



ALASKA STATE LEGISLATURE LEGISLATIVE COUNCIL

CHAIR:

Sen. Gary Stevens

VICE CHAIR:

Rep. Bob Herron

SENATE MEMBERS:

President Kevin Meyer
Sen. John Coghill
Sen. Lyman Hoffman
Sen. Charlie Huggins
Sen. Anna MacKinnon
Sen. Peter Micciche
Sen. Lesil McGuire – alt
Sen. Cathy Giessel - alt

HOUSE MEMBERS:

Speaker Mike Chenault
Rep. Mike Hawker
Rep. Craig Johnson
Rep. Sam Kito
Rep. Charisse Millett
Rep. Mark Neuman
Rep. Steve Thompson – alt
Rep. Harriet Drummond - alt

COMMITTEE CONTACT:**Session/Interim:**

State Capitol 429
Juneau, AK 99801-1182
(907) 465-4925

Committee Aide:

Katrina Matheny
(907) 465-4713

October 6, 2016

DELIVERED VIA E-MAIL

Jeffrey M. Feldman
SUMMIT LAW GROUP, PLLC
315 Fifth Avenue S, Suite 1000
Seattle, WA 98104

Re: Procurement Decision on Contract Claim dated July 8, 2016

Dear Mr. Feldman,

I write in response to the contract claim that you submitted on behalf of 716 West Fourth Avenue, LLC, on July 8, 2016. As the Procurement Officer and the Chair of the Legislative Council, I have issued a decision on that contract claim. Pursuant to your request, I am sending this decision and the supporting materials to you electronically.

Sincerely,

A handwritten signature in black ink, appearing to be "Gary Stevens", with a long horizontal line extending to the right.

Senator Gary Stevens
Chair

Enclosures

cc: Doug Gardner
Don McClintock

PROCUREMENT OFFICER'S DECISION

The following is my Procurement Officer's Decision regarding the contract claim submitted by 716 West Fourth Avenue, LLC ("716") on July 8, 2016.¹ The Contract Claim was timely filed. For the reasons explained below, I am denying the Contract Claim.

Summary of Claim and Decision:² 716 argues that the Legislature "abandoned" its tenant duties under a lease for the building that housed the Anchorage Legislative Information Office (the "Building"), allegedly causing 716 more than \$37 million in damages. In particular, 716 asserts that the Legislature chose not to remain as a tenant due to a Superior Court's decision finding that the procurement process for the lease was flawed. This contention fails for four reasons:

First, as a matter of Constitutional law, the Legislature's lease obligations were subject to appropriations for that purpose. There can be no legislative expenditures without an appropriation.³ The Legislature appropriated funds to cover lease payments through October 2016, and the Legislature has made all payments for its tenancy up through that date. However, the Legislature chose not to appropriate funds for further lease payments consistent with its Constitutional authority. The Contract Claim does not address this non-appropriation.

Second, as a matter of contract law, 716 and the Legislative Affairs Agency ("LAA") agreed that the Legislature's lease obligations were subject to legislative appropriations.⁴ LAA satisfied its contractual obligation to provide adequate notice to 716 of the Legislature's intention to vacate the Building when the appropriated funds were exhausted. 716 is entitled to no more under the contract.

Third, 716's estoppel claim fails on its own terms. Sworn testimony makes clear that 716 knew that the lease's validity was disputed long before 716's expenditures. 716 also independently analyzed the procurement issue with counsel. 716 was aware of the procurement risk and did not rely on LAA's analysis. 716 also was not prejudiced because it now owns a renovated building (paid for, in significant part, with LAA's funds) that it can sell or re-let to others. Finally, it would be unfair to force the public to subsidize a private developer's investment after LAA already paid all rent that was due.

Fourth, 716 seeks as damages the full amount of its investment for the renovated Building plus future rent payments, but following the Legislature's departure from that Building 716 will remain as the owner and landlord. 716's damages calculation does not account for the substantial rents already paid by LAA and also does not include any value for the retained asset. Finally, no information is provided concerning 716's efforts to mitigate its alleged damages by

¹ Letter from Jeffrey M. Feldman on behalf of 716 West Fourth Avenue, LLC, dated July 8, 2016 (the "Contract Claim").

² This summary is provided for ease of reference.

³ Alaska Constitution art. IX, § 13.

⁴ The LAA handles business matters for the Legislative Council, a joint House-Senate committee, and the full Legislature.

seeking another lessee or purchaser for the Building. In short, 716's damages calculations overstate any loss. Because 716 has been paid all amounts owed under the lease, no damages are owed.

I. DESCRIPTION OF THE CONTROVERSY

A. Background

The claimant, 716, has brought a contract claim pursuant to AS 36.30.620(a)⁵ in connection with the 2013 Extension of Lease and Lease Amendment No. 3 (the "Lease") between 716 and LAA. For many years, LAA leased space at 716 West Fourth Avenue in Anchorage for use as the Anchorage Legislative Information Office ("LIO"). In 2013, LAA and 716 negotiated and agreed upon an extension and amendment of the existing lease. Both sides were represented by counsel. During the course of those negotiations, the parties discussed the application of AS 36.30.083(a), which allows the Legislative Council to extend a real property lease for up to 10 years if, at the time of the extension, a minimum cost savings of at least 10 percent below the market rental value of the real property would be achieved on the rent due under the lease. In connection with the Lease, 716 agreed to make substantial renovations to the property. This included purchasing and razing an adjacent property (located at 712 West Fourth Avenue), as well as significant improvements to many aspects of the Building. This work generally commenced in November 2013 and continued through December 2014. The renovated Building was open to the public as of January 2015. LAA has paid rent to 716 on a regular basis since the Lease commenced and did so through October 2016.

B. Budget Shortfalls and Appropriation Considerations

By mid-2015, the State was facing a budget deficit of more than \$3 billion. Following ongoing budget shortfalls, on December 19, 2015, the Legislative Council voted unanimously to recommend to the Legislature that it decline to appropriate additional funds for rent for the Building unless, within a 45-day window, 716 was able to make the Building costs more competitive as compared to other available options.⁶ In mid-April of 2016, Governor Walker indicated that he would veto an attempted purchase of the Building.⁷ The budget ultimately signed by Governor Walker contained a limited appropriation for rent for the Building – the

⁵ The Contract Claim states that it is being submitted pursuant to AS 36.30.620, which relates to contracts awarded under Chapter AS 36.30 (the State Procurement Code). While the extension portion of the lease amendment at issue was subject to the provisions of AS 36.30.083, the amendment of the lease and its award were made pursuant to the Alaska Legislative Procurement Procedures (the "Legislative Procedures"). Accordingly, pursuant to Section 350 of the Legislative Procedures the claim has been filed with me as the procurement officer. The Legislative Procedures govern the handling of the Contract Claim.

⁶ Ex. A (Alaska State Legislature, Legislative Council Meeting Minutes (Dec. 19, 2015)) at 57-60. [Note: All references to exhibit numbers refer to the exhibits included with the Contract Claim. All references to exhibit letters refer to additional documents included with this Decision.]

⁷ Ex. B (Becky Bohrer, *Walker says he'd veto Anchorage LIO purchase*, Juneau Empire (from The Associated Press) (Apr. 15, 2016; updated Apr. 17, 2016)).

appropriation would not cover the rent for all of 2016. On July 18, 2016, LAA’s executive director notified 716’s principals that the Legislature had reduced the original budget request for LAA’s lease obligations and the appropriated funds would not be sufficient to cover the annual Lease payments. LAA exercised its right to terminate the Lease pursuant to its constitutional authority and Sections 1.2 and 43 of the Lease relating to non-appropriation.

