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Date: October 31, 2013

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Subject: GREC LLC Dispute - Equitable Adjustment Analysis

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Memorandum

From: Tim McDermott

To: File

Date: October 31, 2013

Subject: GRU/GREC: Memorandum analyzing Equitable Adjustment for Change of Law

This memo analyzes and discussed the following issues:

1) Whether the City of Gainesville ("City") has a basis to file an action against Gainesville Renewable Energy Center, LLC ("GREC") in court rather than arbitration for declaratory relief declaring the Equitable Adjustment for Change of Law agreement ("Equitable Adjustment agreement") void because it constituted an ultra vires act, noting that the Power Purchase Agreement ("PPA") contains an arbitration clause for dispute resolution;

(2) Regardless of the forum, the elements and viability of a cause of action for declaratory relief alleging an ultra vires act on the part of Mr. Hunzinger (and possibly Mr. Manasco) in executing/approving the Equitable Adjustment agreement; and

(3) the meaning of the word "implement" under Florida law in the context of the City Commission's May 7, 2009 action that authorized Mr. Hunzinger "to take all steps as may be necessary to implement the terms of the PPA . . ."

Basis to File An Action in Court

The PPA contains an arbitration provision at section 24.2 which provides, in pertinent part, that "[a]ny controversy, dispute or claim between Seller [GREC] and Purchaser [City] arising out of or relating to this Agreement, or the breach thereof, shall be settled finally and conclusively by arbitration . . . unless the parties mutually otherwise agree."

The Florida Supreme Court in *Jackson v. Shakespeare Foundation, Inc.*, 108 So.3d 587 (Fla. 2013), recently analyzed Florida law governing arbitration provisions. "Generally, the three fundamental elements that must be considered when determining whether a dispute is required to proceed to arbitration are: (1) whether a valid written agreement to arbitrate exists; (2) whether an arbitrable issue exists; and (3) whether the right to arbitration was waived." *Jackson* at 593.

It is clear that a valid written agreement to arbitrate exists by virtue of the PPA. One potential argument is that the Equitable Adjustment agreement is void ab initio as an ultra vires act and, as a result, a void Equitable Adjustment agreement cannot form the basis of an obligation to arbitrate.

As discussed in *Jackson*, Florida law recognizes two types of arbitration provisions: narrow and broad. *Jackson* at 593. "[A]n arbitration provision that is considered to be broad in scope typically requires arbitration for claims or controversies 'arising out of *or relating to*' the subject contract." *Id.* (emphasis in *Jackson*). "The addition of the words 'relating to' broadens the scope of an arbitration provision to include those claims that are described as having a 'significant relationship' to the contract – regardless of whether the claim is founded in tort or contract law." *Id.* Accordingly, the arbitration provision within the PPA is a "broad" arbitration provision.

Thus, the analysis shifts to whether a claim that the Equitable Adjustment is void as an ultra vires act has a "significant relationship" to the PPA. "A 'significant relationship' between a claim and an arbitration provision does not necessarily exist merely because the parties in the dispute have a contractual relationship." *Jackson* at 593. "Rather, a significant relationship is described to exist between an arbitration provision and a claim if there is a 'contractual nexus' between the claim and the contract." *Id.* "A contractual nexus exists between a claim and a contract if the claim presents circumstances in which the resolution of the disputed issue requires either reference to, or construction of, a portion of the contract." *Id.* "More specifically, a claim has a nexus to a contract and arises from the terms of the contract if it emanates from an inimitable duty created by the parties' unique contractual relationship." *Id.* "In contrast, a claim does not have a nexus to a contract if it pertains to the breach of a duty otherwise imposed by law or in recognition of public policy, such as a duty under the general common law owed not only to the contracting parties but also to third parties and the public." *Id.*

GREC has drafted the Equitable Adjustment agreement with extensive references to the PPA. It will make the argument that the Equitable Adjustment agreement deals with pricing and the change-in-law provision expressly addressed in the PPA and that it has a significant relationship to the PPA. Additionally, GREC would likely point to section 8.5 of the PPA which provides that, in the event of a billing dispute, the undisputed amount shall be paid and that "[t]he remaining disputed amount shall be subject to the dispute resolution procedure in Section 24, *Dispute Resolution*." It will likely cast the City's claims as a dispute about pricing contemplated by the PPA for resolution by arbitration.

