No. 29,911 consolidated with
No. 30,069

IN THE COURT OF APPEALS
OF THE STATE OF NEW MEXICO

BOARD OF EDUCATION FOR THE
QUESTA INDEPENDENT SCHOOL DISTRICT,

Plaintiff-Appellant,

vs.

ARTESANOS DE QUESTA, a non profit corporation, and NANCY GONZALES, in her individual capacity as owner and operator of the Carinos Day Care Center, her private business,

Defendants-Appellees.

REPLY BRIEF

On Appeal from the Eighth Judicial District Court
for the State of New Mexico The Honorable Sam B. Sanchez

ORAL ARGUMENT IS REQUESTED

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Statement Regarding Transcript Citations

The official trial transcript is an audio recording consisting of eight compact discs. Citations to the trial transcript are included in the following form: [CD 1, 8-22-07, x:y:z], [CD 2, 8-22-07, x:y:z], [CD 3, 08-22-07, x:y:z], [CD 4, 08-22,07, x:y:z], [CD 1, 9-19-07, x:y:z], [CD 2, 9-19-07, x:y:z], [CD 1, 10-18-07, x:y:z], and [CD 2, 10-18-07, x:y:z], where "x:y:z" refers to the specific counter at which the recording can be located.

Statement of Compliance

Pursuant to Rule 12-213(G) NMRA, this brief complies with the type-volume limitations set forth in Rule 12-213(F)(3) NMRA, because it is prepared in a proportionally-spaced typeface, 14 point Times Roman, and the body of the brief contains 4,222 words according to Microsoft Word 2007.

TABLE OF AUTHORITIES

NEW MEXICO CASES

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ARGUMENT

I. Appellees Completely Ignore the Relevance of This Court's Prior Holding in *UU Bar Ranch.*

The primary area of inquiry on appeal pertains to this Court's prior holding in *State of New Mexico ex rel. Madrid v. UU Bar Ranch Ltd. Partnership,* 2005-NMCA-079, 137 N.M. 719, 114 P.3d 399. Again, *UU Bar Ranch* stands for the proposition that where a statute, pertaining to the disposition of publicly owned property, contains nondiscretionary language, State Board of Finance approval is required. While Appellees attempt to direct this Court's attention to the equitable affirmative defenses, the paramount issue here relates to whether obtaining approval from the State Board of Finance in and of itself invalidates the underlying lease agreement. Appellees do not substantively address this issue, thus by implication, they recognize that if in fact *UU Bar Ranch* is binding authority they, as a matter of law, cannot prevail. Rather, Appellees argue that *UU Bar Ranch* is "distinguishable and does not control." **[AB 37-38]** Appellees contend that *UU Bar Ranch* is distinguishable because, in that case, the parties were attempting to establish title to state owned property. **[AB 38]** In the present matter, Appellees argue that Artesanos is not trying to establish title to the La Cienega school. This argument is entirely misplaced.

First, there is no question that a term of the lease agreement relates to a provision entitling Artesanos to purchase the La Cienega property at the close of

the 25 year lease term. As such, while title to the property is not at issue currently, there is no question that title to the property will ultimately become an issue in the event Artesanos is allowed to continue to occupy the property throughout the remaining term of the lease agreement. Thus, disposition of the property from QISD, a public entity, to Artesanos, a private party, is without question a potential outcome. Thus, obtaining prior approval from the State Board of Finance was critical under the applicable statute, NMSA 1978, § 13-6-2.1 (2003), since title to the property will ultimately be transferred from a governmental entity to a private party.

Next, Appellees incorrectly confuse the issue pertaining to the mandatory language contained in Section 13-6-2.1. Appellees argue that the issue of estoppel must be addressed in the first instance and that the validity of the lease is of no consequence in the event this Court concludes that estoppel can be applied against the school district. This level of analysis is in no way supported by the holding in *UU Bar Ranch*. *UU Bar Ranch* clearly establishes that in the absence of obtaining State Board of Finance approval for the disposition of publicly owned property, the underlying agreement pertaining to the disposition of the property must be held invalid. 2005-NMCA-79, ¶ 19. In *UU Bar Ranch,* the Court ruled that the language set forth in the statute was clear and unambiguous and, further, that the language was mandatory. *Id.* The same conclusion should result here considering

that the statute at issue in *UU Bar Ranch* and in this case are nearly identical. Appellees simply come forward with no reasonable explanation as to why the Court's holding in *UU Bar Ranch* related to the mandatory, non-discretionary language contained in the case should not be applied in the present matter.

