigation will not impair the underlying bonds or the issuing public entities' ability to operate financially. To the contrary, the public entities' financial position will be improved by recovering funds that were illegally paid out in the first place.

Further, Petitioners' reliance on *McGee v. Torrance Unified School District* (2020) 49 Cal.App.5th 814 is misplaced as that case was wrongly decided and should be disapproved by this Court. *McGee* wrongly concluded at 824 "[t]hus, the lease-leaseback agreements involved the District's financial obligations and were inextricably bound up in the District's bond financing, bringing them within the scope of 'contracts' covered by Government Code section 53511." This conclusion is contrary to 50 years of jurisprudence and sound public policy regarding the interpretation and application of Government Code § 53511. *McGee* also gave too much weight to *Wilson & Wilson v. City Council of Redwood City* (2011) 191 Cal.App.4th 1559. This Court should distinguish *Wilson* from this case because here the Superior Court has in personam jurisdiction over Builder based

on its Answer and participation in the action and effective disgorgement relief can be entered in a judgement against Builder in favor of District to recover all funds wrongfully received by Builder under the void contracts notwithstanding Project completion. Wilson is distinguishable because, no party remained in the action after the completion of the project there against whom any effective relief could be granted.

Finally, if the challenged contracts are found to be subject to the Validation Statutes, (which they are not for the reasons discussed below) this Court should conclude Taxpayer's in personam disgorgement claims on behalf of District against Builder can proceed notwithstanding completion of the Project under Government Code § 869.

SUMMARY OF FACTS & PROCEDURAL HISTORY

This case involves the legality of contracts District awarded on September 26, 2012 for the construction of new school buildings and facilities known as Rutherford B. Gaston Sr. Middle School ("Project"). Per the District Staff Report to the Board of Education at the time of contract award "[s]ufficient funds of $36,702,876 are available in the 2012/13 Measure K and Measure Q budgets." [DOB FN 6; SA0011.] [1] Further, District's

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[1] By way of Footnotes ("FN") District's Opening Brief referenced, incorporated and relied on numerous documents and facts contained therein that were not part of the prior record on appeal, inter alia, DOB Footnotes 5, 6, 7, 18, 19, 20, 21, 22, 28, 57, 59, 61, 62 and 65. These documents and the facts contained therein all relate to the single issue on which this Court granted

Resolution authorizing the contract award states "WHEREAS, in order to ensure that moneys sufficient to pay all costs will be available for the Project, the District desires to appropriate funds for the Project from its current fiscal year as provided by the Facilities Lease;" [DOB FN 6; SA0012; Taxpayer's Appendix, Page 17 denoted hereinafter AA17.]

According to the District's Bond Purchase Agreement, District's Measure K, Series G and Measure Q, Series B bonds used to pay for construction of various projects throughout District, including the Project at issue, were general obligation bonds issued on October 13, 2011. [DOB FN 20, 21; SA0022, 24.] Concurrent with the issuance and sale of the foregoing bonds District executed a Certificate As To Arbitrage. [DOB FN 61, 62; SA 0070-78.]

On September 26, 2012, the District adopted Resolution No. 12-01 (AA at pp. 17-21), authorizing the execution of the Site lease and Facilities Lease whereby the District would lease the project site to Harris, who would build the Middle School Project, and thereafter, lease the improvements and the site back to the

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review and are necessary for that issue's proper determination by this Court. Taxpayer does not object to the Court's consideration of these documents and the facts contained therein and Taxpayer relies on same in this Answering Brief on the Merits. However, District did not formally request this Court accept these documents and the facts contained therein. Taxpayer has concurrently filed such a request for himself and District. Taxpayer has also submitted for filing an electronic copy of the foregoing documents in the form of an indexed and book marked Supplemental Appendix ("SA") bates stamped SA0001-SA0078.

District. The lease-leaseback transaction was comprised of two agreements, the Site Lease (AA, pp. 133-141) and the Facilities Lease (AA, pp.143-158) (collectively the "Lease-Leaseback Agreement.")

The Site Lease provides that beginning on September 27, 2012, the District would lease the site to Harris for $1 in rent (AA, p. 135.) Pursuant to the Facilities Lease, the District paid monthly progress payments for construction services up to 95% of the total value of the work performed, with a 5% retention pending acceptance of the Middle School Project and recordation of the Notice of Completion. (AA, p. 171). The Middle School Project was completed on November 13, 2014 (AA, p. 249) and a Notice of Completion was recorded on December 4,2014 (AA, p. 252).

On November 20, 2012, Taxpayer filed his Verified Complaint for; (1) Reverse Validation Pursuant to CCP § 863; 2. Recovery of Funds Expended on Illegal Contract. [AA6-103]. In response to demurrers by District and Contractor, Taxpayer filed his operative First Amended Complaint ("FAC") on March 19, 2013 which included seven individual causes of action entitled:

1. "Recovery of Funds Paid by DISTRICT to CONTRACTOR For Failure to Comply with Public Contract Code § 20110 et seq." [AA112, Lines 9-10]
2. "Recovery of Funds Paid by DISTRICT to CONTRACTOR For DISTRICT Board of Education's Breach of Fiduciary Duty" [AA114,

Lines 17-18]

3. "Recovery of Funds Paid by DISTRICT to CONTRACTOR For Failure to Comply with Education Code § 17417" [AA116, Lines 2-3]
4. "Recovery of Funds Paid by DISTRICT to CONTRACTOR Based on CONTRACTOR's Conflict of Interest" [AA121, Lines 3-4)
5. "Recovery of Funds Paid by DISTRICT to CONTRACTOR Based on Improper Use of Education Code §§ 17400 et seq" (AA 122, Lines 13-14)
6. "Recovery of Funds Paid by DISTRICT to CONTRACTOR Based on Improper Delegation of Discretion by DISTRICT's Board of Education" [AA123, Lines 13-14]
7. "Declaratory Relief" [AA124, Line 17].

In August 2013, the trial court sustained District's and Builder's demurrers to each of the seven causes of action in Taxpayer's FAC. [2 AA 600.] In September 2013, judgment was entered [2 AA 601- 602.] In October 2013 Taxpayer appealed [2 AA 603.]

In June 2015 the Court of Appeal issued its decision in *Davis I* concluding "The judgment is reversed. The trial court is directed to vacate its order sustaining the demurrer and enter a new order (1) sustaining the demurrer as to the breach of fiduciary duty claim, the violation of the Political Reform Act of 1974 claim, and the fifth cause of action alleging the use of the

lease-leaseback arrangement is improper when funds are available to a school from another source and (2) overruling the demurrer as to the other causes of action." *Id.* at 273.

On or about October 28, 2015 Builder filed its Answer to Taxpayer's FAC [1 AA 219-221] and prayed in relevant part that "Plaintiff take nothing by his First Amended Complaint and that the First Amended Complaint be dismissed with prejudice." [1 AA 221.]

On or about October 29, 2015 District filed its Answer to Taxpayer's FAC [1 AA 222-226] and prayed in relevant part that: "Plaintiff take nothing by way of his Complaint" [2 AA 226.]

Trial in this matter was set for July 8, 2019. [2 AA 466.]

On June 25, 2019 the Superior Court held a hearing on Petitioners' Motion for Judgment on the Pleadings ("Motion JOP") and the hearing was transcribed. [2 AA 470-511.]