In assessing the issue of a "court forum" or an "arbitration" forum for the potential resolution of this dispute, you should be aware of the oft-quoted maxim that "[c]ourts generally favor [arbitration] provisions, and will try to resolve an ambiguity in an arbitration provision in favor of arbitration. *Jackson* at 593.

Ultra Vires Act

In *Liberty Counsel v. Florida Bar Board of Governors*, 12 So.3d 183, 191 (Fla. 2009), relying on *Black's Law Dictionary*, the Florida Supreme Court explained an "'ultra vires' act as one that is 'unauthorized; beyond the scope of power allowed or granted by a corporate charter or by law.'" The Florida Supreme Court recognized that "Florida courts have held that a municipality, county, or town engages in an 'ultra vires' act when it lacks the authority to take the action under statute or its own governing laws." *Id.* at 191-92 (citing *Lykes Bros., Inc. v. City of Plant City*, 354 So.2d 878, 880 (Fla. 1978) and *Town of Lauderdale-by-the-Sea v. Meretsky*, 773 So.2d 1245, 1249 (Fla. 4th DCA 2000)).

In *Crowell v. Monroe County*, 578 So.2d 837, 837 (Fla. 2d 1991), the Court found that "'extension letters' sent by [an] Assistant Building Official" which "were beyond the building official's authority under [the applicable] County Code" "were ultra vires acts and were void ab initio." The Court expressly rejected the plaintiff's estoppel argument. *Id. See also, Santa Rosa County v. Gulf Power Company*, 635 So.2d 96, 102 (Fla. 1st DCA 1994) (Court concluded counties' grant of franchises "must be considered *ultra vires* and of no effect," and that "counties cannot be estopped from denying the validity of acts that exceeded their delegated powers.") and *Richbon, Inc. v. Miami-Dade County*, 791 So.2d 505, 507 n. 5 (Fla. 3d DCA 2001) ("The Miami-Dade County Code authorizes resolutions granting applications to include reasonable conditions which must be met. There were no conditions attached to this approval by the county commission, the only entity empowered to attach conditions to county commission resolutions. Any conditions attempted to be attached by other boards or the county staff are ultra vires and void.")

If the City challenged the actions of Mr. Hunzinger entering into the Equitable Adjustment agreement, it is expected that he would likely seek to counter that attack by alleging that he was "authorized" to enter into that agreement, in two ways.

First, he will likely argue that he was "prospectively authorized" by the City Commission to execute the Equitable Adjustment agreement by virtue of the Commission's May 7, 2009 action, when it authorized him "to execute such documents and take all steps as may be necessary to implement the terms of the PPA . . ." He will likely argue that since one of the terms of the PPA was implementing the Section 3.2 "Change in Law" provision, his decision to approve and execute the Equitable Adjustment agreement was within that authority. A review of the second "WHEREAS" clause in the Recitals of Equitable Adjustment agreement itself makes clear that it was drafted with this very argument in mind. It is likely that Mr. Hunzinger will

seek to bolster his claim that he was supposedly authorized by pointing to the 'certification' that was signed by the "Utilities Attorney," Raymond Manasco, that the document was approved by its staff counsel "as to form and legality." (Note that a response to this point is addressed below).

Second, he will likely argue that even if he did not receive prospective authority from the City Commission in its May 7, 2009 action, he nonetheless had authority under the Commission's Resolution #060732, which established the "Purchasing Policy" of City employees. Specifically, he will likely argue that Section 7.1(1) establishes an exception under which no City Commission approval is required if the action in question constitutes an "adjustment to a contract . . . previously approved by the City Commission which . . . constitutes an addition to the purchase amount of ten (10%) percent or less of the previously approved amount." He will likely argue that the PPA, which the Equitable Adjustment agreement "adjusts," was "previously approved by the City Commission" on May 7, 2009, and that the cost of the Equitable Adjustment falls within this 10% adjustment ceiling allowance, even if the total dollar amount of this adjustment is approximately $105 million. We understand that the overall cost of the Equitable Adjustment agreement, if paid, would amount to approximately 3.5% of the total contract cost, over its 30 years of operation. His likely argument will be that he was authorized to enter into the Equitable Adjustment agreement because the overall "cost" of the "Change in Law" provision was less than 10% of the total contract cost previously approved by the City Commission. He may also argue that other exceptions under Section 7.1 apply.