Finally, Appellees note that private parties will be deterred from engaging in such transactions with a state agency or political subdivision if the holding in *UU Bar Ranch* is enforced in this matter. However, the overarching concern here must relate to the public interest in ensuring that transactions of this type are properly approved by the State Board of Finance as required under state statute. The public policy governing Section 13-6-2.1 is clear—when public property is being disposed of there must be approval by the State Board of Finance in order to ensure that the public interest is protected. Protecting public property is paramount and that interest certainly outweighs the private, proprietary interest that is being advocated by Appellees.

II. Equitable Estoppel Should Not Be Applied Against Appellant, and the Remaining Equitable Doctrines are Likewise Inapplicable.

A. Appellant preserved the equitable estoppel argument at trial.

Appellees initially argue that Appellant did not preserve the equitable estoppel argument in the underlying proceeding. This proposition is a misstatement of what occurred below. The record clearly reflects that the District Court's attention was directed to the equitable estoppel issue on multiple occasions

when referencing this Court's prior holding in *UU Bar Ranch*. In its Pre-Trial Order and Findings of Fact and Conclusions of Law, Appellant argued that *UU Bar Ranch* was binding upon the Court and that the lease, in and of itself was invalid, and as a result equitable doctrines could not be applied. Further, Appellant again raised the issue pertaining to *UU Bar Ranch* in its Docketing Statement and Memorandum in Support of Summary Disposition.

Appellees refer this Court to Rule 12-216(A) NMRA in support of their argument that the equitable estoppel issue was not properly preserved. However, Rule 12-216(A) establishes that the issue was properly preserved since the rule specifically provides that "formal exceptions are not required, nor is it necessary to file a motion for a new trial to preserve questions for review." It is well-settled that an issue is preserved on appeal if the appellant has "fairly invoked a ruling of the trial court on [the] same grounds argued on appeal." *Martinez v. N.M. State Eng'r Office*, 2000-NMCA-074, ¶ 46, 129 N.M. 413, 9 P.3d 657. Clearly, the District Court adopted Appellees' reasoning that the equitable doctrines should be applied and that *UU Bar Ranch* was not binding authority. In sum, it is clear that the issue of equitable estoppel was raised at trial on numerous occasions—in particular, with reference to the *UU Bar Ranch* holding.

B. Equitable estoppel should not be applied against Appellant as a political subdivision of the state.

Appellees argue that as a political subdivision of the state, QISD is more like a municipal corporation than the state and, therefore, equitable estoppel should be applied without limitation. Appellees rely on various treatises and case law from other jurisdictions for this proposition. They do not, however, cite to any New Mexico cases that would establish that school districts are akin to municipal corporations under factual circumstances similar to this case.[1] Appellees' analysis requires this Court to step beyond applicable case law and would carve out a new exception to the equitable estoppel rules which are applied to public entities, such as school districts and other political subdivisions in the state of New Mexico.

First, there is no question that under applicable law QISD is a political subdivision of the state and is protected from suit in numerous contexts. With regard to tort litigation, school districts, like the state of New Mexico, are protected from suit under the New Mexico Tort Claims Act. *See* NMSA 1978, §§ 41-4-1 to -30 (as amended through 2010). In the realm of contractual disputes, NMSA 1978, Section 37-1-23 (1976) provides immunity to governmental entities, including school districts, from liability based upon contract disputes where an unwritten contract is at issue. Appellees argue that, when the principle of sovereign immunity "wanes in importance," the courts should likewise not be reluctant to

[1] To the contrary, New Mexico case law clearly establishes that school districts do not operate in a proprietary capacity. In *Silver City Consolidated School District v. Board of Regents of New Mexico Western College*, 75 N.M. 106, 112 (1965), the New Mexico Supreme Court held that: "While there are undoubtedly some decisions to the contrary, in our view, the operation of a school by a state institution is a governmental rather than a proprietary function."