On July 3, 2019 the Superior Court issued a Minute Order with its Order After Hearing attached whereby the Superior Court granted District and Builder's Motion JOP based on a finding "this action is moot in light of the completion of the project in 2014 and plaintiff can be afforded no effectual relief in this in rem proceeding." [2 AA 512-518, 516-517.)

On July 19, 2019 the Superior Court entered a Judgment of dismissal (2 AA 519-535) in favor of Petitioners.

District served Notice of Entry of Judgment on Taxpayer by mail on July 25, 2019. [2 AA 534.]

Taxpayer filed his Notice of Appeal on August 7, 2019 [2 AA 536] and his Taxpayer's Notice Designating Record On Appeal on

August 16, 2019 [2 AA 537-540] which attached a copy of the Waiver of Deposit of Court Reporter Fees [2 AA 541] and Reporter's Transcript [2 AA 542-583].

A copy of the Superior Court's Register of Actions was also included in Taxpayer's Appendix. [2 AA 584-634.]

On November 24, 2020 the Court of Appeal issued its decision reversing the Superior Court's dismissal of Taxpayer's action as moot and remanding with directions. *Davis v. Fresno Unified School District* (2020) 57 Cal.App.5th 911, as modified on denial of reh'g (Dec. 16, 2020) ("*Davis II*"). In *Davis II* the Court of Appeal summarized the issues on appeal and its conclusion at pp. 916-917 as follows:

> In 2012, plaintiff Stephen Davis sued the Fresno Unified School District (Fresno Unified) and Harris Construction Co., Inc. (Contractor), alleging they entered into a $36.7 million contract for the construction of a middle school in violation of California's competitive bidding requirements, the statutory and common law rules governing conflicts of interest, and Education Code sections 17406 and 17417. Defendants filed a demurrer and obtained a judgment of dismissal. In Davis v. Fresno Unified School Dist. (2015) 237 Cal.App.4th 261, 187 Cal.Rptr.3d 798 (Davis I), we reversed the judgment and remanded for further proceedings. Based on our review of the four corners of the construction agreements and resolution of Fresno Unified's board, which were attached to Davis's pleadings, we concluded Davis properly alleged three grounds for why Education Code section 17406's exception to competitive bidding did not apply to the purported lease-leaseback contracts. First, the contracts used were not genuine leases but were, in substance, simply a traditional construction contract with

progress payments. (*Davis I*, supra, at pp. 286, 290, 187 Cal.Rptr.3d 798.) Second, the contractual arrangement "did not include a financing component for the construction of the project." (*Id.* at p. 271, 187 Cal.Rptr.3d 798.) Third, the contractual arrangement "did not provide for Fresno Unified's use of the newly built facilities 'during the term of the lease' as required by [Education Code] section 17406, subdivision (a)(1)." (*Ibid.*) We also concluded California's statutory and common law rules governing conflicts of interest extended to corporate consultants and Davis alleged "facts showing Contractor, as a consultant to Fresno Unified, participated in the making of a contract in which Contractor subsequently became financially interested"—that is, Contractor participated in creating the terms and specifications of the purported lease-leaseback contracts and then became a party to those contracts. (*Ibid.*)

After remand, the further proceedings included defendants' motion for judgment on the pleadings, which argued the lawsuit had become moot because the construction was finished and the contracts terminated. The trial court agreed, concluding (1) the case was a reverse validation action under Code of Civil Procedure section 863,1 which is an in rem proceeding; (2) invalidating the contracts was no longer effective relief because the contracts had been fully performed; and (3) disgorgement of monies paid to Contractor was not effective relief because California law does not allow disgorgement in an in rem proceeding. Davis appealed. As explained below, we reverse.

First, in determining the type of action or actions Davis is pursuing, his pleading must be given a liberal yet objectively reasonable interpretation. (§ 452.) The interpretation must take account of both the allegations of fact and the relief requested. Here, all of Davis's causes of action, except for the cause of action labeled declaratory relief, requested the

disgorgement of funds paid under the illegal contracts. Disgorgement is an in personam remedy available in a section 526a taxpayer's action, but is not available in an in rem reverse validation action. Consequently, we interpret Davis's pleading as containing both a reverse validation action under section 863 and a taxpayer's action under section 526a. (See Regus v. City of Baldwin Park (1977) 70 Cal.App.3d 968, 972, 139 Cal.Rptr. 196 (Regus) [validation action and taxpayer's action are not mutually exclusive].) Thus, defendants and the trial court erroneously interpreted Davis's lawsuit as exclusively an in rem reverse validation action.

Second, based on our interpretation of Davis's pleading, we consider the legal question of whether California's validation statutes insulate the completed contracts between Fresno Unified and Contractor from attack in a taxpayer's action. The parties' contentions present this issue as whether the purported lease-leaseback contracts fall within the ambit of the validation statutes—more specifically, Government Code section 53511, subdivision (a), which refers to "an action to determine the validity of [a local agency's] bonds, warrants, contracts, obligations or evidences of indebtedness." (Gov. Code, § 53511, subd. (a), italics added.) The term "contracts" is narrowly construed to encompass only contracts involving financing and financial obligations. In Davis I, based on our review of the pleadings and attached documents, we determined the purported lease leaseback contracts "did not include a financing component for the construction of the project." *(Davis I*, supra, 237 Cal.App.4th at p. 271, 187 Cal.Rptr.3d 798.) As a result, we conclude the contracts do not fall within the ambit of Government Code section 53511 and California's validation statutes. It follows that Davis may pursue a taxpayer's action seeking the remedy of disgorgement. (See San Diegans for Open Government v. Public Facilities Financing Authority

of City of San Diego (2019) 8 Cal.5th 733, 737, 257 Cal.Rptr.3d 43, 455 P.3d 311 (San Diegans).) Disgorgement qualifies as effective relief and, therefore, the taxpayer's action part of this lawsuit is not moot.

On March 17, 2021 this Court granted review on the following issue: "Is a lease-leaseback arrangement in which construction is financed through bond proceeds, rather than by or through the builder, a 'contract' within the meaning of Government Code section 53511?"

ARGUMENT

I. TAXPAYER HAS STANDING UNDER CODE OF CIVIL PROCEDURE § 526A AND THE COMMON LAW TO MAINTAIN THIS ACTION

Petitioners emphasize Taxpayer expressly stated his action was brought under the Validation Statutes. However, such allegations are not dispositive. [2] Taxpayer included in his

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[2] Petitioners have also criticized Taxpayer for not seeking an injunction to stop construction of the project. Taxpayer did not seek an injunction so as to not delay the construction of needed school facilities for the District's students and teachers. Moreover, the primary relief requested in each cause of action in Taxpayer's FAC was recovery of funds paid by District to Builder. Injunctive relief would have been denied because monetary relief is available even if a void contract is completely performed. *Thomson v. Call* (1985) 38 Cal.3d 633, 638 & 646-647. What is more, disgorgement of benefits received under a void contract is automatic. *Carson Redevelopment Agency v. Padilla* (2006) 140 Cal.App.4th 1323, 1336.

complaints validation language in an abundance of caution to avoid Petitioners' assertion they were barred for not being validation actions. However, in light of California law as discussed below bringing the complaint as a validation complaint was not necessary and is certainly not fatal to Taxpayer's claims seeking recovery back to District all amounts paid to Builder under contracts that were void because the failed to comply in all respects with applicable legal requirements.

