

O.C. schools skirt bidding rules

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In early May 2008, an employee of Los Alamitos Unified tacked up a notice at the public library in downtown Seal Beach.

The school district, it announced, had sued local residents.

The fine print revealed more: The district had hired an out-of-town construction firm to remodel an elementary school, and anyone opposed was ordered to respond quickly in court with a lawyer.

School officials opted for this strange legal maneuver so they could hire the company without trying to find other firms that would charge less or do better work – which is required by state law. When no one showed up in court, the school district had the judge sign an order declaring that no one could ever challenge the no-bid deal.

"It was all done secretly," said Stan Howard, a 27-year resident of Los Alamitos and the owner of Howard Contracting, which has done dozens of school construction jobs. "I'm a taxpayer and this isn't right."

The 2008 deal was the first of at least eight projects that Los Alamitos Unified awarded to West Coast Air Conditioning through contracts that sidestepped competitive bidding, which is considered a safeguard against inflated pricing. The total cost of those deals: more than \$100 million.

Across the state, roughly 18 percent of all school construction projects in the last five years were arranged using these complex transactions. Known as lease-leaseback contracts, they involve schools leasing a property to a developer and then subleasing it back.

The deals have rewarded a small group of contractors, law firms and architects that have aggressively promoted them to schools at conferences and cocktail parties. But taxpayers will never know just how much their schools could have saved by opening the jobs up to bids by all companies qualified for the work.

Los Alamitos is one of six Orange County school districts that have agreed to one or more of the deals in the last five years, according to the state Office of Public School Construction. Nine of those 16 contracts were signed last year. The other districts are Anaheim City, Cypress, Placentia-Yorba Linda, Saddleback Valley and Savanna.

Soon after being hired in 2008, the San Diego County-based West Coast Air showed its appreciation to Los Alamitos officials. The company donated \$25,000 to the political

campaign that worked to pass a school bond measure in late 2008. The school then gave the company at least seven more building projects.

West Coast also donated \$2,500 toward the cost of a bowling and country club party for principals and staff, district records show. Last year, it and another firm treated at least one board member, Dr. Jeffrey Barke, to a \$175 round of golf, with lunch and dinner included.

"It's too big of a coincidence that you make a contribution and then you pick up all this work," said Paul Mahoney, a lawyer who represents Howard in a legal challenge against the district.

In court papers, Howard and Mahoney allege that the deals are unlawful and costing taxpayers hundreds of thousands of dollars.

"The entire procedure is illegal and unconstitutional because it involves an improper expenditure of public funds," they argued in their civil lawsuit in Orange County Superior Court. "It is nothing more than a blatant effort to bypass competitive bidding."

David Dudley, West Coast Air's president, did not return calls for comment. But Los Alamitos Superintendent Sherry Kropp said West Coast's donations had nothing to do with the district's decision to hire it. "We chose who we thought was best for the job," she said.

At a court hearing last week, the school's lawyers argued that the district had properly followed the law and that no money had been wasted. By choosing the lease-leaseback method of construction, they said, the district had no duty to seek lower bids. They asked the judge to throw out Howard's case.

"Howard has no evidence of any District wrongdoing," the school's lawyers wrote, "nor can Howard prove that the District violated any statute."

OLD LAW, NEW PURPOSE

The state law allowing such deals has been part of the Education Code since 1957. But lawyers working for schools have recently put it to new use.

In their original and intended form, the lease-leaseback contracts gave schools a key advantage that made it easier to build classrooms.

A school could rent a site to a construction firm for \$1 a year. The company then built a new school on the property, financing the project with its own money. The school then subleased the property back from the developer, making rental payments over as many as 40 years. The schools avoided taking on debt to pay for the construction.

The deals don't work this way today. Rather than having developers pay for the

construction, schools pay for it with taxpayer-financed bonds. The contractors are paid as the work is done.

The primary benefit of the deals to schools today is that they avoid competitive bidding, which officials say can result in the hiring of inexperienced contractors who don't perform well.

Yet such open bidding is required by state law because it generally leads to lower prices, stimulating competition between companies qualified to do the work.

"Why are they afraid of competition?" asked Kevin Carlin, a lawyer who has sued several school districts over the deals. "If you avoid competitive bidding, you have opportunity for fraud, favoritism, public corruption and misuse of public funds."

Carlin said the schools were wrongly using an ambiguity in the law to avoid searching for better offers.

In a deposition last month, Mahoney asked Patricia Meyer, deputy superintendent at Los Alamitos, how she knew that another contractor of equal ability couldn't have done the work for less money.

"Cheaper?" Meyer asked Mahoney.

"Right," Mahoney responded.

"How would I know that?" Meyer said. "I don't know that."