C. The Lawsuit Challenging the Lease

Shortly after the Building renovations were completed, a lawsuit was filed against 716 and LAA alleging that the Lease failed to comply with AS 36.30.083(a), a statutory provision concerning extensions of certain leases. On March 24, 2016, a Superior Court judge issued a decision finding that the Lease was invalid because it failed to comply with that statutory provision.⁸ On May 16, 2016, LAA notified 716 and 716’s lender, EverBank, that in the absence of a valid lease LAA would vacate the property and secure alternate premises in due course. A portion of the lawsuit is currently being appealed to the Alaska Supreme Court. As of the date of this Decision, no final judgment has been issued in the case before the Superior Court.

D. 716’s Claim

716 asserts that it is entitled to \$37,016,021 in reliance damages for all investments made by 716 in connection with performance of its obligations under the Lease.⁹ In particular, 716 claims that it relied upon the validity of the procurement process when borrowing and spending these funds to perform under the Lease.

II. PERTINENT CONTRACT PROVISIONS

§ 1.2 AS 36.30.083(a) COST SAVINGS:

Under AS 36.30.083(a), Legislative Council has approved the extension of this Lease as legally required. In addition to any other right of the Lessee under this Lease to terminate the Lease, if, in the judgment of the Legislative Affairs Agency Executive Director, sufficient funds are not appropriated in an amount adequate to pay the then annual lease payments and expenses, the Lease will be terminated by the Lessee as of the date appropriated funds are exhausted, or will be amended by mutual agreement of the Parties. To terminate under this section, the Lessee shall provide not less than 90 days advance written notice of the termination to the Lessor.¹⁰

§ 43 AUTHORIZATION; CERTIFICATION:

⁸ *Alaska Building Inc. v. 716 West Fourth Avenue, LLC*, 3AN-15-05969CI (Anchorage Superior Court) (the “Lawsuit”).

⁹ Contract Claim at 16.

¹⁰ Ex. 32 at 4.

Funds are available in an appropriation to pay for the Lessee's monetary obligations under the Lease through June 30, 2015. The availability of funds to pay for the Lessee's monetary obligations under the Lease after June 30, 2015, is contingent upon appropriation of funds for the particular fiscal year involved. In addition to any other right of the Lessee under this Lease to terminate the Lease, if, in the judgment of the Legislative Affairs Agency Executive Director, sufficient funds are not appropriated by the Legislature, the Lease will be terminated by the Lessee or amended. To terminate under this section, the Lessee shall provide written notice of the termination to the Lessor. The Executive Director will include a budget request to cover the obligations of Lessee in the proposed budget as presented to the Legislative Council for each lease year as a component of Lessee's normal annual budget request and approval process.¹¹

III. STATEMENT OF FACTS

A. Relevant Facts from the Contract Claim

On September 19, 2013, LAA and 716 entered into the Lease.¹² The Alaska Housing Finance Corporation served as LAA's representative in dealing with 716 in connection with the plans and process for the renovations, among other tasks. Under the terms of the Lease, the parties agreed that certain renovations would be completed. The renovations would be funded by \$7,500,000 in direct reimbursement payments from LAA to 716 for that portion of the renovation work that represented the tenant improvements.¹³

On December 22, 2014, representatives from LAA, 716, and 716's lender (EverBank) signed a Subordination and Non-Disturbance Agreement ("SDNA"), which protected LAA's right to remain as a tenant if EverBank or another entity became the owner of the Building.¹⁴ In that agreement, LAA agreed that it would not consent to the "termination or cancellation of the Lease" without EverBank's consent.¹⁵ However, the parties also expressly agreed that this consent requirement was inapplicable if the Lease terminated "as provided in Section 43 of the Lease for failure of the Alaska Legislature to appropriate sufficient funding."¹⁶ EverBank loaned

¹¹ *Id.* at 16. Largely identical language was included in the previous "Renewal of Lease No. 5" between 716 and LAA, dated May 20, 2013, as well as previous contractual arrangements for the property. Ex. 13 at 2-3 § 3; Exs. 9-12.

¹² The Contract Claim includes historical background concerning prior procurements, efforts to obtain space, updates provided during the renovation process, appraisals, and negotiations concerning the possible purchase of the Building. Because this background is irrelevant to the issues in this Contract Claim, they are not discussed further.

¹³ Ex. 32 at 5 § 3.

¹⁴ Ex. 37.

¹⁵ *Id.* at 2 ¶ 5.

¹⁶ *Id.* at 3 ¶ 5. The parties likewise acknowledged that any recovery of attorney's fees against LAA under the SNDA was subject to a specific appropriation for that purpose, that such an

\$28,600,000 to 716 in connection with the renovated Building.¹⁷ 716 paid \$3,150,000 to purchase 712 West Fourth Avenue, which was ultimately incorporated into the Building.¹⁸

In January 2015, LAA began paying new lease amounts for the Building pursuant to the Lease terms, drawing on funds appropriated by the Legislature for that purpose.¹⁹

On March 31, 2015, a neighboring landlord, Alaska Building, Inc., sued 716 and LAA regarding the Lease, and sought a declaration that the Lease was invalid because of its alleged inconsistency with the State procurement code.²⁰ On March 24, 2016, the Superior Court granted the plaintiff's motion for summary judgment and entered a declaratory judgment that the Lease was invalid because it was not an "extension" and therefore did not comply with AS 36.30.083(a).²¹ The Superior Court denied motions for reconsideration on May 20, 2016.²²

LAA has indicated to 716 on several occasions, including on May 16, 2016 (which predated the Superior Court's decision on the motions for reconsideration), that it may vacate the Building at some point and move to a different location.²³ Nevertheless, LAA has continued to make all rental payments while remaining as a tenant, and was making rental payments at the time that 716 submitted this Contract Claim.²⁴

B. Facts Omitted from 716's Contract Claim

The Contract Claim's discussion of relevant facts is materially incomplete.

(. . . continued)

appropriation remained in the sole discretion of the Legislature, and that the Legislature's failure to make such an appropriation created no further liability or obligation of LAA. *Id.* at 4 ¶ 9.

¹⁷ Ex. 38.

¹⁸ Ex. 33. 716 asserts that it contributed \$8,900,000 of its own equity capital for the renovated Building. I assume that the purchase price of the adjacent property is included in this figure, but no other supporting information is provided to substantiate it. Further, 716 cites to Exhibit 54 as support for its damages calculation, but that two-page document is an email and "development budget" from Mr. Pfeffer, one of 716's principals, before any renovations were performed. It shows a "total cost" of \$44,516,021. Offsetting LAA's \$7,500,000 in tenant improvement payments would leave \$37,016,021 – the amount claimed here. But no supporting documentation is provided to confirm the validity of these amounts. For example, 716 is claiming \$771,722 of budgeted "contingency" funds without demonstrating that those funds were invested. The supporting data is lacking.

¹⁹ Ex. 48.

²⁰ Ex. 45.

²¹ Ex. 1.

²² 716 states that the Superior Court issued its "final order" on May 20, 2016, affirming its prior summary judgment ruling. Contract Claim at 8. The May 20 order was an order denying a motion for reconsideration. It was not an entry of judgment.

²³ Ex. 6.

²⁴ Contract Claim at 13 ("[T]he Legislature has continued to pay rent, and most recently has indicated it will continue to do so through September 2016.").