A taxpayer may bring suit against government bodies pursuant to Code of Civil Procedure section 526a and based on common law. *Los Altos Property Owners Assn. v. Hutcheon* (1977) 69 Cal.App.3d 22, 26. Section 526a permits an action to obtain a judgment, restraining and preventing any illegal expenditure of, waste of, or injury to, the estate, funds, or other property of a county, town, city or city and county of the state, ... against any officer thereof, or any agent, or other person, acting in its behalf. A common law taxpayer suit is limited to the grounds of fraud, collusion, ultra vires, or a failure to perform a duty specifically enjoined. The primary purpose of section 526a, originally enacted in 1909, is to enable a large body of the citizenry to challenge governmental action which would otherwise go unchallenged in the courts because of the standing requirement. California courts have consistently construed section 526a liberally to achieve this remedial purpose. *Blair v. Pitchess* (1971) 5 Cal.3d 258, 267-268.

II. THE DAVIS COURT CORRECTLY FOUND THE CONSTRUCTION CONTRACTS AT ISSUE ARE NOT THE KIND SUBJECT TO THE VALIDATION

STATUTES

Not all contracts are subject to validation under statute authorizing an agency to bring action to determine validity of "its bonds, warrants, contracts, obligations, or evidences of indebtedness," only those that are in the nature of, or directly relate to the state or a state agency's bonds, warrants, or other evidences of indebtedness. *Hollywood Park Land Co., LLC v. Golden State Transp. Financing Corp., (2009)* 178 Cal.App.4th 924, 935. The types of contracts subject to validation under Government Code §53511 must involve financing rather than ordinary goods and services such as pens, pencils, information technology, public defenders. *Walters v. County of Plumas* (1976) 61 Cal.App.3d 460, 468.

Thus to be a proper subject for a validation action a contract must be a financing contract, which the ones at issue in this action have been admitted by Petitioners not to be. Moreover, in this case, there is no indebtedness at all because District appropriated all funds necessary to pay the costs of the Project construction contracts out of its current fiscal year as of the date of contract award.[3]

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[3] Per the District Staff Report to the Board of Education at the time of contract award "[s]ufficient funds of $36,702,876 are available in the 2012/13 Measure K and Measure Q budgets." [DOB FN 6; SA0011.] Further, District's Resolution authorizing the contract award states "WHEREAS, in order to ensure that moneys sufficient to pay all costs will be available for the Project, the District desires to appropriate funds for the Project from its

Another factor considered in determining whether the Validation Statutes apply to a particular contract was summarized in *California Commerce Casino, Inc. v. Schwarzenegger* (2007) 146 Cal.App.4th 1406 where the Second District Court of Appeal stated at page 1429:

> Guided by Ontario and other authorities, Kaatz found "[i]t is therefore clear that 'contracts' under Government Code section 53511 should be assigned a restricted meaning. Rather than authorizing proceedings to validate any public agency contract—or even any contract constituting a financial obligation of a public agency [fn. omitted]—the 'contracts' under Government Code 53511 are only those that are in the nature of, or directly relate to a public agency's bonds, warrants or other evidences of indebtedness." (Kaatz, supra, 143 Cal.App.4th at p. 42, 49 Cal.Rptr.3d 95, italics added.)

Here the lack of prompt validation of District's construction contracts with Builder did not impair the District's ability to operate financially. To the contrary, the Project was built without delay from Taxpayer's litigation. Taxpayer never sought injunctions to stop construction of the Project specifically because he did not want to delay the District's occupancy and use of it. The gravamen of Taxpayer's original and First Amended Complaint was disgorgement back to District all monies paid to Builder under the challenged contracts that were void ab initio for their failure to comply with public contract requirements and

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current fiscal year as provided by the Facilities Lease;" [DOB FN 6; SA0012; AA17.]

conflict of interest prohibitions. Success on Taxpayer's action would actually improve District's ability to operate financially rather than impair it.

The Court of Appeal's conclusion in *Davis II* that a lease-leaseback arrangement in which construction is financed through pre-existing general obligation bond proceeds, rather than by or through the builder, is not a 'contract' within the meaning of Government Code § 53511 is correct law and proper public policy in California and should be affirmed by this Court. The Validation Statutes should not be broadly construed by this Court, as urged by Petitioners, to protect Builder from its legal obligation to disgorge back to District all public monies Builder received under the construction contracts that were void ab intio for their failure to comply with applicable public contracting statutes and/or conflict of interest prohibitions.

This interpretation of Government Code § 53511 and all other statutes which allow for review under the Validation Statutes [4] is required and is good public policy because the purpose of the Validation Statutes is the protection of the public fisc not the protection of private parties who illegally obtain money from the public fisc by way of contracts or other actions

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4 District's argument that Education Code § 15110 subjects the challenged contracts to the Validation Statutes is wrong. The phrase "ordering of the improvement or acquisition" in Education Code § 15110 refers to the purpose stated in the bond measure rather than the award of the future specific contracts that will funded thereby.

that are void ab initio. Based on the above referenced authorities, the construction contracts at issue in this case lack the required characteristics and policy considerations that would bring them within the Validation Statutes.

III. TAXPAYER DISGORGEMENT ACTIONS CHALLENGING VOID PUBLIC CONSTRUCTION CONTRACTS WILL NOT MAKE THE INTEREST PAID ON THE PRE-EXISTING MUNICIPAL BONDS THAT FUND THEM TAXABLE

Petitioners incorrectly assert Taxpayer's action on the Lease Leaseback Contracts (and similar actions by other taxpayers) could hypothetically destroy the tax exempt status of California School District Bonds such that District's bonds and the contracts should be found by this Court to be "integral" "inextricably bound up" and/or "intimately intertwined" because of illusory arbitrage risks and therefore subject to the Validation Statutes. [DOB pp. 61-66; BOB pp.21-28.] Petitioners' arbitrage boogeyman arguments are legally nor factually incorrect.

A. Petitioners' Arguments Are Legally Incorrect Because They Are Based on a Misinterpretation and Misapplication of the Relevant Anti-Arbitrage Statutes and Regulations

On the topic of tax free interest on municipal bond issues and the need to minimize arbitrage the Federal Court of Appeal for the District of Columbia Circuit has explained:

> The Internal Revenue Code excludes interest on local government bonds from the gross income of bond purchasers. 26 U.S.C. § 103(a). This federal tax exemption makes it possible to sell municipal bonds

at a lower interest rate than other bonds. It also presents issuers with arbitrage opportunities. A local government entity might be tempted to issue tax-exempt bonds with an interest rate of, say, four percent, and then invest the proceeds in Treasury bonds earning five percent. If the entity invests the proceeds in appropriately structured derivatives, such as Treasury STRIPS, it can earn an instant, risk-free profit on the transaction.

Statutory and regulatory restrictions are designed to "minimize the arbitrage benefits from investing gross proceeds of tax-exempt bonds in higher yielding investments and to remove the arbitrage incentives ... to issue bonds earlier ... than is otherwise reasonably necessary to accomplish the governmental purposes for which the bonds were issued." 26 C.F.R. § 1.148-0(a). An issuer's failure to abide by the restrictions renders the bonds "arbitrage bonds," the interest on which is not tax-exempt. 26 U.S.C. §§ 103(b)(2), 148.