apply equitable estoppel against the state and/or a political subdivision. **[AB 28]** However, based upon the protections still afforded school districts, under the TCA and Section 37-1-23, it is clear that insulating the public interest from suit in the context of a school setting is still paramount. Thus, in New Mexico, school districts, while considered political subdivisions of the state, are afforded similar protections against suit. Adopting Appellees' analysis would require this Court to create a distinction that is not supported by applicable law. Thus, the limited application of equitable estoppel afforded to the state should likewise be afforded to political subdivisions such as QISD.

Next, Appellees incorrectly cite to *Silver City Consolidated School District* for the proposition that equitable estoppel has been applied in New Mexico against a public school. 75 N.M. 106, 401 P.2d 95. Even a cursory reading of the case establishes that the Court held that equitable estoppel would be applied against the university in large part because the "controversy [was] between a public agency and a governmental subdivision." *Id.* at 111, 401 P.2d at 99. This distinction is critical in this matter since the dispute is between a public entity and a private party, not two public entities. Thus, the underlying transaction would result in disposition of public property from the public to a privately owned interest.

C. Equitable estoppel is inapplicable based upon Artesanos' conduct.

In the event this Court concludes that equitable estoppel, or any of the other equitable doctrines, should be applied against QISD, this Court must likewise evaluate Artesanos' conduct. *See Kilmer v. Goodwin*, 2004-NMCA-122, ¶ 128, 136 N.M. 440, 99 P.3d 690. Appellees argue that as a general rule equitable estoppel will be applied against governmental entities only when a statute so provides or when right and justice demand it. *See N.M. Tax. & Rev. Dept. v. Bien Mur Indian Mkt. Ctr.*, 108 N.M. 228, 230, 770 P.2d 873, 875 (1989). Here, Appellees cite to no statutory authority which allows for the application of equitable estoppel against QISD. Thus, the Court must consider whether "right and justice demand it." The facts unquestionably establish that Artesanos' conduct precludes application of equitable estoppel or any of the other equitable doctrines.

As noted in prior submissions to this Court, the evidence produced at trial established that Artesanos materially breached a number of provisions within the lease, thereby, leading to default by Artesanos. The violations, include but were not limited to the following: (1) use of the premises for purposes other than "cultural opportunities," (2) failure to seek prior written approval of assignment or sublease of any interest to the property to Cariños Day Care Center, (3) failure to seek prior written consent for different use of the premises,[2] (4) failure to provide

[2] At trial, Ramon Vigil testified that Artesanos failed to obtain approval from Appellant for the operation of the Cariños Day Care Center. **[CD 1, 03/02/09, 11:42:52-11:44:42]**

property and liability insurance,[3] (5) failure to maintain the premises in good repair, (6) failure to pay all utilities and services in connection with the property, and (7) failure to provide rent or "in-kind" services as provided by Attachment A to the purported lease. **[Pl. Exs. 6, 7; CD 1, 03/02/09, 11:42:52-11:44:42]** Thus, for Artesanos to now come before this Court and argue that QISD "accepted all benefits provided by Artesanos under the Lease" is a blatant misstatement of the facts. **[AB 33]** There can be no question that there is a substantial taint from Artesanos' fundamental failure to comply with the terms outlined in the lease. QISD received little benefit from Artesanos as established by Artesanos' failure to provide the services and/or other compensation outlined in the underlying agreement.