1. 716's involvement in the procurement analysis

During the course of negotiations for the Lease in 2013, both 716 and LAA focused on AS 36.30.083 to determine how and whether the renovated Building would comply with the requirements for lease extensions set forth in that statute. 716 was an active participant in those discussions and affirmatively presented its own assessment of how best to ensure that the Lease satisfied the statute. In internal email exchanges, one of 716's lawyers noted to a 716 principal that John Steiner (716's in-house counsel) "and I are not confident that the entire deal [for the Building] can be done under section 083 with the material modification as well."²⁵ Mr. Steiner responded that he conferred with LAA's in-house counsel concerning AS 36.30.083 and how to meet its requirements.²⁶ After noting that LAA's in-house counsel had tended to focus on procurement issues, Mr. Steiner stated his belief that the Alaska Procurement Code made the transaction exempt from all procurement rules other than AS 36.30.080, which only requires approval by the Legislature if total lease payments are to exceed \$2,500,000. That is, Mr. Steiner believed that there was no need to comply with the below market value extension requirements of AS 36.30.083.²⁷ Mr. Steiner then noted internally his concern that AS 36.30.083 addresses only extension of a lease, not enlargement of a leased property.²⁸

Mr. Steiner also prepared two memoranda with his own "procurement analysis" for 716. In the first memorandum, Mr. Steiner stated, "I do not believe the proposed Anchorage Legislative Information Office (LIO) lease extension and potential project plan is subject to any reasonable issue as to its compliance with applicable procurement rules."²⁹ He went on to advocate for an extension of the existing lease under AS 36.30.083(a), followed up by a material modification of that lease for various renovations to the Building.³⁰ In describing this proposed course of action, however, Mr. Steiner noted that "[n]othing . . . in AS 36.30.083(a)[] suggests an expectation, contemplation, or even authority for the Legislative Council to double the area leased or total lease cost immediately before or in conjunction with an extension under that statute."³¹ Mr. Steiner then expressed his core concern about potential application of AS 36.30.083(a) to the Lease:

For the Legislative Council to attempt to accomplish redevelopment [i.e., the renovations] and an associated change in rent (increasing both the space leased and the rent per square foot)

²⁵ Ex. C at 3 (716-001264). Mr. Steiner relayed to 716's lawyer and Mr. Pfeffer that LAA's in-house counsel had indicated it would be disingenuous to seek a lease extension that complied with section .083's 10% below market value requirement but did not contemplate any renovations, get the lease extension approved, and then promptly do substantial renovations, because the Legislature did not plan to continue leasing the building in the absence of renovations. *Id.* at 2 (716-001263). LAA instead insisted, despite pushback from 716, that upfront approval for the renovations be obtained as part of the extension.

²⁶ *Id.* at 1-2 (716-001262-63).

²⁷ *Id.* at 2 (716-001263).

²⁸ *Id.*

²⁹ Ex. D at 3 (LAA_003419).

³⁰ *Id.* at 3-6 (LAA_003419-22).

³¹ *Id.* at 4 (LAA_003420).

under AS 36.30.083(a) would seem much more likely to be seen as an end-run around the statutory requirement for full legislative approval.³²

Mr. Steiner expressed his belief that modifications to the Legislative Procurement Procedures and the full Legislature's approval of the Lease would insulate the Lease from legal challenge.³³ In his second memorandum, Mr. Steiner noted that there may be "concern" that competitive procurement ought to be required for the selection of LAA's office space. But Mr. Steiner then asserted that there should be a "complete exemption from further competitive procurement" for the Lease.³⁴ He explained that, in his view, "the only step lacking to perfect the exemption from competitive procurement in this instance is for the chairman of the Legislative Council, being the relevant procurement officer, to prepare a written determination in compliance with Alaska Legislative Procurement Procedures Section 040(a)."³⁵ He went on to state:

Exemption from competitive procurement based on a written determination under Alaska Legislative Procurement Procedures Section 040(a) would eliminate any concern about compliance with the competitive solicitation under past practice and the Alaska Legislative Procurement Procedures. That exemption would, thus, also eliminate any need to accomplish the proposed enlargement and renovation of the existing space under AS 36.30.083 in order to justify not issuing a new competitive solicitation.³⁶

These memoranda were shared with LAA as the structure for the proposed Lease was being addressed. LAA did not adopt Mr. Steiner's analytical approach with respect to extending the lease "as is" and then making material modifications afterwards, but nevertheless, there was extensive discussion between LAA and 716 concerning the procurement process, the potential risks, and what steps were required to comply with AS 36.30.083(a).³⁷

2. Within three weeks after the Lease was signed, 716 was on notice of a challenge to the Lease's validity yet 716 proceeded with construction

Within days after the Lease was signed on September 19, 2013, the owner of the neighboring building (Mr. James Gottstein) reached the conclusion that the Lease was inconsistent with the State Procurement Code and AS 36.30.083 in particular. Mr. Gottstein's concerns would later become the basis for the Lawsuit. He communicated this view to 716

³² *Id.* at 6 (LAA_003422).

³³ *See id.* at 6-7 (LAA_003422-23).

³⁴ Ex. E at 1 (716-005930).

³⁵ *Id.* at 2 (716-005931).

³⁶ *Id.*

³⁷ 716 points to the findings of the procurement officer under Legislative Procedures 040(d) as the assertion of LAA's position that the Lease was valid (on which 716 claims to have relied). Contract Claim at 11. These findings, however, are precisely the findings that Mr. Steiner advocated would exempt the Lease from competitive solicitation requirements. Ex. E at 2 (716-005931).

through 716's counsel by early October 2013, as confirmed in Mr. Gottstein's sworn testimony and discovery responses.³⁸ At that time, Mr. Gottstein stated that he was contemplating filing for an injunction to stop the project on that basis.³⁹ Mr. Gottstein then followed up with an in-person meeting with 716's counsel on October 28 and an email on October 30, stating that the project was in violation of state law.⁴⁰ 716 did not address Mr. Gottstein's concerns in any substantive way.⁴¹ 716 did not seek to remove any doubts concerning the validity of the Lease through a declaratory judgment action. The demolition and other construction work for the Building began in earnest in early December 2013 – roughly two months after Mr. Gottstein first raised the issue with 716.⁴² Thus, 716 learned about questions regarding the validity of the Lease before it spent significant sums on the Building.

3. Non-appropriation

The Lease extended the previous term of the parties' arrangement for ten years, subject to a variety of conditions that could shorten or lengthen that term.⁴³ For example, LAA could exercise an option to extend the Lease for up to ten years following the end of the expiring lease term.⁴⁴ If either LAA or 716 was in default of certain obligations under the Lease, the other could terminate the Lease prior to the expiration of the lease's term.⁴⁵ Likewise, the term could be reduced if 716 failed to furnish insurance for the Building,⁴⁶ if the Building was not delivered in a satisfactory condition,⁴⁷ or if 716 became headquartered in certain countries.⁴⁸ Another condition that could reduce the term of the Lease was "non-appropriation" – that is, if the Legislature did not appropriate sufficient funds to pay the annual lease payments and expenses for the Building, the Lease would terminate after a 90-day period following written notice of such termination and the exhaustion of the appropriated funds.⁴⁹

716 recognized the possibility of non-appropriation during the Lease negotiations. In July of 2013, 716 expressed concern to LAA that the Legislature may decline to appropriate sufficient funds necessary to make the payments for the first year of the Lease. Accordingly, 716 sought to negotiate some contractual protection in the Lease to address this risk. In an effort to accommodate 716's concern, LAA proposed language that would have entitled 716 to a payment of up to \$1.5 million as reimbursement for certain engineering and other renovation expenses

³⁸ Ex. F, Deposition of James Gottstein, Vol. 1, at 18:7-11, 26:10-23 (Oct. 16, 2015); Ex. G (Responses to Legislative Affairs Agency's First Discovery Requests to Plaintiff) at 10 (Oct. 5, 2015).

³⁹ Ex. G at 10.

⁴⁰ Ex. H (Exhibit D to Deposition of James Gottstein, Vol. II (Oct. 23, 2015)).

⁴¹ *Id.*

⁴² Ex. F at 44:11-14.

⁴³ Ex. 32 § 1.1(b).

⁴⁴ *Id.* § 47.

⁴⁵ *Id.* § 33.