Although investing bond proceeds in higher yielding investments normally causes the bonds to become arbitrage bonds, Treasury Department regulations contain an exception. Up to $10 million of bonds may remain tax-exempt and the issuer may retain any profits earned during a three-year "temporary period" after the issue date if the issuer "reasonably expects" to satisfy three tests: the expenditure test, the time test, and the due diligence test. 26 C.F.R. § 1.148-2(e)(2). The expenditure test requires the issuer to spend "at least 85 percent" of the bond proceeds on "capital projects" within three years. Id. § 1.148-2(e)(2)(A). The time test requires that the issuer incur "within 6 months of the issue date a substantial binding obligation" to spend "at least 5 percent" of the bond proceeds on "capital projects." Id. § 1.148-2(e)(2)(B). The due diligence test requires that "completion of the capital projects and the allocation

> of the [funds] ... to expenditures proceed with due diligence." Id. § 1.148-2(e)(2)(C).
>
> Because the Treasury regulations look to whether the issuer reasonably expected to satisfy the three tests "as of the issue date," Id. § 1.148-2(b), not to whether it actually satisfied them later, there is potential for abuse....

Weiss v. S.E.C. (D.C. Cir. 2006) 468 F.3d 849, 850–851.

Petitioners argue the exception to the IRS's statutory and regulatory arbitrage prohibitions is the rule and that taxpayer actions threaten to end tax free municipal bonds by preventing public entities from complying with the 3 year limitation. The fallacy of their argument becomes apparent upon a closer examination of 26 U.S.C. §§ 103(b)(2), 148 and 26 C.F.R. §§ 1.148-0 through 1.148.11. Specifically, 26 C.F.R. § 1.148-0(a) provides the following overview:

> Under section 103(a), interest on certain obligations issued by States and local governments is excludable from the gross income of the owners. Section 148 was enacted to minimize the arbitrage benefits from investing gross proceeds of tax-exempt bonds in higher yielding investments and to remove the arbitrage incentives to issue more bonds, to issue bonds earlier, or to leave bonds outstanding longer than is otherwise reasonably necessary to accomplish the governmental purposes for which the bonds were issued. To accomplish these purposes, section 148 restricts the direct and indirect investment of bond proceeds in higher yielding investments and requires that certain earnings on higher yielding investments be rebated to the United States. Violation of these provisions causes the bonds in the issue to become

> arbitrage bonds, the interest on which is not excludable from the gross income of the owners under section 103(a). The regulations in §§ 1.148–1 through 1.148–11 apply in a manner consistent with these purposes.

Distilled to their core, these statutes and regulations say public entities are only at risk of having their tax exempt bonds declared taxable arbitrage bonds if they invest them in higher yielding investments in amounts or durations longer than the limited arbitrage exception summarized in *Weiss*. The solution to the fake 'taxpayer action problem' Petitioners have manufactured is for the public entity to invest the unspent proceeds of their bond issue in investments that pay the same or less than the yield rate of their bonds so there is no arbitrage. Moreover, if a public entity does receive yield earnings in excess of the statutory/regulatory arbitrage limitations 26 U.S.C. §148(f) and 26 C.F.R. § 1.148-3 allow the public entity to pay a rebate to the federal government to maintain the tax exempt status of their qualified bonds.

As discussed in the next section District's Certificate as to Arbitrage ensures compliance with foregoing. Additionally, District's investments are handled by the County Treasurer based on Education Code § 15146(g) which states:

> The proceeds of the sale of the bonds, exclusive of any premium received, shall be deposited in the county treasury to the credit of the building fund of the school district, or community college district as designated by the California Community Colleges Budget and Accounting Manual. The proceeds

> deposited shall be drawn out as other school moneys are drawn out. The bond proceeds withdrawn shall not be applied to any purposes other than those for which the bonds were issued. **At no time shall the proceeds be withdrawn by the school district or community college district for investment outside the county treasury.** Any premium or accrued interest received from the sale of the bonds shall be deposited in the interest and sinking fund of the school district or community college district (emphasis added).

Based on the foregoing District can independently control and avoid a loss of tax exempt status arbitrage penalty irregardless of whether there is taxpayer litigation.

B. Petitioners' Arguments Are Factually Incorrect Because District Issued a "Certificate As To Arbitrage" Concurrent with the Sale of the Bonds By Which It Promised to Take Actions That Eliminates The Potential For a Taxable Interest Arbitrage Penalty

In its Opening Brief District acknowledges and quotes from its Certificate as to Arbitrage for Measure K, Series G and Measure Q, Series B ("Anti-Arbitrage Certificate") signed under penalty of perjury by District's Superintendent at the time of the subject bond issuance on October 13, 2011. [DOB p. 63, FN 60-61; SA0070-78.] October 13, 2011 is the "Closing Date" referenced on page 2 of District's Bond Purchase Agreement. [DOB pp.15-16 FN 20-21 Bond Purchase Agreement Measure K, Series G and Measure Q, Series B, p. 2, SA0022-41.] District's execution of the Anti-Arbitrage Certificate was an express

condition of closing under the Bond Purchase Agreement. [Id. at p. 11, ¶ 6, SA0027.]

In compliance with 26 C.F.R. § 1.148-2(b) District's Superintendent certified District's "reasonable expectations as of the issue date regarding the amount and use of the gross proceeds of the issue" by way of the Anti-Arbitrage Certificate executed on October 13, 2011 concurrent with Districts sale of bonds certifying and covenating relative to those bonds, in relevant part, as follows:

> (d) Completion of Project; Investment of Building Funds; Capital Expenditures. The District has entered into a contract for construction with respect to the Project [5], which contract constitutes a substantial binding obligation of the District to a third party and will be in excess of five percent (5%) of the "Net Sale Proceeds" of the Bonds (namely, an amount of proceeds of the Bonds equal to the issue price of the Bonds, below, less accrued interest, if any). The District will proceed with due diligence to complete the Project and to spend the proceeds of the Bonds. Completion is expected by September 1, 2014. All expenditures from the Building Fund will be capital expenditures. Not less than eighty-five percent (85%) of the Net Sale Proceeds will be spent within three (3) years of the date hereof. Amounts deposited in the Building Funds will be invested without yield restrictions for the period from the date

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The term "Project" in the District's bond related documents referred to more projects than just the Project at issue in this litigation as evidenced by the difference in the amount of the bond issue ($108,432,318.35 [DOB FN 61, 62; SA0074]) compared to the amount District authorized to pay for its contract with Builder ($36,702,876 [DOB FN 6; SA0011]).

hereof to the date that is three (3) years after the date hereof unless earlier expended (the "3-year Temporary Period"). Interest earnings and gains resulting from investment of each Building Fund will be retained in that Fund and used for the payment of costs of the Project. **Proceeds of the Bonds and interest earnings and gains thereon, if any, remaining in the Building Funds following the 3-year Temporary Period will be invested at a yield not in excess of the yield of the Bonds (see below) or yield reduction payments under Section 148 of the Internal Revenue Code of 1986, as amended (the "Code"), will be made to the federal government with respect to such investment after the end of the 3-year Temporary Period.** Amounts, if any, remaining in the Building Funds upon completion of the Project will be retained in the Building Funds and used for capital expenditures in furtherance of the governmental purposes of the District (emphasis added). [DOB FN 61, 62; SA0071-72.]

(f) Pledge of Tax Revenues: Excess Tax Revenues. The District has pledged the receipts from certain levies of ad valorem property taxes on taxable property within the boundaries of the District (the "Tax Revenues") to the payment of debt service on the Bonds....[DOB FN 61, 62; SA0072.]

