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California Supreme Court dismantles no-bid school construction contracts



BY DAN WALTERS MAY 3, 2023

Last week, the California Supreme Court [issued a unanimous decision](#) in a very complex – but very important – case that had been percolating for more than a decade, dealing with how local school officials evade competitive bidding on construction projects.

The case began in 2010 when Fresno Unified School District persuaded its voters to approve a bond to build new schools and upgrade old ones. In 2011, the district sold more than \$100 million in bonds from that issue and an earlier one, and in 2012 awarded a \$36.7 million contract for a new middle school to Harris Construction Co.

The contract with Harris, which had been a major contributor to the bond issue campaign, was structured as a “lease-leaseback” deal in which the district leased the school site to Harris for a nominal sum, Harris built the school and the district then leased the completed facility from Harris.

“Lease-leaseback” arrangements have been common for years, providing a way for school systems to build new facilities without borrowing money themselves. Typically the “leaseback” runs for several decades, after which the district becomes the owner.

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In the Harris project, however, Fresno Unified made payments to the contractor and once the school was completed in 2014, it used bond funds to immediately acquire ownership from Harris. Meanwhile, another contractor, Stephen Davis, had sued the district alleging that the Harris lease-leaseback deal was a subterfuge to avoid competitive bidding.

The district won two rulings from a local trial judge that the deal was legitimate, but both were overturned by a state appellate court and eventually Fresno Unified asked the state Supreme Court to determine whether the Harris deal was a legitimate contract protected under state law. Last week, the court declared that it was not, [sending the case back down](#) the legal ladder to determine what damages will be assessed.

San Diego attorney Kevin Carlin, who represents Davis and has carved out a niche career of challenging questionable school contracts, says that Harris Construction may be forced to pay back the \$36.7 million it received for building Gaston Middle School.

The case has reverberated in other ways. The superintendent who approved the contract, Michael Hanson, [was fired by the school board](#) after the suit was filed. Critics cited Hanson's close personal relationship with Harris Construction's president, Michael Spencer, including the firm's sponsorship of a gala event to honor Hanson, and the hiring of Harris as a consultant before the contract was awarded.

The FBI launched an investigation, although nothing official came of it. However, when Davis started winning his case, it sent shudders through other school districts that had used lease-leaseback in the same questionable manner.

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In 2015, just a week after an appellate court ruled against the Harris contract, a lawyer for affected companies, P. Randolph Finch, [outlined a plan “to mitigate our losses”](#) by seeking legislation to legitimize questionable contracts.

“We have clients with well over a half-billion dollars of current backlog,” Finch wrote, “and another billion in completed projects, at risk on the Davis case. Consequently, we need a devoted industry effort to press these legislative changes.”

Using a parliamentary loophole known as “gut-and-amend,” a [bill to absolve contractors of liability](#) was drafted, but never enacted.

In 2004, the staff of the State Allocation Board, which parcels out school construction money, had described how lease-leaseback rules were being distorted, questioned the legality, and declared “the integrity of the use of general obligation bonds...must be above reproach,” and suggested that the lease-leaseback law be clarified.

Officialdom ignored that warning but now the Supreme Court is telling school officials and contractors to play fair or suffer the consequences.