D. The remaining equitable doctrines are likewise inapplicable.

Appellees' reliance on the remaining equitable doctrines of laches and waiver is similarly baseless. As noted above, *UU Bar Ranch* is binding authority upon this Court. Again, where the language of a statute is mandatory and non-discretionary, equitable doctrines, including laches and waiver, will not be liberally applied. **[*See* BIC 27-31]** Further, Appellees continue to rely on the argument that as a "municipal corporation" laches should be applied against QISD. **[AB 40]** Again, there is no case law supporting Appellees argument that a political

[3] No such evidence of insurance prior to 2007 was presented by Artesanos in discovery responses, which were attached as trial exhibits. **[*See* Pl. Exs. 1, 2]**

subdivision, such as QISD, should be held to the legal standard applied against municipal corporations in other jurisdictions. Similarly, the doctrine of unclean hands is closely related to the doctrine of estoppel. *See Medina v. Medina*, 2006-NMCA-042, ¶ 25, 139 N.M. 309, 131 P.3d 696. Thus, QISD incorporates by reference the arguments raised above pertaining to estoppel in reference to Appellees' contention that the doctrine of unclean hands should be applied in this matter.

E. Appellees' request to be made "whole" is untimely.

In their Answer Brief, Appellees request that this Court make them "whole" based upon the "large sums of money" it expended to repair the La Cienega property. It is QISD's position that Artesanos did not file a counterclaim for such relief in the underlying proceeding, the District Court made no such award at trial, and to request such compensation at this juncture is untimely. Simply put, Appellees failed to preserve this issue in the underlying proceeding.

III. Substantial Evidence Did Not Support Findings Regarding Appellees' Breach of the Real Estate Lease.

Appellees were required by the lease to maintain liability insurance on the property which was a material term of the lease agreement. **[Def. Ex. 3; RP/A 5-64]** In addition, any modification of the lease had to be in writing. From this requirement, Appellees have essentially bobbed and weaved over time, including taking a position at trial that conflicted with other evidence and with a legal

requirement that would not allow an oral modification of a contract with a state public entity. In response, Appellees argue that someone, at some undefined time, told Appellees it would be acceptable to orally modify that portion of the lease agreement, so they did not have to carry insurance on the property. Such a claim is a stretch. Substantial evidence did not support Appellees' findings of fact as they pertain to a breach of the lease agreement for failing to obtain insurance on the property. **[*See* RP/NG 425-34, Def. FOF 27, 30]**

Clearly, the lease required that Appellees obtain liability insurance on the property. This requirement was written into the lease to protect Appellant from any liability. An investigation conducted by Ramon Vigil determined that there were various violations of the lease agreement, including a failure to provide insurance for the property. **[Pl. Exs. 6, 7; CD 1, 03/02/09, 11:42:52-11:44:42]** Mr. Vigil sent numerous correspondence to Appellees requesting copies to confirm that they complied with the terms of the lease requiring insurance coverage. **[Pl. Exs. 5, 25, 26; CD 1, 03/02/09, 11:53:45-11:56:39, 11:58-54-12:01:53]** As demonstrated by the evidence, those requests for confirmation of insurance coverage were repeatedly ignored. Yet, notably, Roberto Vigil, who was the president of Artesanos, did finally address the issue with an October 30, 2007, letter to the Questa Board of Education stating, "The current property insurance

and liability meet state requirements. We are also under the assumption that the district as the owner of the property has insurance as well." **[Pl. Ex. 24]**

Notably, during pretrial discovery, Appellees' Answers to Interrogatories did not state that there was any modification to the lease requirement when they were asked to provide copies of insurance coverage. Those answers were admitted into evidence to demonstrate there was no contention prior to trial that insurance was required. **[Pl. Exs. 1, 2]** To the contrary, Ramon Vigil testified that there was never any insurance policy provided to him in response to his requests to verify insurance coverage, although he did receive an insurance proposal dated May 16, 2008 from Carinos which did not demonstrate any coverage whatsoever and came months after the request for insurance was made. **[CD 1, 03/02/09, 11:56:53–11:57:33; Pl. Ex. Y]**

This application begs the question: if there was an oral modification that released Artesanos from its duty to obtain insurance coverage, then why were there attempts in October 2007 to apply for coverage? If no insurance coverage was required, then why did Artesanos clearly state so in its Answers to Interrogatories?

The same question applies to the earlier correspondence between Mr. Vigil and Artesanos prior to the lawsuit being filed. If no insurance was required to be obtained by Artesanos for the La Cienega property based on an oral modification to the lease agreement, then why did Artesanos not state so up front? It seems far-

fetched that a party to a lease could be so coy and unresponsive about a material term of the lease, and then later argue that it was actually *the other party* who was acting in bad faith.