(j) No Improper Financial Advantage. The transaction contemplated herein does not represent an exploitation of the difference between tax-exempt and taxable interest rates to obtain a material financial advantage and does not overburden the tax exempt bond market in that the District is not issuing more bonds, issuing bonds earlier, or allowing bonds to remain outstanding longer than is otherwise reasonably necessary to accomplish the governmental purposes of the Bonds. [DOB FN 61, 62; SA0073.]

(l) Rebate Requirement. The District has covenanted in the Resolutions to comply with requirements for rebate of excess investment earnings to the federal government to the extent applicable and acknowledges that the first payment of excess investment earnings, if any, is required to be rebated to the federal government no later than sixty (60) days after the end of the fifth (5th) bond year for the Bonds. No portion of the Bonds will constitute a private activity bond within the meaning of section 141 (a) of the Code, the average maturity of the Bonds is greater than five (5) years and none of the interest rates on the Bonds vary during the term of the Bonds. As a consequence of the foregoing, investment earnings on the Debt Service Funds will be excluded for the purposes of computation of the amount required to be rebated to the federal government as referenced in this subparagraph without regard to the total amount of said earnings. The use of actual facts is elected for purposes of determining eligibility for and compliance with any expenditure exceptions to arbitrage rebate. [DOB FN 61, 62; SA0073.]

(m) Yield of the Bonds. The Underwriter has represented that the yield of the Bonds is 6.5791%, determined on the basis of regularly scheduled principal and interest payments on the Bonds, adjusted by assuming present value in lieu of certain principal payments in the case of Bonds constituting certain discounted term Bonds, if any, and by assuming certain early redemption of principal in the case of certain yield-to-call Bonds, if any, all in accordance with the procedures for computing the yield on a fixed yield issue contained in Treasury Regulation §1.148-4(b). Said amounts are all discounted to the issue price of the Bonds of $108,432,318.35 (being the face amount of the Bonds of $106,005,764.40, plus net original issue premium of $2,426,553.95.... [DOB FN 61, 62; SA0074.]

> **On the basis of the foregoing, it is not expected that the proceeds of the Bonds will be used in a manner that would cause the Bonds to be arbitrage bonds within the meaning of section 148 of the Code and applicable regulations. To the best of my knowledge, information and belief, the expectations herein expressed are reasonable and there are no facts or estimates, other than those expressed herein, that would materially affect the expectations herein expressed** [emphasis added]. [DOB FN 61, 62; SA0076.]
>
> IN WITNESS WHEREOF, I have hereunto set my hand this 13th day of October, 2011.
> Michael E. Hanson
>
> Superintendent [DOB FN 61, 62; SA0076.]

Based on the foregoing good faith and informed certifications by District's Superintendent, and because, according to *Weiss v. S.E.C.* (D.C. Cir. 2006) 468 F.3d 849, 851, IRS regulations "look to whether the issuer reasonably expected to satisfy the three tests for arbitrage exemption under 'as of the issue date,' and because the issue date for the bonds in question was more than one year before Taxpayer filed his initial complaint there can be no way Taxpayer's action could cause District's general obligation bonds to lose their tax exempt status as asserted by Petitioners. Simply stated, the District promised to the prospective buyers of their bonds at the time of sale that they would take all steps necessary and required by law to ensure the interest earned on the bonds remained tax exempt. No subsequent taxpayer litigation could change that.

IV. MCGEE'S CONCLUSION THAT THE LEASE-LEASEBACK AGREEMENTS WERE SUBJECT TO VALIDATION IS LEGALLY INCORRECT AND SHOULD BE DISAPPROVED BY THIS COURT TO PROMOTE UNIFORMITY OF LAW AND SOUND PUBLIC POLICY IN CALIFORNIA

Petitioners cite to *McGee v. Torrance Unified School District* (2020) 49 Cal.App.5th 814 ("*McGee III*") in support of their assertion *Davis II* should be reversed. McGee cannot stand that weight and instead should be disapproved by this Court to promote uniformity of law and sound public policy in California.

The *McGee III Court* stated; "[h]ere, the challenged lease-leaseback agreements were "funded through Torrance Unified School District General Obligation Bond Measure[s]." (See *McGee II*, supra, 247 Cal.App.4th at p. 240, 202 Cal.Rptr.3d 251 ["The contracts were awarded to Balfour and were funded through a general obligation bond."].) *Id.* at p. 824.

The *McGee III* Court's conclusion at p. 824 "[t]hus, the lease-leaseback agreements involved the District's financial obligations and were inextricably bound up in the District's bond financing, bringing them within the scope of 'contracts' covered by Government Code section 53511" is contrary to 50 years of jurisprudence and sound public policy regarding the interpretation and application of Government Code § 53511. From *Ontario v. Superior Court* (1970) 2 Cal.3d 335 to *Davis II* California Courts have construed Government Code § 53511 and statutes like it narrowly to limit the application of the Validation

Statutes to only contracts which involve financing and whose lack of prompt validation would impair the public entity's ability to operate financially. Moreover, *McLeod v. Vista Unified School Dist.* (2008) 158 Cal.App.4th 1156 cited by *McGee III* is distinguishable because it involved an action that directly challenged the validity of a planned bond issuance and the lack of a prompt validating procedure would impair the district's ability to issue those bonds. *Id.* at 1170. In the *McGee* cases the bonds that funded the challenged contracts were in existence prior to the award of those contracts.

Contracts financed with general obligation bonds, unlike those financed with project related lease revenue bonds, tax increment bonds or other bonds funded by a particular project, do not have the ability to impair the public entity's ability to operate financially because general obligation bonds are funded by all taxable property within a public entity's jurisdiction rather than by the specific project or specific properties within a redevelopment area. Taxpayer litigation involving projects funded by pre-existing general obligation bonds does not have the ability to meaningfully impair the tax assessed value of properties within an entire school district to such a degree as to impair the school district's ability to operate. As further assurance ad valorem tax revenues can satisfy general obligation bond debt, the amount of general obligation bond debt a school is allowed to take on is limited by statute to ensure sufficient ad valorem tax revenues exist to satisfy it. See Education Code § 15270, § 15268, § 15102, 15106, 15270, etc. See also 56 Cal. Jur.

3d Schools § 126.

A. This Court Should Distinguish *Wilson* Upon Which *McGee III* is Based

In *McGee III* the trial court entered judgment dismissing taxpayers' in personam conflict of interest claims because the challenged projects had all been completed, which it held rendered the reverse validation action moot based on *Wilson & Wilson v. City Council of Redwood City* (2011) 191 Cal.App.4th 1559.

The facts of *Wilson* are that a law firm brought an action against " the City Council of Redwood City (City Council), the City of Redwood City (Redwood City), and the Redwood City Redevelopment Agency (Redevelopment Agency) (hereafter collectively the City)[6] to challenge the approval and construction of a retail-cinema redevelopment project in Redwood City's downtown. Plaintiff Wilson asked the court to invalidate resolutions enacted by the City Council and the Redevelopment Agency and to void agreements entered into by the City to carry out the redevelopment." *Id.* at 1563. ***Nowhere in Wilson is a***

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Neither the party that received the money from the city under the allegedly illegal contract nor "All Persons Interested" in the action are recognized by the Wilson Court as being parties to the action. They would have to be parties to the action in order to grant disgorgement relief which is the remedy for illegal public entity contracts.

void contract disgorgement remedy sought against a defendant named in that action. Instead, the prayer for relief "requested that the court direct the City Council and the Redevelopment Agency to seek reimbursement "for all monies illegally and improperly spent on the Project." *Id.* at 1567. The foregoing relief is a remedy the *Wilson* Court could not grant because "[i]t has long been held that a government entity's decision whether to pursue a legal claim involves the sort of discretion that falls outside the parameters of waste under section 526a and cannot be enjoined by mandate *Daily Journal Corp. v. County of Los Angeles* (2009) 172 Cal.App.4th 1550, 1558. Instead the only relief the *Wilson* plaintiffs could obtain involved whether the developmental entitlements were proper since the party who received those entitlements was not a party to the action.