Based upon the preliminary facts made available to us (and subject to expansion, based upon discovery and further investigation), it appears that the City does have viable arguments and evidence to support a claim that the action of Mr. Hunzinger in approving and executing (via Ms. Hunt) the Equitable Adjustment agreement, and the action of attorney Raymond Manasco in approving the Equitable Adjustment agreement as to "form and legality," constitute ultra vires actions that were not "authorized." Those arguments and evidence include the following:

1. Neither the May 7, 2009 City Commission action authorizing Mr. Hunzinger, or his designee, to "implement" the terms of the PPA, nor the Purchasing Policy was ever intended to apply to action that obligated the City to pay another approximately $105 million dollars on the PPA contract over its life, which contract was, by Mr. Hunzinger's own admission to the City Commission during the May 7th meeting, "probably the biggest commitment for GRU and the city since Deerhaven 2. And certainly will likely be one of the biggest decision points for many years to come.";

2. Even if the action of the City Commission on May 7, 2009 is construed to have provided Mr. Hunzinger with prospective authorization to "implement" the terms of the PPA in a manner that would apply to an adjustment of this financial magnitude, his action in approving and executing (via Ms. Hunt) the Equitable Adjustment agreement does not "implement" the terms of the PPA but, instead, is

in derogation of its terms since his actions obligate the City to pay out another $105 million dollars for costs that do not fall within the scope of Section 3.2; and

3. Even if the Section 7.1(1) exception in the Purchasing Policy can be construed to mechanically apply to his execution of the Equitable Adjustment agreement (i.e., the cost of the Equitable Adjustment is within the 10% maximum allowance otherwise permitted by that Policy), his action in approving and executing (via Ms. Hunt) the Equitable Adjustment agreement is not authorized under that Section, because it only applies to "an addition to the purchase amount of ten (10%) percent or less **of the previously approved amount**" (emphasis added). The City Commission did not previously approve **any amount** to be paid under Section 3.2 for any cost that was not, in fact and law, an additional cost resulting from a "Change in Law." Phrased somewhat differently, only additional generating or selling costs of up to 10% of the contract amount, **that result from "Changes in Law,"** qualify for payment authority under the Purchasing Policy. The costs reflected in the Equitable Adjustment agreement are not from "Changes in Law."

4. The Equitable Adjustment agreement is not an implementation of the "Change in Law" provision, or an "adjustment" to the PPA but, in fact and law, is actually a "settlement agreement" for an amount of over $50,000 in value for which he obligated the City and for which he needed prior City Commission approval which he did not receive. If one reads the document itself, it has all the attributes of a "settlement agreement," including "Whereas" clauses and a de facto release and satisfaction of supposed claims held by GREC.

5. Mr. Hunzinger is not a lawyer. He is an engineer. He has no competency to make a legal determination as to what is, or is not, a "change in law." He must rely on experienced counsel for that assessment.

6. Mr. Hunzinger knew of the extreme financial consequences and other significance that the PPA had to the City. In fact, at the May 7, 2009 Commission meeting, his recognition of that fact is established by his characterization of the PPA as being "probably the biggest commitment for GRU and the city since Deerhaven 2. And certainly will likely be one of the biggest decision points for many years to come.".[1] He arguably knew that a change that obligated the City to pay another $105 million on this contract over its life was required to have been brought back to the City Commission for its approval, just like the changes to the PPA that he

[1] The President of GREC, and other of its high ranking officers, were present at that May 7, 2009 City Commission meeting and would have heard this candid assessment. Their own comments to the City Commission that day did not challenge or qualify the magnitude of the PPA contract to the City. This recognition by them may bear on the issue of any purported "reasonable reliance" they allege they placed on any claimed "apparent authority" that Mr. Hunzinger had regarding the PPA.

brought back to the City Commission in May of 2009 for its approval, and for which he made the PPA subject to City Commission ratification.