Substantial evidence does not demonstrate there was an oral modification of the lease. On the contrary, Interrogatories and pre-trial correspondence do not support that there was a claim that the insurance provision of the lease was orally modified since there was never any mention of it. Additionally, one of Artesanos' witnesses thought insurance had actually been procured.

The reality is that despite the fact that there were no claims of an oral modification leading up to trial, Appellees determined that a claim of "oral modification" was the only route they could take to get around this requirement in the lease. So, unsubstantiated testimony was offered by Marcus Rael that a modification occurred. While Appellees imply there was testimony from then-superintendant Nelson Lopez, it is clear that Mr. Lopez offered no such testimony.

It is interesting that in the Answer Brief Appellees state, "At no time between 2000 and 2007 did the School Board ask Artesanos to provide insurance." **[AB 20]** In making this statement, Appellees seemingly ignore the lease agreement itself, which does require insurance. Appellees seem to argue that a term of a contract is no good unless a party requests it over time. Nevertheless, when Mr. Ramon Vigil did request copies of insurance coverage, he was

repeatedly ignored and then misled by Roberto Vigil in his letter of October, 30, 2007. **[Pl. Ex. 24]**

Finally, Appellee does very little to address the legal issues involved to justify its claim that the lease agreement was orally modified. First, the lease was explicit that oral modifications were not allowed. **[Def. Ex. 3; RP/A 5-64]** Any such modification had to be in writing and approved by the parties. The District Court simply ignored this provision.

Secondly, the lease between Artesanos and Appellant had another important component. It was a contract with a government entity, and thus required that it be contained in writing. "[A]ny enforceable contract with a governmental entity must be in writing." *Hoggard v. City of Carlsbad*, 121 N.M. 166, 170 n.1, 909 P.2d 726, 730 (Ct. App. 1995). Here, Appellees claim on one end that they have a written lease agreement. On the other end, though, they claim they have an "oral agreement." Undeniably, the concept of an oral agreement is not supported by law.

The District Court simply ignored this key principle. Aside from the substantial evidence supporting a breach of the lease agreement as it relates to the provision requiring insurance, the trial court allowed an oral modification that is not even tenable under the law. Appellees' contention that no insurance was necessary is not supported by any facts or the law.

IV. The District Court's Award of Attorney Fees was an Abuse of Discretion Because the Court's Findings are Lacking a Factual and Legal Basis and Because There is No Applicable Exception to the American Rule.

Despite Appellees' efforts in their Answer Brief to provide a factual and legal basis for the District Court's award of attorney fees, their arguments are unavailing. Appellees assert that the District Court made "extensive findings" from the bench to support an award of attorney fees under the bad faith exception to the American Rule despite the fact that the District Court never mentioned the American Rule or any exceptions during its ruling. **[AB 46]** In addition, the District Court's findings that Appellees cite in support of applying the bad faith exception are based on pre-litigation conduct, which cannot serve as the basis for an award of attorney fees. *See ACLU v. City of Albuquerque*, 1999-NMSC-044, ¶ 28, 128 N.M. 315, 992 P.2d 866. Moreover, the record does not support an award of attorney fees under the bad faith exception, especially in light of the District Court's denial of Appellees' motions to dismiss and for directed verdict, and the investigation prior to Appellant's filing of the Complaint—arguments which Appellees notably failed to address in their Response.

In an effort to proffer a legal basis for the District Court's award of attorney fees, Appellees argue that the District Court "heard ample evidence of [Appellant's] bad faith." **[AB 45]** However, nowhere in the District Court's ruling did the Court discuss the American Rule or any exceptions to the American Rule.

At no time did the District Court identify the bad faith exception to the American Rule as the legal basis for its ruling. Appellees have proffered such a legal basis after the fact, but at no time did the District Court identify the bad faith exception to the American Rule as the legal basis for its ruling.