Plaintiff McGee argued on appeal the trial court was wrong because (1) the lease-leaseback agreements were not subject to validation; (2) his conflict of interest claims were in personam claims separate from his in rem reverse validation claims; and (3) the court could have ordered disgorgement as a remedy even though the projects have been finished. *Id.* at 819. The Court of Appeal rejected McGee's contentions and held the challenged lease-leaseback construction contracts were subject to validation and his conflict of interest claims moot because the subject construction projects had been built. *Id.* The *McGee III* Court said allowing McGee's claims to proceed after the projects

finished would undermine the strong policy of promptly resolving the validity of public agency actions. *Id.*

In support of its mootness analysis the *McGee III* Court relied on *Wilson & Wilson v. City Council of Redwood City* (2011) 191 Cal.App.4th 1559. However, this case and *McGee* are distinguishable from *Wilson* because *Wilson* did not involve concurrent in personam claims for disgorgement based on void public contracts against a defendant who had appeared in the case and against whom the court could grant effectual relief. Here, such defendants are present and such relief can be granted.

B. McGee's Mootness Conclusion Cannot Be Reconciled with Supreme and Appellate Opinions That Allow Disgorgement of Public Funds Received Via Conflicted Contracts After The Subject Contracts Are Fully Performed and Fully Paid

The *McGee III* Court quotes from *Wilson & Wilson v. City Council of Redwood City* (2011) 191 Cal.App.4th 1559, 1575 for the proposition "California law has long recognized that the completion of a public works project moots challenges to the validity of the contracts under which the project was carried out" is incorrect because those cases are factually and legally distinguishable from this case. As authority for the foregoing proposition *Wilson* relies on *Jennings v. Strathmore Public etc. Dist.* (1951) 102 Cal.App.2d 548, 549-550. Unlike this case, neither *Wilson* nor *Jennings* were adjudicating a disgorgement claim based on void contract and had a defendant over whom the court had in personam jurisdiction to enter a judgment for

disgorgement. For this reason alone *Wilson* and *Jennings* should be rejected because an appellate court's opinion "is to be understood in the light of the facts and issue then before the court, and an opinion is not authority for a proposition not therein considered" *Kirk v. First American Title Ins. Co.* (2010) 183 Cal.App.4th 776, 797. Further, there was no defendant named in *Wilson* or *Jennings* from whom monetary damages could be obtained. Neither case is on point.

Second, the McGee Court improperly generalizes *Wilson's* statements into a universal rule of law that 'completion of a project always moots a reverse validation action.' *Wilson* will not bear that weight, and did not purport to announce any such universal rule. The flaw in the *McGee III* Court's reasoning is that it assumes that all reverse validation actions are the same for purposes of mootness, and it tries to treat "mootness" as some kind of idealized quality independent of the nature of the facts and issues of the action at hand.

Mootness is really just shorthand for "is there any meaningful relief that can still be granted?" As *Wilson* put it, "The pivotal question in determining if a case is moot is therefore whether the court can grant the plaintiff any effectual relief. If events have made such relief impracticable, the controversy has become 'overripe' and is therefore moot." *Id.* at 1574 (citations omitted).

In *Wilson*, the relief granted by the trial court consisted of a retroactive invalidation of certain public contracts, and a

declaration that the city had lacked authority to enter into them. *Id.* at 1571. (There were also some prospective items of relief, but the court separately held that they were unripe.) The relief granted was therefore in the nature of historical criticism of the city's now-completed actions, but without any real-world, present-day consequences. In other words, it was moot. However, as *Wilson* recognizes, mootness must be judged in light of the relief sought. If there remains relief available that would still be meaningful, the case is not moot. And that is precisely why *Wilson* will not bear the weight the McGee Court ascribes to it and it must be reviewed.

Likewise, *Jennings* to which *Wilson* cites for its proposition "California law has long recognized that the completion of a public works project moots challenges to the validity of the contracts under which the project was carried out" was unable to provide any meaningful relief to the Plaintiff who sought to stop a construction project and obtain a declaration that higher wage rates were required. Because no defendant was named against whom a judgment for higher wage rates could be entered and the project sought to be stopped was completed, the *Jennings* plaintiff's claims were deemed moot since no meaningful/effectual relief could be granted.

Here, Taxpayer seeks a form of relief that is neither meaningless nor moot today, namely disgorgement of the funds

Builder [7] received from District under the conflicted contracts. It is analogous to saying that while it may be moot to seek an injunction against a completed trespass, one may still seek damages for it. Hence, in the context of this case, the question "is it moot?" can be rephrased as, "is disgorgement an available remedy, notwithstanding that the challenged contracts have been fully performed?"

On this question the McGee Court is in direct conflict with this Court in *Thomson v. Call* (1985) 38 Cal.3d 633. Government Code § 1090(a) prohibits officers or employees [including consultants] from being "financially interested in any contract made by them in their official capacity." This Court and the Appellate Courts cited above held disgorgement is available - indeed, required - in a § 1090 action even after completion of the project. In *Thomson* this Court expressly stated contrary to the McGee Court "the primary issue presented by this case: what is the appropriate remedy where a fully executed and performed contract has been found to violate section 1090?....the city or agency is entitled to recover any consideration which it has paid, without restoring the benefits received under the contract." *Id.* at 646-647.

V. EVEN IF THE CHALLENGED CONTRACTS FALL

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[7] Builder was a named defendant over whom the Superior Court had in personum jurisdiction based on Builder's appearance in the action and requesting for relief in its favor by way of its answer.

WITHIN THE MEANING OF GOVERNMENT CODE SECTION § 53511 TAXPAYER IS ENTITLED TO TRIAL ON HIS IN PERSONAM CLAIMS

If this Court finds the challenged contracts are subject to the Validation Statutes, which they are not for the reasons stated in *Davis* and above, Taxpayer's action should be allowed to proceed to trial because: (a) there has been no express or implied validation; (b) Taxpayer's action was filed within 60 days of District's award of the challenged contracts; and (c) Taxpayer still has justiciable in personam claims on behalf of District against Builder.