7. Prior to approval of the Equitable Adjustment, and very early on, Mr. Hunzinger was told by one of his experienced Assistant Managers, John Stanton, that Mr. Stanton "emphatically" felt that what GREC was proffering as a Change in Law was not a "Change in Law." (See Stanton's email of 1/18/11 to Regan and Manasco, the contents of which we understand that Mr. Stanton related to Mr. Hunzinger orally). Mr. Stanton recommended that a legal opinion on the issue be provided.

8. The Orrick law firm provided a robust, thorough legal opinion, in writing, dated December 20, 2010, in which it unequivocally opined that the arguments and grounds advanced by GREC did **not** constitute any "change in law." Since Mr. Hunzinger had relied upon Orrick's opinions at every stage of the PPA, and since Orrick had been long-time outside counsel to GRU with respect to other GRU matters, there was no reason for him to challenge the merit or accuracy of its opinion on this issue. Moreover, if he did disagree with that opinion, one would expect that he would have immediately challenged Orrick on its opinion or otherwise discussed any differences of opinion he had with their legal opinion. We understand that no such discussion or challenge occurred. (The Equitable Adjustment agreement was executed in March of 2011, after Mr. Hunzinger had received the Orrick opinion months before. We understand that Carl Lyons of Orrick has informed the City Attorney that after his firm issued that opinion, it did not hear of any other issue with respect to the Change in Law matter and was not consulted with respect to Mr. Hunzinger's execution of the March, 2011 'Equitable Adjustment' document).

9. We understand that Mr. Hunzinger was also orally told by the Utilities Attorney, Raymond ("Skip") Manasco, that Mr. Manasco did not believe that grounds proffered by GREC constituted any "change in law" under the PPA, and that Mr. Manasco was involved in requesting the written opinion from Orrick. We understand that he also agreed with Orrick's opinion. (We understand that Manasco also candidly admitted to the City Attorney recently that in the period prior to his retirement he had signed a number of documents that he "probably should not have signed." If Mr. Hunzinger put pressure on Mr. Manasco to approve of the "form and legality" of the "Equitable Adjustment document, in the face of the Orrick opinion and what we understand to be the Manasco-expressed opinion, that will be further evidence of the ultra vires nature of Mr. Hunzinger's action, and possibly that of Mr. Manasco as well. It may be, however, that Mr. Manasco viewed the "approval as to form and legality" statement on the Equitable Adjustment agreement as being more perfunctory in nature, and not of the import that GREC may now allege it to be).

10. The City Attorney at the time, Marion Radson, did not approve of the Equitable Adjustment document and was not asked to review that document before Hunzinger signed it. While he was aware of the Orrick written opinion at the time, he believed that such opinion "was the end of that issue," given the unequivocal conclusion that Orrick reached in that opinion. He was not consulted or informed to the contrary thereafter, by Mr. Hunzinger, Mr. Manasco or otherwise.

11. We understand that John Stanton believes that Mr. Hunzinger specifically scheduled the date of the execution of the Equitable Adjustment agreement to take place when Mr. Hunzinger knew that Mr. Stanton would be out of the office.

12. We understand that Ms. Jennifer Hunt, GRU's Chief Financial Officer, has informed you that she was asked by Mr. Hunzinger to sign the Equitable Adjustment agreement since he was out of the office. We further understand that she was never informed of the Orrick legal opinion that concluded that the grounds submitted by GREC did not constitute a "change in law" under the PPA, and that had she been told, she would not have executed that document.

