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Docket No. 41316-2013

In the Supreme Court of the State of Idaho

NORTH IDAHO BUILDING CONTRACTORS ASSOCIATION, an Idaho non-profit corporation; TERMAC CONSTRUCTION, INC., an Idaho corporation, on behalf of itself and all others similarly situated,

Plaintiffs-Appellants-Cross Respondents

and

JOHN DOES 1-50, whose true names are unknown,

Plaintiffs,

v.

CITY OF HAYDEN, an Idaho municipality,

Defendant-Respondent-Cross Appellant.

FILED - COPY
JUL 18 2014
Supreme Court Court of Appeals
Entered on ATS by

CROSS APPELLANT'S REPLY BRIEF

Appeal from the District Court of the First Judicial District of
The State of Idaho, in and for the County of Kootenai,
Honorable Benjamin R. Simpson, Presiding

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INTRODUCTION

This is the reply brief on the cross appeal of Defendant-Respondent-Cross Appellant City of Hayden ("Hayden" or "City").[1] It follows Hayden's *Response Brief of Respondent and Opening Brief of Cross-Appellant* ("*Hayden's Opening Brief*"). It responds to the *North Idaho Building Contractors Association's Reply Brief and Cross-Appeal Response Brief* ("*Builders' Reply Brief*") of Plaintiffs-Appellants-Cross Respondents North Idaho Building Contractors Association, et al. ("Builders").[2]

The City recognizes that it faces a tough standard in seeking reversal of an exercise of discretion regarding attorney fees. The City suggests, however, that this is one of those cases where abuse of discretion is sufficiently apparent that reversal is appropriate.

To justify reversal, Hayden must show either that (1) the district court failed to recognize the discretionary nature of its decision, (2) that it acted outside the bounds of such discretion or inconsistently with applicable legal standards, or (3) that it failed to reach its decision through an exercise of reason. *Shore v. Peterson*, 146 Idaho 903, 914, 204 P.3d 1114, 1125 (2009). Hayden respectfully suggests that the district court did not meet the second and/or third test. This is because the district court identified clear controlling precedent, explained how each of the Builders' legal arguments was inconsistent with that authority, and then inexplicably concluded that a fee award was not justified because the Builders had litigated in "good faith."

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[1] Plaintiff North Idaho Building Contractors Association ("NIBCA") appealed the judgment entered in favor of the City that was based on the district court's determination that the City's sewer capitalization fee comported with Idaho law. The City cross appealed the denial of its request for attorney fees.

[2] Hayden employs the same shorthand references to documents in the record as set out in *Hayden's Opening Brief* at 12-14.

I. THE DISTRICT COURT'S DENIAL OF HAYDEN'S ATTORNEY FEE REQUEST SHOULD BE OVERTURNED.

A. The Builders pursued this litigation without a reasonable basis.

The district court concluded that "the authority was not so clear as to preclude good faith litigation of the issue." *Decision on Fees* at 13 (R. Vol. 4, p. 818). That statement, standing alone, sounds like an exercise of discretion that might be difficult to overturn. But it does not stand alone. The conclusion that the authority was "not so clear" cannot be reconciled with the district court's thoughtful and carefully articulated explanation of how each of the Builders' legal arguments was inconsistent with statutes and precedent. As the district court recognized: "As to the legal issues brought before the Court, the Court was able to reach its conclusion based upon existing Idaho statutory and case law that had previously addressed fees similar to the City's and that said law authorized the City to collect sewer capitalization fees as a matter of law." *Decision on Fees* at 12-13 (R. Vol. 4, pp. 817-18). If that is so, attorney fees should have been awarded.

The Builders complain that "there is not one statute or Idaho appellate court decision that has dealt exclusively with whether municipalities may charge capitalization fees solely to fund future expansion projects." *Builders' Reply Brief* at 9. In fact, the central issue presented here—Hayden's use of replacement cost for system capacity consumed by the new user—was decided in *Viking Const., Inc. v. Hayden Lake Irrigation Dist.*, 149 Idaho 187, 233 P.3d 118 (2010) (Eismann, C.J.).[3] This Court held:

[3] The *Viking* case built on the firm foundation laid by *Loomis v. City of Hailey*, 119 Idaho 434, 807 P.2d 1272 (1991) (Boyle, J.). Both *Viking* and *Loomis* say that a connection fee may be imposed equal to "the value of that portion of the system capacity that the new user will utilize." *Viking*, 149 Idaho at 194, 233 P.3d at 125 (emphasis supplied) (quoting *Loomis*, 119 Idaho at 443, 807 P.2d at 1281). *Viking* then answered the question left open by *Loomis*, holding that the revenues may be spent on construction of new capacity to serve future demand.