For jurisdictional purposes, civil actions and proceedings are classified as "in personam," "in rem," or "quasi in rem," depending on the nature of the judgment sought. *Shaffer v Heitner* (1977) 433 U.S. 186, 199. "As we have noted, under Pennoyer state authority to adjudicate was based on the jurisdiction's power over either persons or property. This fundamental concept is embodied in the very vocabulary which we use to describe judgments. If a court's jurisdiction is based on its authority over the defendant's person, the action and judgment are denominated 'in personam' and can impose a personal obligation on the defendant in favor of the plaintiff. If jurisdiction is based on the court's power over property within its territory, the action is called 'in rem' or 'quasi in rem.' The effect of a judgment in such a case is limited to the property that supports jurisdiction and does not impose a personal liability on the property owner, since he is not before the court." *Id.*

An action that seeks to impose a personal liability or obligation on the defendant is an in personam action, and the court must have jurisdiction over the defendant. *Kulko v Superior Court* (1978) 436 U.S. 84, 91. A court has personal jurisdiction over a defendant that has made a general appearance in the action. CCP § 410.50(a) (general appearance by defendant is equivalent to personal service of summons on that defendant); *In re R.L.* (2016) 4 Cal.App.5th 125, 148 (general appearance constitutes consent to court's personal jurisdiction regardless of any prior defect in notice); *Marriage of Obrecht* (2016) 245 Cal.App.4th 1, 6 (unlike subject matter jurisdiction which cannot be conferred by consent, personal jurisdiction may be conferred by defendant's consent manifested in various ways, including a general appearance); *Sierra Club v Napa County Bd. of Supervisors* (2012) 205 Cal.App.4th 162, 171 (general appearance waives any irregularities and is equivalent to personal service of summons); *Serrano v Stefan Merli Plastering Co., Inc.* (2008) 162 Cal.App.4th 1014, 1028 (court acquires personal jurisdiction over defendant that makes general appearance in action even if no summons was served on that defendant). It has long been the rule in California that a defendant waives any objections to the court's exercise of personal jurisdiction by making a general appearance in the action. *Air Mach. Com SRL v Superior Court* (2010) 186 Cal.App.4th 414, 419.

A defendant makes a general appearance by (1) appearing in the action without limiting the purpose of the appearance, or

(2) asking for relief that only a court with personal jurisdiction over the defendant can give. *Greener v Workers' Comp. Appeals Bd.* (1993) 6 Cal.4th 1028, 1036–1037. A defendant may preserve objections to personal jurisdiction only by making a special appearance, i.e., an appearance for the sole purpose of objecting to the court's jurisdiction. A special appearance does not confer jurisdiction on the court for any purpose other than determining the question of jurisdiction over the defendant. *Marriage of Obrecht*, supra, 245 Cal.App.4th at 6.

Here the Court had personal jurisdiction over Builder and District because both made general appearances by filing general denials, participated in the action on the merits through this appeal. The fact that the challenged contract had been completed and Builder had been paid in full from District by the time Taxpayer's claims were ready to be tried did not divest the Superior Court's personal jurisdiction over Builder nor preclude it from determining the subject contracts to be void ab initio and ordering Builder to disgorge all payments received thereunder back to District.

This Court and the Appellate Courts have heretofore uniformly allowed disgorgement of funds received after completion of a void contract. See e.g. *Miller v. McKinnon* (1942) 20 Cal.2d 83; *Thomson v. Call* (1985) 38 Cal.3d 633; *Gilbane Building Co. v. Superior Court* (2014) 223 Cal.App.4th 1527; and *Strategic Concepts, LLC v. Beverly Hills Unified School Dist.* (2018) 23 Cal.App.5th 163, as modified on denial of reh'g (June 6,

2018). No case has ever found void contract disgorgement action where there was in personam jurisdiction over the recipient of the public funds moot as the *McGee III* Court did because each has recognized disgorgement is an effective remedy that can be awarded even after a void contract was fully performed and fully paid for. Each of the grounds cited in the *McGee III* Court for its conclusion are legally incorrect and can be dispelled such that the McGee Court is an outlier that cannot be reconciled with current law.

In an abundance of caution Taxpayer filed each of their complaints for disgorgement within 60 days of contract award so they could not be argued to be time barred by the validation statutes. Consequently, there can be no argument of an untimely challenge as was the case in *California Commerce Casino, Inc. v. Schwarzenegger* (2007) 146 Cal.App.4th 1406, 1420 and *McLeod v. Vista Unified School Dist.* (2008) 158 Cal.App. 4th 1156, 1166. Likewise, no other party filed a validation action and obtained a final judgment thereon. Consequently there could be no argument of res judicata as was the case in *Colonies Partners, L.P. v. Superior Court* (2015) 239 Cal.App. 4th 689,693-694 and *San Bernardino County v. Superior Court* (2015) 239 Cal.App.4th 679,682-687. Further, there is no outside statute of limitations by which Taxpayer claims had to adjudicated other than the 5 year rule of Code of Civil Procedure § 583.310 which has not triggered here on account of tolling due to the appeals in *Davis I* and *Davis II.*

This interpretation of the Validation Statutes is required and is good public policy because the purpose of the Validation Statutes is the protection of the public fisc not the protection of private parties who illegally obtain money from the public fisc by way of contracts or other actions that are void ab initio.

VI. BY SUING ON BEHALF OF DISTRICT TAXPAYER'S IN PERSONAM CLAIMS AGAINST BUILDER CAN PROCEED UNDER CODE OF CIVIL PROCEDURE § 869 EVEN IF THE CHALLENGED CONTRACTS FALL WITHIN THE MEANING OF GOVERNMENT CODE SECTION § 53511

If this Court finds the challenged contracts are subject to the Validation Statutes, which they are not for the reasons stated in *Davis* and above, Taxpayer should be deemed an agent of District and Taxpayer's in personam claims against Builder should be allowed to proceed to trial under Government Code § 869. Government Code § 869 provides:

> No contest except by the public agency or its officer or agent of any thing or matter under this chapter shall be made other than within the time and the manner herein specified. The availability to any public agency, including any local agency, or to its officers or agents, of the remedy provided by this chapter, shall not be construed to preclude the use by such public agency or its officers or agents, of mandamus or any other remedy to determine the validity of any thing or matter.

It is well settled that money paid under a void contract may be recovered in a suit filed by a taxpayer on behalf of the

governmental agency involved . *Miller v. McKinnon* (1942) 20 Cal.2d 83, 96. Just as here, in *Miller* "Plaintiff, as a citizen resident and taxpayer of Santa Clara County, commenced in his name on behalf of the county, an action against a partnership doing business under the name of Nash Englehardt Silva Mfg. Co., and the members thereof, and certain county officers to recover money claimed by him to have been illegally expended by the county and received by the partnership. He also named the county as a defendant." *Id.* at 86. "As heretofore pointed out, however, a cause of action exists to recover from the person receiving the money illegally paid, independent of any statute, and it is also clear that **the action may be prosecuted by a taxpayer in his name on behalf of the public agency**. See Mock v. City of Santa Rosa, 126 Cal. 330, 58 P. 826; Osburn v. Stone, supra; Hansen v. Carr, supra; Newton v. Brodie, 107 Cal.App. 512, 290 P. 1058; Briare v. Matthews, 202 Cal. 1, 258 P. 939 [emphasis added]." *Id.* at 86.

Here, Taxpayer specifically alleged in his FAC:

> 1. **TAXPAYER brings this action on behalf of himself, the FRESNO UNIFIED SCHOOL DISTRICT,** the students, teachers and taxpayers of the FRESNO UNIFIED SCHOOL DISTRICT and all others similarly interested to contest the validity of the contracts referenced below relative to the leasing and construction of the Rutherford B. Gaston, Sr., Middle School Buildings, Phase II Project ("Project") located at 1100 E. Church Ave., Fresno, California **and recover to the FRESNO UNIFIED SCHOOL DISTRICT all monies paid by it under said contracts** (emphasis added). [AA107].