13. We understand that when the fact and magnitude of the Equitable Adjustment agreement only recently surfaced to the attention of the Mayor and the City Attorney, that the Mayor and the City Attorney promptly met with Mr. Hunzinger to discuss the surrounding facts with him. We understand that when they asked Mr. Hunzinger directly if he believed that the Equitable Adjustment actually reflected an actual "change in law," he did not answer that question directly. Instead, he responded by citing to Mr. Regan's claimed belief (who, like Mr. Hunzinger, is also not a lawyer) that the grounds proffered by GREC did constitute a "change in law," and Mr. Hunzinger's stated belief that he, Hunzinger, felt he had to go ahead and sign the Equitable Adjustment agreement because Mr. Regan had allegedly told the GREC people that he, Regan, felt that it was a "change in law." (Mr. Hunzinger knows that Mr. Reagan is not a lawyer). While Mr. Hunzinger repeatedly told the Mayor and the City Attorney that he signed the Equitable Adjustment for "business reasons," he refused or was unable to identify any such "business reason," even after repeated questioning from them in that regard. He also alluded to attorney Manasco's signature as to the "form and legality" of the Equitable Adjustment document.

Definition of "Implement"

An assessment of a claim by the City that Mr. Hunzinger's actions in approving signing (via Ms. Love) the Equitable Adjustment agreement includes, in part, an analysis of the concept of the term "to implement." In *Florida Department of State v. Florida State Conference of NAACP Branches*, 43 So.3d 662, 671 (Fla. 2010), Justice Canady's dissent offered the following definition of the word "implement":

> "Implement" means "to carry out: accomplish, fulfill." *Webster's Third New Int'l Dictionary of the English Language, Unabridged* 1134 (1993). More particularly, "implement" means "to give practical effect to and ensure of actual fulfillment by concrete measures." *Id.*

Applying this definition to the language of the Equitable Adjustment, GREC will likely argue that the authority to "implement" the PPA includes executing amendments and modifications to the PPA including the Equitable Adjustment, particularly because the Equitable Adjustment was contemplated by Section 3.2 of the PPA.

The City's counter argument is that such an argument by GREC would represent an improperly superficial analysis of the issue which would ignore the very definition of "implement." Specifically, the authority to "implement" the PPA did not vest Mr. Hunzinger with authority to modify or amend the PPA to authorize costs which were not authorized under its existing provisions. More specifically, "to implement" the terms of the PPA, pursuant to the definition outlined above, means that Mr. Hunzinger's action must be **in furtherance of the PPA terms**, i.e., in furtherance of its "actual fulfillment." If the grounds for the extra costs advanced by GREC did not actually constitute a "Change in Law," then Mr. Hunzinger was not authorized to execute or sign (via Ms. Love) an Equitable Adjustment that agreed to pay for those costs. His actions in that regard would appear to be ultra vires. While his state of mind is perhaps not legally necessary to the assessment, if it proves that he also knew, or should have known, that those grounds did not constitute "Change in Law," but he approved/signed off anyway, that circumstance would likely improve the argument that his actions were ultra vires. We know that he received a very thorough assessment of that issue by the Orrick firm, and that he apparently disregarded their legal opinion altogether. Under this assessment, if the grounds advanced by GREC did not amount to a "Change in Law," then any approval of those costs by Mr. Hunzinger would not be to "implement" the terms of the PPA, but, instead, would be in "derogation" of those terms, and not "in fulfillment" of those terms.

As noted, the City will likely need to address the defense/argument that GREC will be expected to make that the fact that the "Utilities Attorney" "approved" the Equitable Adjustment

agreement as "to form and legality," precludes/estops the City's contemplated argument that the Equitable Adjustment agreement is ultra vires. As noted in the case law cited above, there is a heavy burden to establish estoppel against a municipality from enforcing its laws. Some Florida Statutes require a government agency's attorney to sign agreements approving "form and legality." *See, e.g.*, §§ 253.025(7)(h) and 287.059(4), Fla. Stat. We need more facts to determine whether the City has a similar ordinance or charter requirement. If attorney Manasco orally advised Mr. Hunzinger that the grounds proffered by GREC did not constitute any "Change in Law," (as we understand to have been the case), but Mr. Manasco nonetheless approved the document as to its "legality" due to pressure imposed upon him by Mr. Hunzinger, that 'approval,' in turn, may have been 'ultra vires' as well. There is no Florida case law that has been identified in our research as to the meaning and import of this approval. There is also a question as to whether this approval is intended strictly for the benefit of the governmental employee (in which case an argument can be made that a third party such as GREC has no legal right to rely in any respect on that approval), or whether it is intended to be relied upon by third parties, and if so, under what circumstances and to what degree.