⁴⁶ *Id.* § 35.

⁴⁷ *Id.* § 36.

⁴⁸ *Id.* § 46.

⁴⁹ *Id.* §§ 1.2, 43.

required under the Lease, subject to appropriation by the Legislature.⁵⁰ This correspondence and the proposed language, which was not ultimately included in the Lease, confirms 716's awareness that the Legislature may choose not to appropriate funds with respect to even the initial Lease payment. It likewise reaffirms that even a "reimbursement" payment that was triggered by a non-appropriation would itself be subject to appropriation by the Legislature.

Since the Lease was executed, the Legislature has looked actively for cost savings in all areas of government spending, including but not limited to office space. Before the Lawsuit was filed, members of the Legislature were already reviewing the Lease and publicly assessing whether those costs were justifiable in this difficult economic environment.⁵¹ This included the possibility that the Legislature would decline to appropriate sufficient funds for further rent of the Building, thereby terminating the Lease according to its terms and state law. Over the course of 2015, the Legislature continued to discuss a wide range of possibilities – including the possibility of non-appropriation – as a means of reducing the State's budget shortfall. This included the Senate Finance Committee's proposal to non-appropriate in early April 2015.⁵² The Legislative Council considered buying a different building to house the LIO and address "the state's serious and sudden revenue shortfall and deepening budget concerns," but ultimately voted 13-1 to recommend funding the Lease for FY 2016.⁵³ The Legislature also discussed a possible purchase of the Building.⁵⁴ By late November, both options were under consideration.⁵⁵ As noted above, on December 19, 2015, the Legislative Council voted unanimously to recommend the non-appropriation of funds for rent in the upcoming fiscal year unless 716 was able to present a more cost-competitive option within 45 days that could garner adequate support.⁵⁶ 716 attempted to do so, but an independent economic analysis from Navigant showed that the proposed purchase price was still millions of dollars more expensive than other available options.⁵⁷ Shortly thereafter, Governor Walker announced that he would veto the proposed purchase of the Building, effectively eliminating that as an option.⁵⁸

As part of the Legislature's usual discretionary budgetary process, LAA's Executive Director had included a budgetary request to the Legislative Council to cover LAA's payment

⁵⁰ Ex. I (Gardner letter to McClintock (Jul. 24, 2013; *corrected* Jul. 25, 2013)).

⁵¹ Ex. J (Nathaniel Herz, *Legislature Reconsiders Its Anchorage Building As It Hunts For More Cuts*, Alaska Dispatch News (Mar. 28, 2015)).

⁵² Ex. K (Nathaniel Herz, *Senate Committee Strips Funds For Legislature's New Anchorage Offices*, Alaska Dispatch News (Apr. 2, 2015)).

⁵³ Ex. L (Alaska State Legislature, Legislative Council Meeting Minutes (Apr. 13, 2015)).

⁵⁴ *Id.*; Ex. A (Alaska State Legislature, Legislative Council Meeting Minutes (Dec. 19, 2015)) at 3-54.

⁵⁵ Ex. M (Anchorage LIO Office Space Report (Nov. 24, 2015)).

⁵⁶ Ex. A (Alaska State Legislature, Legislative Council Meeting Minutes (Dec. 19, 2015)) at 57-60.

⁵⁷ Ex. N (Alaska State Legislature, Legislative Council Meeting Minutes (March 31, 2016)) at 7-8; Ex. O (Nathaniel Herz, *Report: State Saves \$7.5M If Lawmakers Leave New Anchorage Offices*, Alaska Dispatch News (March 18, 2016)).

⁵⁸ Ex. B (Becky Bohrer, *Walker says he'd veto Anchorage LIO purchase*, Juneau Empire (from The Associated Press (Apr. 15, 2016; *updated* Apr. 17, 2016)).

obligations under the Lease for the period of July 1, 2016 through June 30, 2017.⁵⁹ The Legislative Council ultimately recommended that the Legislature fund only a portion of the FY2017 Lease payments, which the House Finance Budget Subcommittee recommended to the House Finance Committee.⁶⁰ The budget that was finally passed by the Legislature and signed by Governor Walker included a reduced amount for those rental payments; the appropriation only covered roughly three months of rent under the Lease.⁶¹ On July 18, 2016, LAA's Executive Director notified 716 that, in her judgment, sufficient funds had not been appropriated by the Legislature to cover the annual Lease payments and expense obligations of LAA for the fiscal year.⁶² Accordingly, she provided written notice that LAA was terminating the Lease under sections 1.2 and 43 of the Lease.

IV. REASONS SUPPORTING DECISION

A. The Legislature Did Not Appropriate Further Payments Pursuant to Its Constitutional Authority and the Constitutional Limitations on Appropriations (Alaska Constitution Article IX § 13)

Generally speaking, the Alaska Constitution prohibits one legislative body from binding a future legislature to make certain expenditures. Each legislature must decide for itself, after weighing all relevant considerations, whether to appropriate funds for a particular purpose like a lease payment. Otherwise, one legislative body could enter into a long-term contract promising to pay rent in future years without regard to whether or not future funds may be available. This would violate the Alaska Constitution's debt restriction.⁶³ Accordingly, the Alaska Constitution contains an express prohibition – the “appropriations clause” – on expenditures of State funds in the absence of an appropriation:

No money shall be withdrawn from the treasury except in accordance with appropriations made by law. No obligation for the payment of money shall be incurred except as authorized by law. Unobligated appropriations outstanding at the end of the period of time specified by law shall be void.⁶⁴

⁵⁹ Ex. P (Alaska State Legislature, Legislative Council Meeting Minutes (Feb. 11, 2016)) at 3-4 (discussing Ex. Q (Legislative Council FY 2017 Proposed Budget)).

⁶⁰ Ex. R (Alaska State Legislature, FY 2017 House Finance Budget Subcommittee Narrative Report (Feb. 26, 2016)).

⁶¹ Ex. S (C.C.S. H.B. 256, at 45-45 (2016)).

⁶² Ex. T (Varni letter to Pfeffer and Acree (Jul. 18, 2016)).

⁶³ Alaska Constitution art. IX, § 8; *Carr-Gottstein Props. v. State*, 899 P.2d 136, 142 (Alaska 1995) (“When taken together, this court finds that the foregoing Alaska cases and the cases cited by the Alaska Supreme Court define constitutional ‘debt’ as a term of art used to describe an ‘obligation’ involving borrowed money where ‘there is a promise to pay sums such as rents accruing in the future whether funds are available or not.’” (internal citation omitted) (adopting the Superior Court’s decision)).

⁶⁴ Alaska Constitution art. IX, § 13. This provision is implemented by AS 37.05.170: “[O]bligations may not be incurred against a fund unless . . . an appropriation or expenditure obligation has been made for the purpose for which it is intended to incur the obligation.

This clause limits the terms under which the Legislature is permitted to enter into certain contracts. As a result, even if a government contract is silent about the potential for non-appropriation, this constitutional provision still operates to require adequate legislative appropriation for any government expenditure. That is, without a constitutionally-mandated appropriation, there is no authority for any government outlay of funds, regardless of contractual terms. Here, this constitutional provision operates to require adequate legislative appropriation for any future obligation by the Legislature for the Building, irrespective of the Superior Court’s declaratory judgment that the Lease was invalid.

As the Alaska Supreme Court has explained, “the appropriations clause defines how the legislature may spend state money after it has entered state coffers.”⁶⁵ Along with the governor’s ability to veto certain expenditures, the appropriations clause helps govern “the legislature’s and the governor’s ‘joint responsibility . . . to determine the State’s spending priorities on an annual basis.’”⁶⁶ These spending priorities are reflected in the appropriations that the Legislature elects to make in any given year and, as in this instance, those it elects not to make.