> Thus, this section permitted the Irrigation District to charge new users of the domestic water system a connection fee that included an amount equal to the value of that portion of the system capacity that the new user will utilize at that point in time.
>
> The Irrigation District had discretion to decide what methodology to use in order to determine that value. For example, it is entitled to use replacement cost rather than historical cost as the basis of its calculations.

Viking, 149 Idaho at 194, 233 P.3d at 125 (emphasis supplied).

Viking further held that the bond act[4] authorizes expenditures to "extend works" and that "[s]pending revenues from connection fees for these purposes would be consistent with the Act." *Viking*, 149 Idaho at 197, 233 P.3d at 128. In other words, fees based on consumption of system capacity may not only be quantified based on replacement cost, but may also actually be used to construct that new system capacity. Kind of a no brainer.

Despite *Viking's* clear holding, which disposes of their central argument, the Builders insist they were justified in ignoring the precedent: "In advancing this argument, the City ignored the fundamental basis of the decision in *Viking*. *Viking* held that a fee to buy into a current system would not be invalid just because it resulted in incidental reserves for replacing or improving the system." *Builders' Reply Brief* at 4 (emphasis supplied). It is unclear what the Builders are talking about. Viking contains no reference to "incidental reserves." There was nothing incidental about the irrigation district's use of connection fees to fund future construction. To the contrary: "The record reflects the primary purpose of hook-on fees was to pay for future capital assets and future improvements due to population growth." *Viking*, 149

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[4] *Viking*, of course, applied the Irrigation District Domestic Water System Revenue Bond Act ("Irrigation District Bond Act") §§ 43-1906 to 43-1920, which this Court recognized is functionally identical to the Idaho Revenue Bond Act, Idaho Code §§ 50-1027 to 50-1042. *Viking*, 149 Idaho at 191, 233 P.3d at 122. The corresponding provisions authorizing "extension of works" are found in section 50-1030(a) of the Idaho Revenue Bond Act and section 43-1909(a) of the Irrigation District Bond Act. *Viking* also relied on section 43-1909(e) of the Irrigation District Bond Act, which is functionally identical to section 50-1030(f) of the Idaho Revenue Bond Act.

Idaho at 196, 233 P.3d at 127 (emphasis supplied). The Court upheld fees based on the replacement cost of the system capacity consumed and said those revenues could be spent on new system capacity. "The important issue was . . . that they were not *used* for city functions other than the sewer and water systems." *Viking*, 149 Idaho at 197, 233 P.3d at 128 (emphasis original). *Viking* is on all fours with the case at bar, and the Builders were unreasonable in ignoring it.

Builders then complain that the "City's fee is not an equity buy-in fee" because it does not meet the *Viking* test that the fee "must be based upon some calculation designed to determine the value of that portion of the system the user will be utilizing." *Builders' Reply Brief* at 4 (quoting *Viking*, 149 Idaho at 194, 233 P.3d at 125). But Hayden readily meets that requirement. Importantly, the Builders skip over the preceding sentence in the *Viking* decision in which the Court held: "For example, it is entitled to use replacement cost rather than historical cost as the basis of its calculations." *Viking*, 149 Idaho at 194, 233 P.3d at 125. That, of course, is exactly what Hayden did. Indeed, the *Welch Comer Report* (A.R. pp. 5-118)), prepared by the highly regarded engineering firm of the same name, was precisely the sort of technical analysis of replacement cost for consumed capacity that the Court found missing in *Viking* (resulting in a remand).

Proceeding in the face of *Loomis* and *Viking* is sufficient, in itself, to justify an award of fees. The unreasonableness of pursuing this litigation is further reinforced by the separate authority under Idaho Code § 63-1311. The Builders' contention that they may ignore the teaching of *Kootenai County Property Owners Assn. v. Kootenai County* ("*Kootenai Property Owners*"), 115 Idaho 676, 769 P.2d 553 (1989) (Bakes, J.) because that case dealt with a different user fee statute does not hold up. Sure, the statute in *Kootenai Property Owners* is different. But section 63-1311 is

even broader in that it authorizes cities to impose user fees to fund anything that may be "funded by property tax revenues." Obviously sewer expansions may be funded by property tax revenues. If that is not clear from the statute, it is certainly clear in the legislative history—which the Builders have ignored throughout this litigation. See *Hayden's Opening Brief* at 16 n.9.

As it has acknowledged, Hayden's argument that the Legislature extended home rule to cities (at least as to proprietary functions and perhaps to others) in its 1976 amendment to Idaho Code § 50-301 is "cutting edge stuff"—quite the opposite of well-settled law. *Hayden's Opening Brief* at 36. However, this is merely an additional (and, admittedly more far reaching) argument. It is cumulative with the well-settled law that has already nailed the Builders' coffin shut. Irrespective of how the Court rules on section 50-301, it was unreasonable for the Builders to proceed with this litigation in light of the other plain precedents.

