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OPINION	:	No. 79–402
of	:	June 6, 1979
GEORGE DEUKMEJIAN Attorney General	:	
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SUBJECT: PUBLIC LEASEBACK CORPORATIONS—The term “public agency” in Civil Code section 1670 does include public leaseback corporations as defined in the Government Code.

The Honorable Howard L. Berman, Assemblyman for the Forty-Third District, has requested an opinion on the following question:

Does the term “public agency” in Civil Code section 1670 include public leaseback corporations as defined in section 4220 *et seq.* of the Government Code?

CONCLUSION

The term “public agency” in Civil Code section 1670 does include public leaseback corporations as defined in section 4220 *et seq.* of the Government Code.

ANALYSIS

The question concerns so-called “leaseback” corporations. Such corporations are legal mechanisms utilized in a procedure which enables governmental entitles to acquire

capital improvements by lease arrangements which avoid the debt limitations of the state Constitution.[1] (See *Dean v. Kuchel* (1950) 35 Cal. 2d 444; 48 Ops. Cal. Atty. Gen. 110 (1966); 56 Ops. Cal. Atty. Gen. 572, 575–577, 585 (1973).)

Under this procedure a governmental entity conveys realty to a corporation pursuant to an agreement whereby the corporation is to construct a building or other facility to the specifications desired by the governmental entity and then lease back to the governmental entity the property and the structures at an agreed rental. The project is financed by bonds which are issued by the leaseback corporation. (Rogers, *Municipal Debt Restrictions and Lease-Purchase Financing* (1963) 49 ABA J. 49, 52, see also Kosel, *Municipal Debt Limitation in California* (1977) 7 Golden Gate I. Rev. 641, 654.) This procedure is held not to be violative of the constitutional debt limitation provisions on the theory that the governmental entity is at no time liable for the aggregate amount of the lease but only for the amount of each individual rental payment as it becomes due. (*Dean v. Kuchel*, *supra*, 35 Cal. 2d at pp. 446–448; 48 Ops. Cal. Atty. Gen. 110, *supra*.)

Several aspects of construction contracts awarded under such public leaseback arrangements are governed by Government Code section 4220-4224[2]. Those sections provide for the payment of prevailing wages, for the giving of notice of the time and place for opening bids, and procedures for the withdrawal and rejection of bids.

Several of the major terms used in these provisions are defined in section 4220 which provides:

> "As used in this chapter:
>
> "(a) 'Public leaseback' means any lease by a public entity, as lessee, of buildings, structures, or other facilities which are permanently attached to land, where the lease is between the public entity and a public leaseback corporation, as lessor, and the lease is executed before the buildings, structures or facilities have been built.
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> "(b) 'Public entity' means any city, charter city, city and county, county, district, public corporation, or political subdivision of the state.

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[1] Article XVI. section 1 of the California Constitution prohibits the state Legislature from incurring debts exceeding $300,000 without approval by the electorate.

Similarly, article XVI, section 18 of the Constitution prohibits, without such electoral approval. specified local government entitles from incurring debts exceeding their yearly income and revenue.

[2] Hereafter all section references are to the Government Code unless otherwise specified.

> "(c) 'Public leaseback corporation' means any corporation or nonprofit corporation organized or controlled by a public entity which constructs or arranges for the construction of buildings, structures, or other facilities which are permanently attached to land for public leaseback.
>
> "(d) 'Public projects' means the construction of buildings, structures, or other facilities which are permanently attached to land."

Section 1670 of the Civil Code also relates to public construction contracts and provides:

> "Any dispute arising from a construction contract with a public agency, which contract contains a provision that one party to the contract or one party's agent or employee shall decide any disputes arising under that contract, shall be resolved by submitting the dispute to independent arbitration, if mutually agreeable, otherwise by litigation in a court of competent jurisdiction."

The question at issue here is whether a "public leaseback corporation," as defined in section 4220(c), is a "public agency" as that term is used in Civil Code section 1670 which governs the resolution of public agency construction contract disputes.

Prior to the enactment of Civil Code section 1670 in 1978 (Stats. 1978, ch. 1374, § 1, p. –) governmental entitles often incorporated in their construction contracts a provision authorizing an agent of the governmental agency to decide disputes arising under the contract and making such decision final and conclusive. See *Zurn Engineers v. State of California ex rel. Dept. Water Resources* (1977) 69 Cal. App. 3d 798, 802, 808 fn. 8; Legislative Counsel's Digest, SB. 2197 (1978); 10 Pacific L.J. 300 (1979). The validity of such unilateral determination clauses was confirmed in *Zurn Engineers v. State of California ex rel. Dept. Water Resources, supra*, 69 Cal. App. 3d at 823–824, 828. By providing for independent arbitration or litigation to resolve contract disputes, Civil Code section 1670 nullified these unilateral determination clauses. (See 10 Pacific L.J., *supra*, 301–302.)

From this background it is apparent that the purpose of Civil Code section 1670 was to relieve building contractors of the constraints of those contractual clauses which allowed the government agency for which the project was constructed to unilaterally resolve contract disputes.[3]

[3] The statute was enacted in response to the *Zurn* case, *supra*, and was supported by contractors groups. (See *How AGC's Zurn Bill Became Law*, the California Constructor (Sacramento, Calif.

"Taking into consideration the policies and purposes of the act, the applicable rule of statutory construction is that the purpose sought to be achieved and the evils to be eliminated have an important place in ascertaining the legislative intent . . . ." (*Freedland v. Greco* (1955) 45 Cal. 2d 462, 467; see also *Judson Steel Corp. v. Workers' Comp. Appeals Bd.* (1978) 22 Cal. 3d 658, 669; *Rushing v. Powell* (1976) 61 Cal. App. 3d 597, 604.)

As already noted, public leaseback corporations are corporations which acquire land owned by a public entity on which it constructs a building or other permanent structure which is leased back to the public entity by a lease purchase agreement which does not violate the debt limit provisions of the state Constitution. Since public leaseback corporations are, by definition "organized or controlled" by the public entity (see Gov. Code § 4220), that public entity can insist upon a clause in the construction contract providing that contract disputes will be decided by the public entity or its agent whether the construction contract is let by the public leaseback corporation or the public entity directly. No reason is apparent why the Legislature's purpose of nullifying such unilateral determination clauses in public agency construction contracts would be affected by the manner in which the public agency finances the construction. The legislative target of Civil Code section 1670 is the clause in construction contracts which allows a public agency to decide contract disputes unilaterally without arbitration or litigation. We think the maxim that 'where the reason is the same, the rule should be the same" (Civil Code § 3511) is applicable here. Furthermore, if the term "public agency," as used in Civil Code section 1670, were to be construed in a manner that would exclude public leaseback corporations from that section's restrictions, such restrictions could be easily avoided by public entitles which can readily utilize the leaseback mechanism in their construction activities. As stated in *Freedland v. Greco*, *supra*, 45 Cal. 2d at 468:

> ". . . That construction of a statute should be avoided which affords an opportunity to evade the act, and that construction is favored which would defeat subterfuges, expediencies, or evasions employed to continue the mischief sought to be remedied by the statute, or to defeat compliance with its terms, or any attempt to accomplish by indirection what the statute forbids.'" (See also *People v. Hacker Emporium, Inc*. (1971) 15 Cal. App. 3d 474, 478.)

We therefore conclude that public leaseback corporations as defined in Government Code section 4220 *et seq*. are public agencies as that term is used in Civil Code section 1670.

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Oct. 1978) p. 1; 10 Pacific L.J., *supra*, 300.)