Even if the District Court had identified the bad faith exception as the legal basis for its award of attorney fees, the District Court's findings cited by Appellees as support for application of the bad faith exception were based on pre-litigation conduct. For example, Appellees argue that in its ruling, the District Court pointed out that Appellant had to get approval from the State Board of Finance, but failed to do so. **[AB 46]** Appellees also cite to the District Court's finding that Appellant did nothing for seven years, but then decided to "get rid of Artesanos" and fall back on its failure to seek approval of the lease. **[AB 46]** However, a district court's authority to award attorney fees does not extend to conduct that gave rise to the underlying cause of action, or pre-litigation conduct. *See ACLU*, 1999-NMSC-044, ¶ 28 ("The bad faith exception applies to conduct which occurs before the court or in direct defiance of the court's authority."). Failing to get Board of Finance approval for seven years is pre-litigation conduct which cannot form the factual basis for the application of the bad faith exception to the American Rule.

Although Appellees cite to other portions of the record to argue that the District Court heard "ample evidence" of bad faith, Appellees do not assert that the

District Court relied on those portions of the record in its award of attorney fees. For instance, Appellees argue that Appellant requested a continuance of the trial setting to get a property appraisal, but tried to evict Artesanos a second time. **[AB 45]** Even if this were true, Appellees do not cite to the portion of the District Court's ruling to show that the District Court actually relied on this as support for its attorney fee award. Similarly, Appellees argue that prior to filing suit, Appellant knew that Nancy Gonzales had relied on "unsound advice" from a CPA, that the district attorney had declined to prosecute Ms. Gonzales, and that Cariños had reverted to its non-profit status. **[AB 45]** Again, Appellees do not cite to any portion of the District Court's ruling on attorney fees to demonstrate that the District Court based its ruling on these facts.

Moreover, Appellees have mischaracterized the facts in the record. Despite Appellees claim to the contrary, Appellant did not request a continuance from the District Court in order to evict Artesanos. Appellant attempted to terminate the lease due to safety concerns. The safety concerns became critical after three separate assessments of severe property damage were made, and after it was recommended that the building be vacated immediately. **[Pl. Exs. 8, 16; CD 1, 03/02/09, 4:11:19-4:13:33, 5:47-44-5:50:30, 5:50:56-5:53:06; CD 1, 03/03/09, 10:29-39-10:30:22]**

Additionally, even if Appellant was aware, prior to filing suit, that (1) Nancy Gonzales had relied on "unsound advice" from a CPA, (2) that the district attorney had declined to prosecute Ms. Gonzales, and (3) that Cariños had reverted to its non-profit status, this does not change the fact that Appellant's attorney had advised it that the lease was invalid based on the lack of Board of Finance approval and breaches of various lease provisions by Appellees. **[BIC 10-11; Pl. Exs. 6, 7, RP/A 5-64; CD 1 03/02/09, 11:00:43-11:02:43, 11:42:52-11:44:42]** In fact, the record demonstrates that Appellant attempted to renegotiate the lease, but that Appellees responded by asserting that the lease was indeed valid. **[BIC 11-13; Pl. Exs. 4, 24, 25; CD 1, 03/02/09 11:46:41-11:48:32, 11:51:52-11:53:22; 11:58:54-12:01:53]** Contrary to Appellees' assertion, the record demonstrates good faith efforts by Appellant to renegotiate the lease. The record also demonstrates that Appellant only pursued legal action after those negotiations fell through. **[*See* Pl. Ex. 25; CD 1, 03/02/09, 11:58:54-12:01:53]**

Further, Appellees' argument that Appellant had alternatives other than filing suit is not evidence to support application of the bad faith exception. **[AB 45-46]** Just because an alternative to legal action may have existed does not mean that Appellant filed the lawsuit in bad faith, and Appellees cite no legal authority to support such a proposition.

CONCLUSION

Based on the foregoing, Appellant respectfully requests this Court to reverse the District Court's judgment in favor of Appellees as well as its award of attorneys fees.

Respectfully submitted,

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I hereby certify that a true copy of the foregoing pleading was mailed on this 7th day of February 2011 to:

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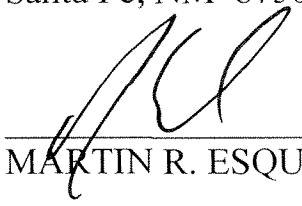

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