The Legislature’s appropriation decisions are a vitally important responsibility that the Legislature undertakes annually, along with the Governor, to safeguard the public treasury. In order to ensure that each Legislature may act as a responsible steward of the public treasury, the Alaska Constitution dictates that expenditures such as lease payments are only valid to the extent that they are subject to the Legislature’s ability to “exercis[e] the option of non-appropriation” so as “not [to] restrict the Legislature’s free exercise of discretion.”⁶⁷

In light of the State’s current fiscal situation, the Legislature exercised its Constitutional right of non-appropriation with respect to the Lease. While 716 complains that LAA “abdicated” its duties under the Lease, termination of the Lease pursuant to the Legislature’s non-appropriation authority is consistent with the Legislature’s constitutional duty and obligation to the citizenry. The Constitution precludes payment of any non-appropriated amounts for the Lease and 716’s claim for damages therefore fails.

716’s request for damages based on the totality of its investment in the Building is a demand that, in essence, the State purchase the Building outright. This request misapplies any potentially applicable damages theory, as discussed below.⁶⁸ It is also improper because the

⁶⁵ *State v. Ketchikan Gateway Borough*, 366 P.3d 86, 101 (Alaska 2016) (emphasis omitted).

⁶⁶ *Id.* (quoting *Simpson v. Murkowski*, 129 P.3d 435, 447 (Alaska 2006) (which, in turn, quoted the trial court’s decision)).

⁶⁷ *Carr-Gottstein Props.*, 899 P.2d at 143 n.5 (adopting the Superior Court’s decision) (citing and quoting *Schulz v. State*, 639 N.E.2d 1140, 1149 (N.Y. 1994) (“Such spending plans are effectual only to the extent subsequent legislatures indeed do ‘give effect to them by providing the means of and directing their payment, but the discretion and responsibility is with them as if no former appropriations had been made. No duty or obligation is devolved upon them by the acts of their predecessors.’”)).

⁶⁸ See Section IV.D below. Indeed, the \$37,016,021 damages demand far exceeds the amount that 716 had agreed to sell the Building for earlier in 2016.

State – through the Legislature and the Governor – already elected not to purchase the Building. 716 cannot compel the Legislature to make an appropriation to purchase the Building under the guise of reliance damages in this Contract Claim.⁶⁹

The non-appropriation authority exists in many states’ constitutions, and decisions relating to that authority are instructive here. In *KHK Associates v. Department of Human Services*, the Supreme Judicial Court of Maine considered a nearly-identical circumstance. Maine’s Department of Human Services had solicited bids for office space and awarded the contract to a contractor.⁷⁰ The contractor proceeded to construct a building according to the Department’s specifications and entered into a ten-year lease with the Department. That lease included provisions for termination of the lease in the event of non-appropriation of funds by the legislature, consistent with the provision in Maine’s Constitution stating that no funds can be drawn from the treasury unless the legislature chooses to appropriate them.⁷¹ Months after construction, it became apparent that Maine would experience a budget shortfall and the legislature examined potential savings options. The legislature elected to reduce the appropriation for the lease and, when the parties were unable to agree upon different terms, the Department terminated the lease pursuant to the legislature’s non-appropriation authority and the attendant clause in the lease.⁷² The contractor sued. Maine’s highest court rejected that claim, noting that both the Maine Constitution and statutory law required that the lease be subject to funding by the legislature.⁷³ The court concluded by noting that governmental entities have “an obligation to communicate to the legislature appropriate ways to reduce state spending” and that the exercise of the non-appropriation authority followed from that.⁷⁴ Other states have similarly confirmed the propriety of the legislature’s exercise of the non-appropriation power.⁷⁵

⁶⁹ 716’s damages request is somewhat unclear. While 716 articulates the amount demanded, it says that these amounts include the loss of 716’s equity investment and the improvements to the Building. This suggests that 716’s anticipated loss includes the loss of the Building and that the \$37 million in damages would compensate them for that loss, presumably with LAA becoming the owner after having paid for 716’s equity investment and the improvements. If 716 is claiming that it should be entitled to \$37 million in damages and still be permitted to keep the Building, this would appear to be double counting.

⁷⁰ 632 A.2d 138, 139 (Me. 1993).

⁷¹ Maine Constitution art. V, pt. 3, § 4.

⁷² See 632 A.2d at 139-40.

⁷³ See *id.* at 140.

⁷⁴ See *id.* at 140-41.

⁷⁵ See, e.g., *Glennon Heights, Inc. v. Cent. Bank & Trust*, 658 P.2d 872, 879 (Colo. 1983) (noting that “[r]enewal of each lease term is specifically tied to appropriation of sufficient funds, and the lease terminates with no further obligation of the department if funds are not available”); *State v. Goldschmidt*, 783 P.2d 988, 995 (Ore. 1989) (“The state’s promise of repayment is conditioned on the willingness of future legislative assemblies to appropriate the funds. The state does not promise that future legislatures will appropriate any funds. The lenders take the risk of nonpayment.”); see also *id.* at 996 n.12 (collecting cases for the proposition that the non-appropriation authority allows legislatures to engage in certain financing transactions without incurring impermissible “debt”).

B. The Legislature’s Decision Not to appropriate Further Rent Payments Triggered the Lease’s Non-Appropriation Clause (Sections 1.2 and 43) and Limited the Scope of Potentially Available Damages

As discussed above, non-appropriation clauses like those included in the Lease are standard and constitutionally required.⁷⁶ The clause at issue is contained in both Sections 1.2 and 43 of the Lease. 716 was aware of the non-appropriation clause and, during the Lease negotiations, sought to secure certain contractual protections in the event that the clause was triggered.⁷⁷ Consistent with Sections 1.2 and 43, LAA’s Executive Director included a budget request to cover the obligations of LAA in the proposed budget as presented to the Legislative Council for FY 2017 as a component of LAA’s normal annual budget request and approval process.⁷⁸ However, sufficient funds were not appropriated by the Legislature to pay for LAA’s monetary obligations under the Lease for the period of July 1, 2016 through June 30, 2017.⁷⁹ LAA’s Executive Director confirmed in writing to 716 that, in her judgment, sufficient funds had not been appropriated by the Legislature and therefore the Lease would be terminated in 90 days pursuant to Sections 1.2 and 43 of the Lease.⁸⁰ In following these steps, LAA exercised its contractual right to terminate the Lease.

The non-appropriation clause helps define the scope of the parties’ obligations under the Lease. Under the Lease, 716 agreed that it would perform certain renovations in connection with the extension of the Lease and would remain as owner of the Building. LAA agreed that it would pay \$7.5 million upfront for assorted tenant improvements. LAA further agreed that it would be the tenant at the Building for up to ten years (with the possibility of an extension), and the tenancy was annually subject to appropriations. The Lease was, effectively, a year-to-year arrangement because it was subject to these annual appropriations. Aside from LAA’s payment for tenant improvements, the parties agreed that 716 was entitled to rent payments for as long as LAA was a tenant in the Building – nothing more.

In its Contract Claim, 716 claims that it should receive an *additional* \$37 million in “reliance damages” over and above the millions it has already received in tenant improvements and rent payments.⁸¹ 716’s characterization of its claim as “reliance damages” does not give it the right to recover more than what is owed under the fully-performed Lease, however. Here, 716 assumed the risk that the Lease would be terminated long before the anticipated 10-year term was over. If LAA remained as a tenant for ten years (or more), then the Lease could be quite profitable to 716. If, however, LAA terminated the Lease early – as occurred here – then 716 would bear the risk of loss if it proved unable to locate a replacement tenant. 716 now seeks

⁷⁶ See *Carr-Gottstein Props.*, 899 P.2d 136, 143-44 (Alaska 1995) (adopting Superior Court decision) (finding lease-purchase agreements to be appropriate where they contain a non-appropriation clause, limit the recourse to the leased property, and do not create a long-term obligation binding future generations or Legislatures).