SELLING 'A PROVEN METHOD'

Hundreds of California school officials learned about the lease-leaseback approach to building new classrooms at a May 2003 conference at the Wyndham hotel in downtown San Diego. Andreas Chialtas, a lawyer from Cerritos-based Atkinson, Andelson, Loya, Ruud & Romo, told the crowd that the deals were "a proven method" of constructing schools.

Chialtas explained that the deals gave schools "great latitude" in hiring companies. "In fact, no selection or request for proposal process whatsoever is required," Chialtas explained in a paper distributed to the audience.

Since then, other firms have promoted the deals at conferences put on by groups like the Coalition for Adequate School Housing, where school officials mingle with legal and financial executives looking for new business.

A conference in April of the California Association of School Business Officials included an hourlong seminar on lease-leasebacks. That night, school officials enjoyed food, cocktails and entertainment in corporate hospitality suites, followed by a "gala cabaret

and casino night" at the Renaissance in Long Beach. The event was heavily subsidized by companies, including Lozano Smith, a law firm that advises schools about the contracts.

Meyer said Los Alamitos officials became interested in the leaseback contracts after hearing about them at conferences and from other schools.

Chialtas' firm first gave a presentation on the deals to Los Alamitos officials in 2005, Meyer said. The district has since paid the firm fees as high as \$230 an hour for drafting the myriad documents required for each construction project.

Chialtas didn't reply to repeated calls seeking comment.

In a newsletter last year, Meyer touted the continuing success of the district's construction efforts. "All the modernization projects are 'On Time and On Budget,' she wrote, "and are helping our students and teachers enjoy a 21st Century learning environment."

Her note echoed what companies promoting the deals use as a selling point: the contracts have a fixed price that keeps projects on budget by requiring the developer to cover unanticipated costs.

But a review of the contracts signed between Los Alamitos and West Coast Air show that the so-called "guaranteed maximum price" is not guaranteed. Instead, the school gave the company several ways to ask for more money, which it did repeatedly.

For example, the maximum price to remodel McGaugh Elementary, according to the agreement approved by the school board on May 27, 2008, was \$11.9 million. The "guaranteed maximum" was then increased at least twice – to more than \$15 million – a 26 percent increase.

Kropp explained that the district has repeatedly found problems after breaking ground on its many projects that raised the expected costs. The district handles the increases in the "guaranteed maximum price" just like other schools using leaseback contracts, she said.

TRUCKS FROM OUT OF TOWN

Lawyers working for the schools know the agreements stretch the law's limits. That's why they have encouraged schools to file the pre-emptive lawsuits against residents. Their goal is to obtain a court decree that makes challenging the deals impossible.

In Los Alamitos, when no one appeared in court to question the deals with West Coast Air, the district's lawyers wrote an order and asked the judge to sign it. The order declared the agreements were "lawful, valid and binding" and "in the best interests" of the district. It also stated that the school did not have to award the work to the lowest

bidder as required by state contracting law.

Such an outcome is just what Chialtas had promised when he recommended the lawsuits to schools in 2003. He had explained that the court proceedings, known as "validation actions," would prevent "any would-be bidding contractor or disgruntled taxpayer" from stopping the deals.

"No claim can be made that the project is in any way unlawful," Chialtas explained.

Mahoney called the court proceedings "a sham." He said the posting of notices in small print in the Orange County Register, as well as on the wall of a library, a school and the district's offices, did not properly notify the public of the district's plans.

Michelle Tucker of the Construction Industry Force Account Council said Los Alamitos officials had pointed to the judges' orders when she called the school and asked whether companies were being hired without bidding. The council, which represents the construction industry, works to ensure governments follow the law when hiring contractors.

Tucker said she doubted that anyone who happened to see the school's posted notices would understand the complex legal language. "I've talked to attorneys who aren't familiar with these," she said of the pre-emptive suits. "In my opinion, it's almost shady."

Los Alamitos' Kropp said she couldn't discuss why the district chose to file the validation lawsuits because of the pending litigation with Howard.

Howard said he discovered that the district was hiring contractors when he noticed West Coast Air trucks parked outside of Los Alamitos High School, which is near his home.

He wanted to challenge the deals with West Coast Air, he said, but was too late. The district had already obtained a judge's order on each one.

But Howard found a similar notice for a leaseback deal that the school was proposing with Byrom-Davey, another firm from San Diego County. That agreement was for the construction of an all-weather track at Los Alamitos High. Howard and Mahoney filed a challenge to that no-bid deal in court. They argue that the contract was not only illegal, but also unconstitutional and a theft of public funds.

Howard recently bid on and won a contract for work on a similar track at Hollywood High School. He estimates that the \$3.9 million that Los Alamitos agreed to pay Byrom-Davey for the track was at least \$300,000 too high and possibly much more. In the slow economy, he said, contractors have been offering lower bids to keep crews busy.

The judge is expected to rule as soon as this week on the school's motion to have Howard's challenge dismissed.

"I've been in the competitive bidding arena for 50 years," Howard said. "I would just like all this crooked stuff to stop."