

New Case Confirms Competitive Bidding Exception for Lease-Leaseback Projects Award by School Districts

A court of appeal case published on September 18, 2014, *Los Alamitos Unified School District v. Howard Contracting, Inc.*, confirmed the existence of an exception to competitive bidding for “lease-leaseback” agreements awarded by school districts pursuant to Education Code section 17406. Many involved in school district construction have held the view that “lease-leaseback” agreements were exempt from competitive bidding, despite the fact that these agreements result in new construction projects which are ultimately owned by a school district. This case confirms that view by applying a plain meaning interpretation of section 17406. In the court’s words:

The primary issue presented by this appeal is a legal one: Does Education Code section 17406 exempt school districts from obtaining competitive bids when entering into what are known as “lease-leaseback” agreements to improve school property? We conclude the answer is yes. More than 40 years ago, the California Attorney General concluded the language of the statute is plain, unambiguous, and explicit, and does not impose bid requirements on school districts. We agree, and nothing has occurred in the interim that would change our conclusion.



by David S. Gehrig

Lease-leaseback agreements by school districts involve two separate lease agreements: 1) a ground lease awarded by the district to a contractor, normally for \$1 a year; and 2) the lease of the new facility being constructed by the contractor. The term of both lease agreements generally expires after the completion of the construction, and the lease payments to the contractor are established in an amount to pay for construction costs and the contractor’s profit. Effectively, a lease-leaseback agreement is a construction contract couched as lease agreements.

Education Code section 17406 states clearly that competitive bidding is not required for lease-leaseback agreements awarded by school districts:

Notwithstanding Section 17417, the governing board of a school district, without advertising for bids, may let, for a minimum rental of one dollar (\$1) a year, to any person, firm, or corporation any real property therein to construct on the demised premises, or provide for the construction thereon of, a building or buildings for the use of the school district during the term thereof, and provides that title to that building shall vest in the school district at the expiration of that term. The instrument may provide for the means or methods by which that title shall vest in the school district prior to the expiration of that term, and shall contain such other terms and conditions as the governing board may deem to be in the best interest of the school district.

Despite the clear language in section 17406, the plaintiff contractor challenged the school district's award of a lease-leaseback agreement to a competitor as violating competitive bidding requirements for construction projects awarded by school districts. Plaintiff raised several arguments, including: 1) the exception to competitive bidding only applies to the site lease, not the facility lease which includes the construction work; and 2) Education Code section 17417, which requires school districts to competitively bid construction work, should take precedence over section 17406. The court was not persuaded by either argument. The court also pointed to an unsuccessful attempt by the legislature to remove the exception to competitive bidding from section 17406 in 2004 as further proof that lease-leaseback agreements do not require competitive bidding.

Los Alamitos Unified School District v. Howard Contracting, Inc. goes a long way toward resolving any ambiguity regarding the necessity of competitive bidding for school district lease-leaseback agreements. However, it should be noted that this is still just one appellate court decision. For school districts within the 4th appellate district's boundaries (San Diego, Imperial, Orange, San Bernardino, Riverside and Inyo counties), the issue has been resolved for the time being. In other districts, this case provides very strong authority that the process is legal, unless and until an appellate court in another district addresses the same issue and comes to a different conclusion. In an abundance of caution, a school district might still want to consider a validation action in order to ward off any challenge to a lease-leaseback award. It is also possible that this case could be appealed to the California Supreme Court, or that the legislature could amend section 17406 in an attempt to bring it in line with other public agency statutes requiring competitive bidding for construction work.

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