⁷⁷ See *supra* note 50 and accompanying text.

⁷⁸ Ex. P (Alaska State Legislature, Legislative Council Meeting Minutes (Feb. 11, 2016)) at 3-4 (discussing Ex. Q (Legislative Council FY 2017 Proposed Budget)).

⁷⁹ Ex. S (C.C.S. H.B. 256, at 45-46 (2016)).

⁸⁰ Ex. T. By this time, the appropriated funds would be exhausted.

⁸¹ Contract Claim at 15.

to avoid the risks of its bargain by claiming it is entitled to more than \$37 million in reliance damages. “Reliance damages are not insurance. Courts will not knowingly put the plaintiff [receiving a reliance recovery] in a better position than he would have occupied had the contract been fully performed.”⁸² LAA fully performed its obligations under the Lease by paying rent and other expenses up through the date that the tenancy concluded pursuant to the non-appropriation power. 716 cannot use its “reliance damages” theory to obtain more than it could have received (and, in fact, did receive) under the Lease. The losses that 716 claims here are a function of the bargain it struck, and it cannot shift the risks of that bargain to LAA.

C. Based on the Existing Record, 716’s Estoppel Claim Fails

716 brings its Contract Claim under the doctrine of estoppel, asserting that the Lease was cancelled based on a court determination in March 2016 that the contract violated a statute.⁸³ As explained above, 716 is mistaken. The Lease was cancelled pursuant to the Legislature’s constitutional non-appropriation power and LAA’s contractual rights under Sections 1.2 and 43 of the Lease.⁸⁴ In any event, 716’s estoppel claim also fails factually and legally.

In order to find estoppel against a government agency, four requirements must be met: (1) LAA must have asserted a position by conduct or word; (2) 716 must have reasonably relied upon that position; (3) 716 must have been prejudiced as a result; and (4) the interests of justice must require estoppel. Based on the factual record here, 716 is unable to satisfy three of the four elements necessary to demonstrate that this is an “exceptional case[]” in which a private party may invoke estoppel against the State.⁸⁵

⁸² *Merry Gentleman v. George and Leona Productions, Inc.*, 799 F.3d 827, 832 (7th Cir. 2015) (internal quotations omitted; alteration in original); *see also, e.g., Bausch & Lomb Inc. v. Bressler*, 977 F.2d 720, 729 (2d Cir. 1992) (“[T]he alternative reliance ‘measure of damages rests on the premise that the injured party’s reliance interest is no greater than the party’s expectation interest.” (quoting 3 FARNSWORTH, FARNSWORTH ON CONTRACTS § 12.16, at 265 (2d ed. 1990))); *Agam v. Gavra*, 186 Cal. Rptr. 3d 295, 307 (Cal. Ct. App. 2015); *Doering Equip. Co. v. John Deere Co.*, 815 N.E.2d 234, 240-41 (Mass. App. Ct. 2004); 3 DOBBS, DOBBS ON REMEDIES § 12.3(2), at 57 (2d ed. 1993) (“[I]f the reliance claim is to be justified as a contract claim, then a recovery that makes the plaintiff better off by reason of breach seems wrong: the plaintiff should not be put in *better* position by reason of breach than by performance. In accord with this view, the Restatement and the leading decisions have taken the position that the expectancy is a ceiling on reliance damages.”); RESTATEMENT (SECOND) OF CONTRACTS § 349 cmt. a.

⁸³ Contract Claim at 10.

⁸⁴ *Cf. Steffel v. Thompson*, 415 U.S. 452, 471 (1974). Formal notice was provided on July 18, 2016, but the Legislature had begun the process of exercising this non-appropriation right several months earlier.

⁸⁵ *Alaska Trademark Shellfish, LLC v. State*, 91 P.3d 953, 960 (Alaska 2004); *Municipality of Anchorage v. Schneider*, 685 P.2d 94, 97 (Alaska 1984).

1. 716 did not reasonably rely on a determination that the Lease complied with AS 36.30.083

Generally speaking, a person dealing with a government agency is bound to take notice of the legal limits of the agency's powers and those of its agents.⁸⁶ There are exceptions to this rule, and there are circumstances in which a private citizen may reasonably rely upon a government agency's determination even when that determination is outside of the legal limits of the agency's authority.⁸⁷ This is not one of those circumstances for several reasons.

First, prior to signing the lease 716 was heavily involved in the analysis of the procurement statute at issue. LAA and 716 considered and debated the applicability of AS 36.30.083 extensively. 716 was represented by capable in-house and outside counsel who evaluated whether or not the transaction for the Building would comply with that statute, even going so far as to prepare an independent evaluation of the statutory framework and to recommend steps that the Legislature could take to increase the defensibility of the transaction.⁸⁸ While providing this evaluation, 716's in-house counsel, Mr. Steiner, expressed his concern to others at 716 that AS 36.30.083 addressed only extension of a lease, not enlargement of a leased property.⁸⁹ As it turns out, Mr. Steiner had accurately predicted the basis for the Superior Court's ruling that the Lease was invalid. 716 was guided in these discussions by one of its principals, Mark Pfeffer, a very sophisticated businessman who likewise advocated that the Lease should not be the subject of a competitive bidding process. Mr. Pfeffer even went so far as to say that LAA's counsel's legal analysis was "flat out wrong" and then offered his own analysis of the procurement regulations.⁹⁰ Given 716's familiarity with the procurement statute at issue, its heavy consultation concerning the structure of the transaction, its use of counsel on these procurement issues, and the sophistication of its principal, it does not appear that 716 reasonably relied upon LAA's determination that the Lease complied with AS 36.30.083, but instead relied upon its own analysis and internal conclusions.⁹¹

Second, immediately after the lease was signed in 2013, Mr. Gottstein informed 716 of his concern that the Lease did not comply with AS 36.30.083 because it was not the subject of competitive bidding and that he was considering legal action. 716 was therefore put on notice

⁸⁶ See, e.g., *Municipality of Anchorage*, 658 P.2d at 96.

⁸⁷ See *Property Owners Ass'n v. City of Ketchikan*, 781 P.2d 567, 573 (Alaska 1989) (noting that an average citizen's good faith reliance upon an erroneously issued building permit was reasonable).

⁸⁸ Ex. E at 1 (716-005930).

⁸⁹ Ex. C at 2 (716-001263).

⁹⁰ Ex. C at 1 (716-001262). In particular, Mr. Pfeffer opined that if the Legislature approved the Lease and the Governor signed off as well, then the procurement would necessarily satisfy any legal requirements.

⁹¹ See, e.g., *Messerli v. State, Dept. of Nat. Resources*, 768 P.2d 1112, 1121 (Alaska 1989), overruled on other grounds, *Olson v. State, Dept. of Nat. Resources*, 799 P.2d 289 (Alaska 1990) (finding no reasonable reliance because it was presumed that the citizen knew the law and the citizen was assisted by counsel in connection with the government's action); *Property Owners Ass'n*, 781 P.2d at 573 (declining to find reasonable reliance where plaintiffs were sophisticated businessmen).

both that there was a serious question about the validity of the Lease *and* that Mr. Gottstein, a lawyer, planned to bring suit on the issue.⁹² Rather than seeking clarity about the Lease’s validity through the court system, 716 chose to spend tens of millions of dollars (and take \$7.5 million from LAA for tenant improvements) on renovations to the Building. 716 did so despite the fact that Mr. Gottstein’s analysis of AS 36.30.083 largely mirrored 716’s internal concerns about the application of the procurement statute. Especially when combined with 716’s internal doubts about the validity of the procurement, Mr. Gottstein’s early efforts to alert 716 about the apparent invalidity of the Lease should have given 716 pause and prompted 716 to confirm the Lease’s propriety before expending the funds it now claims as damages. 716’s decision to proceed and spend tens of millions of dollars in the face of this early and direct warning was unreasonable.