13. For over 150 years in California, the rule has been that public contracts executed without full compliance with all applicable legal requirements are: (1) void and unenforceable as being in excess of the agency's power; (2) estoppel to deny their validity cannot be asserted; and (3) quasi-contract recovery is not allowed. See, e.g., Zottman v. San Francisco (1862) 20 Cal. 96; Reams v. Cooley (1915) 171 Cal. 150; Los Angeles Dredging Co. v. Long Beach (1930) 210 Cal. 348; Miller v. McKinnon (1942) 20 Cal.2d 83, 87-88. **It is equally well settled that money paid under a void contract may be recovered in a suit filed by a taxpayer on behalf of the governmental agency involved. Id. at 96.** The Supreme Court noted "It may sometimes seem a hardship upon a contractor that all compensation for work done, etc., should be denied him; but it should be remembered that he, no less than the officers of the corporation, when he deals in a matter expressly provided for in the charter, is bound to see to it that the charter is complied with." Id. at 89. Further, contractors are presumed to know the laws relating to public contracting. Id. The rational for the Court's strict application of this doctrine is that to hold otherwise would create a disincentive for contractors and public entities to follow the law. Id. Based on the foregoing legal precedent, **TAXPAYER brings this Complaint to recover funds paid by DISTRICT to CONTRACTOR under the Lease-Leaseback Contracts for the Project on the grounds that said agreements are ultra vires void and unenforceable for their failure to comply with all applicable legal requirements under California law for the reasons set forth herein below** (emphasis added). [AA109].

15. **TAXPAYER alleges the Lease-Leaseback Contracts DISTRICT entered into with CONTRACTOR on September 26, 2012 were not awarded in the manner required by law and are**

> **therefore ultra vires, illegal, void and/or unenforceable such that any monies paid by the DISTRICT to CONTRACTOR thereunder must be paid back by CONTRACTOR to the DISTRICT. By this action TAXPAYER seeks a judgment on behalf of DISTRICT against CONTRACTOR for the amount money paid by the DISTRICT to CONTRACTOR under the challenged contracts.** Further, TAXPAYER requests DISTRICT make no further payments to CONTRACTOR under the Lease-Leaseback Contracts pending the disposition of this action (emphasis added). [AA110].

In his FAC Taxpayer prayed for judgment on each of his causes of action, inter alia, as follows [AA125-126]:

> 3. That the Court find and declare the Site Lease, attached hereto as Exhibit "B" and Facilities Lease, attached hereto as Exhibit "C" are ultra vires, illegal, void, and/or unenforceable:
>
> 4. That CONTRACTOR be ordered to pay back to DISTRICT all monies received under the Site Lease, attached hereto as Exhibit "B" and Facilities Lease, attached hereto as Exhibit "C"

Based on the foregoing allegations, Taxpayer was an agent of District authorized by this Court to bring his action on its behalf against Builder to recover to District all monies it paid to Builder under the challenged contracts which were ultra vires, illegal, void, and/or unenforceable for the reasons stated in the FAC. As an authorized agent of District, Taxpayer's in personam claims against builder can proceed under Code of Civil Procedure § 869.

This interpretation of Code of Civil Procedure § 869 is

required and is good public policy because the purpose of the Validation Statutes is the protection of the public fisc not the protection of private parties who illegally obtain money from the public fisc by way of contracts or other actions that are void ab initio.

VII. PETITIONERS BRIEFS ON THE MERITS RELATING TO EDUCATION CODE § 17406 IMPROPERLY EXCEED ISSUE ON WHICH THIS COURT GRANTED REVIEW

Taxpayer has filed an objection and motion to strike Petitioners' attempt to raise, in violation of California Rule of Court 8.516(a)(1) and 8.520(b)(3), issues involving the interpretation Education Code § 17406 unrelated to the issue on which this Court granted review, namely "Is a lease-leaseback arrangement in which construction is financed through bond proceeds, rather than by or through the builder, a 'contract' within the meaning of Government Code section 53511?" Taxpayer's objection and motion to strike should be granted.

Without waiving the foregoing objection and motion to strike, and subject thereto, Taxpayer asserts *Davis I*'s interpretation of Education Code § 17406 is well reasoned at pp. 275-290, speaks for itself and constitutes sound public policy. What is more, In 2016 the Legislature amended Education Code § 17406 after *Davis* I by way of AB 2316, effective January 1, 2017, to add a "best value" contractor selection procedure specifically laid out in the amended statute. Under the amendment proposals are now required in response to a request for proposals

(RFP) published by a school district and the proposals are to be ranked by way of a pre-defined scoring system. Taxpayer is critical of 'competitive selection process' because the identity of the proposers is still known and a thumb can be placed on the scale to tilt it still to the favorite contractor. In addition their were some get out of jail free provisions for prior law breakers added by way of AB 2316 that Taxpayer contends are of questionable constitutionality.

The foregoing weaknesses aside what is most important for this Court's analysis is that the Legislature made no changes to 17406 to address any of the criticisms Petitioners raise with regard to *Davis I*'s interpretation of Education Code § 17406. Therefore the Legislature has acquiesced to *Davis I*'s interpretation. *People v. Bouzas* (1991) 53 Cal.3d 467, 475 "When a statute has been construed by the courts, and the Legislature thereafter reenacts that statute without changing the interpretation put on that statute by the courts, the Legislature is presumed to have been aware of, and acquiesced in, the courts' construction of that statute."

CONCLUSION

Based on 50 years of precedent and sound public policy this Court should conclude a lease-leaseback arrangement in which construction is financed entirely through District's general obligation bond proceeds already on hand rather than by or through the builder is not a "contract" within the meaning of Government Code § 53511 and not subject to the limitations and immunities afforded by Government Code §§ 860-870 (the

"Validation Statutes"). This was the conclusion in *Davis v. Fresno Unified Sch. Dist.*, (2020) 57 Cal.App.5th 911 ("*Davis II*") which is well reasoned and should be affirmed by this Court.

DATED: July 2, 2021

/s/ Kevin R. Carlin
Kevin R. Carlin
Attorneys for
Respondent
Stephen K. Davis

CERTIFICATE OF WORD COUNT

Pursuant to California Rules of Court, rule 8.520(c)(I), the text of this Respondent Stephen K. Davis' Answering Brief On The Merits, including footnotes and excluding the cover information, table of contents, table of authorities, signature blocks, and certificate, consists of 11661 words in 13-point Century Schoolbook type. In making this certification, I have relied on the word count of the Corel WordPerfect program used to prepare the brief.

DATED: July 2, 2021

/s/ Kevin R. Carlin
Kevin R. Carlin
Attorneys for
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Stephen K. Davis

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I am a citizen of the United States and a resident of the County aforesaid; I am over the age of eighteen (18) years and not a party to the within-entitled action. My business address is 4452 Park Boulevard, Suite 310, San Diego, CA 92116. On July 20, 2021, I served the within document(s):

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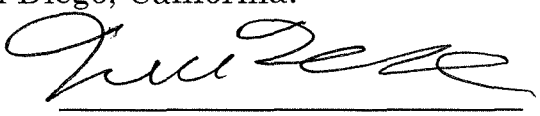
Via U.S. Mail Honorable Kimberly Gaab Fresno County Superior Court 1130 "O" Street Fresno, CA 93721	*Via U.S. Mail* Fifth District Court of Appeal 2424 Ventura Street Fresno, CA 93721

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

Executed on July 2, 2021, at San Diego, California.



Duane Besse

STATE OF CALIFORNIA
Supreme Court of California

PROOF OF SERVICE

STATE OF CALIFORNIA
Supreme Court of California

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Case Number: **S266344**
Lower Court Case Number: **F079811**

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I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

7/2/2021

Date

/s/Duane Besse

Signature

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