2. 716 was not prejudiced

716 is unable to show that it was prejudiced by its alleged reliance upon the procurement here. While 716 clearly invested substantial time and money to renovate the Building, 716 received exactly what it bargained for: It now owns a substantially renovated building – paid for in part by LAA – in downtown Anchorage and had LAA as a paying tenant since June 1, 2014. 716’s claims of prejudice hinge upon its assumption that LAA was required to remain as a tenant for a specific duration of time.⁹³ In particular, 716 asserts that unless the Legislature remains as the tenant under the Lease for ten full years, 716 will fall into default of its loan terms and may lose certain investments as a result.⁹⁴ As explained above, 716 and its lender, EverBank, have always been aware that the Legislature may terminate the Lease at any time (with 90 days advance written notice) pursuant to the Legislature’s non-appropriation authority. The termination of the Lease earlier than 716 wished – but still within the contemplation of the parties as reflected in the Lease’s terms – does not constitute “prejudice.”⁹⁵ 716 was not entitled to have LAA remain as a tenant any longer than it did, irrespective of the Superior Court’s finding regarding the validity or invalidity of the Lease.

Likewise, 716’s claims of prejudice concerning the “special use” nature of the Building are misplaced. 716 asserts that it will need to spend an unknown amount of money to undo certain specialized features requested by LAA that a future tenant may not wish to retain. But 716’s speculation that a future tenant may insist on unidentified changes to the Building does not constitute prejudice, particularly because a new tenant may not actually want to make changes to the Building. There is no concrete harm identified here. In addition, LAA could terminate the

⁹² See *supra* at 8.

⁹³ Contract Claim at 13-14.

⁹⁴ Contract Claim at 13.

⁹⁵ Cf. *Earthmovers of Fairbanks, Inc. v. Dep’t of Transp. & Pub. Fac.*, 765 P.2d 1360, 1370-71 (Alaska 1988) (finding prejudice where contractor incurred out-of-pocket expenditures for mobilization activities when construction was halted, so mobilization activities were wasted); *Municipality of Anchorage v. Schneider*, 685 P.2d 94, 98 (Alaska 1984) (finding prejudice where municipality sought to revoke a building permit after citizens spent money on building materials, and those expenditures would be wasted). 716 states that “the economics of the lease agreement do not work for a shorter tenancy [than ten years],” Contract Claim at 14, but 716 was undisputedly aware that LAA could terminate its tenancy in fewer than ten years.

Lease at any time, after giving appropriate notice, pursuant to the non-appropriation clause. 716 would then be faced with the identical circumstance – changing the Building after LAA’s departure to accommodate some new tenant. Any such expenses, if incurred, are an inevitable function of the shift from one tenant to the next.⁹⁶

3. The public interest would be significantly prejudiced by the application of the estoppel doctrine here

The final element requires me to weigh the potential injury to the public interest if the estoppel doctrine is applied against the gravity of the injustice to the private entity if the doctrine is not applied. This element has special importance in cases against the government.⁹⁷

In effect, 716 is asking to be paid more than \$37 million from the public’s coffers because 716 obtained a sole-source contract for the Lease and performed extensive renovations to the Building, pursuant to a contract that provided a cancellation right in the event of non-appropriation. It is unclear whether or not 716 envisions that it would remain as the owner of the Building if such relief were granted. Either scenario is problematic.

If LAA would become the owner of the Building upon payment of \$37 million in damages, this would effectively constitute the Legislature’s purchase of the Building without a duly authorized appropriation. When a party’s request for estoppel would require the government to take unauthorized action, the Alaska Supreme Court has “carefully restricted the [doctrine’s] use to circumstances in which the balance of equities manifestly favors the requesting party and estoppel is necessary to avoid further injustice.”⁹⁸ The balance of equities does not manifestly favor 716. After independently analyzing and identifying potential compliance problems with the procurement code – including AS 36.30.083 – and advocating for a sole-source contract, 716 agreed to enter into the Lease. 716 was promptly alerted by Mr. Gottstein of his professional concern as a lawyer that the Lease was invalid due to its inconsistency with the procurement code – a professional assessment that mirrored 716’s internal concerns – and that Mr. Gottstein intended to litigate the issue. Despite this combination of internal concerns about the extension’s validity and an external litigation threat, 716 decided to spend tens of millions of dollars without first requesting that a court confirm the validity of the Lease. 716 also knew before the Lease was signed that the Legislature could exercise the non-appropriation power at any time to terminate the Lease, which it did. LAA satisfied its obligations under the Lease by paying rent up through the termination of the Lease. Risks identified by 716 early in the process (e.g., challenges to the Lease’s validity, termination of the Lease through non-appropriation) – before it had invested substantial monies into this project –

⁹⁶ 716 also expresses concern that it may have difficulty locating a replacement tenant because it may not have sufficient time to market the Building or to make any necessary changes to the Building to make it more attractive to tenants. LAA provided 716 with the full 90-day notice provided in the Lease, however. 716’s complaints concerning the timing cannot be squared with the contractual notice provision for termination of the Lease to which 716 agreed.

⁹⁷ *Property Owners Ass’n v. City of Ketchikan*, 781 P.2d 567, 574 (Alaska 1989) (recognizing the “importance of this element in cases against the government”).

⁹⁸ *Alaska Trademark Shellfish, LLC v. State*, 91 P.3d 953, 960 (Alaska 2004).

ultimately materialized. In these circumstances, the balance of equities does not favor payment of \$37 million to 716.

On the other hand, if LAA would *not* become the owner of the Building upon payment of \$37 million in damages, then 716 is functionally requesting that LAA buy the Building for 716's use as it sees fit. As reflected in press reports, the Legislative Council had recommended that the Legislature purchase the Building for \$32.5 million, subject to approval by the Legislature and the Governor, and 716 had agreed to that figure.⁹⁹ 716 now seeks as damages roughly \$4.5 million *more* than the value of the entire Building, but 716 would also retain the Building and could rent it to other tenants. In effect, 716 is asking that the taxpayers purchase the Building outright for 716 with the benefits flowing entirely to this private developer. The balance of equities does not favor forcing the public to subsidize 716's ownership of the Building.¹⁰⁰

716 acknowledges correctly that a purpose of the procurement code is to protect the public purse.¹⁰¹ This is, in fact, a primary purpose of the procurement code.¹⁰² There are some instances where sole-source contracting is appropriate, but the default approach in many circumstances is to require competitive sealed bidding to help ensure that the public receives the best deal possible.¹⁰³ It is unknown what financial impact, if any, the sole-source nature had on this procurement. What is known is that the sole-source procurement was used in lieu of standard competition. Where the defect in the procurement award would seriously impair the purpose of the competitive bidding statutes, the contract at issue is typically deemed void.¹⁰⁴ That is precisely what the Superior Court held here: "A court finding that this leasing scheme could be sole-sourced would *eviscerate* the competitive principles of the state procurement code. The court finds this lease invalid as it does not comply with AS 3[6].30.083(a)."¹⁰⁵ Applying estoppel here would effectively reward 716 for its role in this sole-source procurement and punish the public by requiring payment of \$37 million, which is more than the amount at which

⁹⁹ Ex. U (Nathaniel Herz, *Walker says he'd veto Anchorage legislative office purchase*, Alaska Dispatch News (May 17, 2016) (quoting 716's spokeswoman: "The Legislative Council proposed a solution. We have agreed to it.")).

¹⁰⁰ *Property Owners Ass'n*, 781 P.2d at 574 ("The fourth element of estoppel allows enforcement only to the extent justice requires. Because of the importance of this element in cases against the government, we are not inclined to find estoppel at all. It would be unjust to force the population at large to subsidize the purchasers of Ketchikan's 'most exclusive' lots as a result of an ambiguous assertion by a city council which had repeatedly expressed the opposite intent.").

¹⁰¹ Contract Claim at 14.

¹⁰² See, e.g., *Pacifica Marine, Inc. v. Solomon Gold, Inc.*, 356 P.3d 780, 792 (Alaska 2015) (finding that the government's objectives in the procurement context include maximizing "the use of public resources by getting the best deal possible"); *Earthmovers of Fairbanks, Inc.*, 765 P.2d at 1370 ("The primary purpose of [a statute requiring construction of public works under bid contract in accordance with the procurement code] is to protect the public purse.").

¹⁰³ See AS 36.30.100.

¹⁰⁴ *Earthmovers*, 765 P.2d at 1369 ("However, as noted above, many state courts find a contract void . . . where the defect in the award seriously impairs the purposes of the competitive bidding statutes.").

¹⁰⁵ Ex. 1 at 16 (emphasis added).

716 valued the Building. This would significantly prejudice the public interest and strongly weighs against application of the estoppel doctrine here: “Often, even where reliance has been foreseeable, reasonable, and substantial, the interest of justice may not be served by the application of estoppel because the public interest would be significantly prejudiced.”¹⁰⁶ Requiring payment of \$37 million to 716 – in effect, purchasing the Building for 716 – when “the benefit of the project has flowed almost entirely to the developer”¹⁰⁷ would unjustly force the population at large to subsidize 716’s involvement in this sole-source procurement.

716 argues that the State’s decision to terminate the Lease after 716 fully performed the renovations for the Building would be “a serious blow to the public interest.”¹⁰⁸ Respectfully, I believe 716 misdescribes the unique circumstances at issue here. Both 716 and LAA fully performed their respective obligations under the Lease. Following the Legislature’s exercise of its non-appropriation authority, LAA terminated the Lease as permitted under Sections 1.2 and 43 of the Lease. This authority was not used lightly, and the highly unusual circumstances surrounding this procurement are unlikely to recur. For example, it is unlikely that a contractor will actively advocate for a sole-source contract, using its own counsel to argue in favor of a particular interpretation of the State Procurement Code. It is also unlikely that a contractor with its own private doubts concerning the validity of a sole-source procurement will be immediately confronted by a future litigant challenging the validity of that procurement, yet nevertheless decide to proceed with a substantial construction project. Under these unique circumstances, and in light of the constitutional appropriation limitation and the plain language of the Lease, I believe that the public interest is favored by declining to apply the doctrine of estoppel to purchase the Building for the benefit of a private contractor. Instead, the public interest is best supported by LAA terminating the Lease and exiting the Building after having paid all rent owed.

D. 716 Has Failed to Show That It Is Entitled to Damages

Finally, 716’s claim must be denied because it failed to show its entitlement to damages here.

716 contends that it is entitled to damages equal to LAA’s “gain” from the Lease, which 716 states should be “the market value of its services” or its investment of \$37 million.¹⁰⁹ 716’s damages calculation reveals the stark disconnect between the amounts claimed and the benefits delivered. In the Lease, LAA did not purchase the Building, nor did it commit to the payment of tens of millions of dollars for various improvements that could be used by LAA or by other future tenants. LAA agreed only to be a tenant in the Building for a period of time (which, due to the termination of the Lease, was through October 16, 2016). That was LAA’s “gain” from the Lease – the value of the rent for the period of time during which LAA was a tenant. LAA has paid in full for that tenancy under the terms of the Lease.

¹⁰⁶ *Municipality of Anchorage v. Schneider*, 685 P.2d 94, 97 (Alaska 1984).

¹⁰⁷ *Property Owners Ass’n*, 781 P.2d at 574.

¹⁰⁸ Contract Claim at 14.

¹⁰⁹ Contract Claim at 15-16.

In *Earthmovers*, the case upon which 716 relies almost exclusively, the court declined to grant *quantum meruit* recovery to the contractor because there had been no “benefit” to the State and therefore the contractor would receive no payment for the preparatory work it performed (which was not used by the State).¹¹⁰ Here, however, 716 billed LAA for rent of the Building for nearly two years. Since LAA moved into the Building, it will have paid 716 \$6,059,759.55 in rent and another \$1,119,262.77 in utilities and operating costs for its tenancy up through October 2016, plus \$7.5 million for tenant improvements.

716’s damages calculation necessarily assumes that the Building will have zero value after the Lease is terminated. 716 contends that it will be impracticable to re-let the Building when LAA exits and that 716 will therefore lose the entirety of its investments. Even assuming, however, that the termination of the Lease constituted a breach by LAA of some obligation under the Lease, 716 would still have a duty to mitigate its damages.¹¹¹ 716 has provided no evidence of any such attempt to re-let the Building, despite the fact that it admits being on notice that the Legislature would be exiting the Building since at least May 2016. Based on the facts presented in the Contract Claim, I find that 716 failed to take reasonable steps to mitigate its alleged damages. The information presented by 716 includes an estimate of rental value for the Building as of June 1, 2014, showing that the agreed-upon rent for LAA was 86.48% of the market rent.¹¹² Therefore, even if 716 agreed to re-let the Building for roughly 13.5% less than the market rate as it existed in mid-2014, 716 would suffer no damages by LAA’s exit from the Building. 716’s failure to market the Building or to seek alternative tenants may cause it additional damages, but those are not damages for which LAA is responsible.

Leaving aside 716’s duty to mitigate its alleged damages, the Building continues to have substantial value. This is not an instance where a contractor started mobilization efforts for a project and then was prevented from proceeding with the work, effectively rendering those efforts worthless, as was the case in *Earthmovers*. The Building is a highly valuable commercial building that can be leased or sold. 716’s Contract Claim seeks the full value of all work performed as though the Building was now demolished or worthless. Despite 716’s certification that the supporting data for its Contract Claim are accurate and complete, the data are clearly lacking as to (1) the amount of money spent on the Building; (2) 716’s efforts to mitigate its damages; and (3) the residual value of the Building. This provides an alternative basis for the denial of 716’s claim.

V. CONCLUSION

The Alaska Constitution requires legislative appropriations to cover all government

¹¹⁰ *Earthmovers of Fairbanks, Inc.*, 765 P.2d at 1371.


¹¹¹ *Alaska Children’s Servs., Inc. v. Smart*, 677 P.2d 899, 902 (Alaska 1984) (“The duty to mitigate damages is a well-recognized rule of contract law in Alaska.”); *O’Brien v. Black*, 648 A.2d 1374, 1376 (Vt. 1994) (“In recent years, almost all courts which have faced the question have refused to allow landlords to recover money from a defaulting tenant in damages when the landlord could have avoided those damages by leasing the premises to another with no greater risks to the landlord than he assumed under the original lease.” (quoting 5 A. Corbin, Corbin on Contracts § 1039A (Supp. 1993))).

¹¹² See Ex. 30 at 3, 99.

expenditures. The Lease reflected the risk that the Legislature might not appropriate rent payments beyond the first year of the Lease and allocated this risk accordingly: it required upfront payment of \$7.5 million for tenant improvements, which LAA has paid, and it required 90 days' notice of termination, which LAA gave, so that 716 could mitigate any potential damages by re-letting the Building. Because the Legislature decided not to appropriate further Lease payments consistent with its constitutional authority, which the Lease terms reaffirm, the Contract Claim fails.

VI. FINAL DECISION – APPELLATE RIGHTS

This is the final decision of the procurement officer. This decision may be appealed to the Legislative Council. If you appeal, you must file a written notice of appeal with the Legislative Council within 14 days after you receive this decision.



Senator Gary Stevens
Procurement Officer
October 6, 2016