B. Hayden was the overall prevailing party.

In its brief, the Builders cite the recent decision by this Court in *Idaho Military Historical Society, Inc. v. Maslen*, 2014 WL 2735320 (Idaho June 17, 2014) (Schroeder, J. pro tem.). This is curious. The new case reinforces prior precedent holding that a party may be the overall prevailing party despite not having won every single issue. (See discussion in *Hayden's Opening Brief* at 37-38.)

The case involved a dispute over a PT23 Fairchild airplane donated to an aviation museum by then Micron President Steve Appleton. When the museum ran low on funds to store the plane, it accepted an offer from defendants Maslen and another aviation museum to house the plane. Sometime later, the original museum decided to give the plane to a third aviation museum (the plaintiff). Upon learning of this, the defendants filed a $12,025 lien on the plane and refused to surrender possession to the plaintiff museum. The district court ordered the defendants to

surrender possession of the plane to the plaintiff but denied the plaintiff's $796,218 damage claims as well as $14,630 in counterclaims by the defendants. Although the plaintiff did not prevail on its $796,218 damage claims, the district court found that it was nonetheless the prevailing party, because securing title and possession of the plane was the key goal of the litigation. This Court affirmed.

In so ruling, the Court disavowed language in *Nampa & Meridian Irrigation Dist. v. Washington Fed. Savings*, 135 Idaho 518, 522, 20 P.3d 702, 706 (2001) (Walters, J.) suggesting that a party could escape an attorney fee award in an otherwise frivolously litigated case if it managed to present a single triable issue:

> Arguably, a single, triable issue of fact may excuse a party from the aggregate of misconduct that necessitates or dominates the conduct of the lawsuit. This Court does back away from and clarify the overly strict application of Idaho Code section 12–121 set forth in *Nampa Meridian*. Apportionment of attorney fees is appropriate for those elements of the case that were frivolous, unreasonable, and without foundation. Apportionment of costs and fees is common even for district courts, and this step back from the language of *Nampa Meridian* is consistent with the general principles of apportioning costs and fees.

Idaho Military Historical Society at *7.

Although *Idaho Military Historical Society* arose in the context of section 12-121, the case was decided on the basis of Idaho R. Civ. P. 54(d)(1)(B), which applies equally to section 12-117 (and every other prevailing party statute). *Idaho Military Historical Society* at *4. Consequently, it is good precedent for this case.

In sum, *Idaho Military Historical Society* makes clear that attorney fees may be awarded to the overall prevailing party, which is determined based on a broad view of the action that identifies the principal issues and goals in the case. In some instances, that award may be reduced where less important issues are pursued by the other party in a non-frivolous fashion.

This is consistent with the express language of Idaho R. Civ. P. 54(d)(1)(B) as well as the provisions in both 12-117(1) and (2).

In short, Hayden is entitled to an award as the overall prevailing party. In the larger scheme of things, the City's inadvertent and largely self-cancelling accounting errors did not amount to much. They pale when considered against the core issue in the case—the right to impose cap fees that will fund replacement of the capacity consumed by new sewer customers thus ensuring that the City may continue to provide vital infrastructure to accommodate growth in the most efficient and cost-effective manner possible. The Builders are not immunized from an award simply because they arguably prevailed as to a few erroneous accounting entries in the mountain of transactions that took place over the years.

We say "arguably" prevailed because this was a pyrrhic victory for them at best. Before they were corrected, the inadvertent accounting errors worked, on balance, in the Builders' interest. Correcting them made the Builders worse off. The key point is that the substantial and intentional misuse of funds for non-sewer projects, which the Builders were convinced was taking place, simply did not occur. This costly litigation was hardly necessary to figure that out. The Builders could have obtained all the records they received in discovery simply by asking for them under the Public Records Act. Indeed, they were given unlimited access to those records and to city staff prior to this litigation being filed.[5]

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[5] This is acknowledged in the Builders' own complaint: "NIBCA has obtained City accounting records that detail the collection and use of the Capitalization Fees. The records identified nearly 20 capital projects tied to sewage system expansion from 2005 to 2011." *Amended Complaint* ¶ XVII at 4 (R. Vol. 1, p. 35). After reviewing the City's accounting information with the help of their own accountant and with the full cooperation of city staff, the Builders wrote the City saying: "Based on the substantial investigation and research performed by NIBCA, my client and I are in agreement with your statement that, 'Neither the HARSB nor the City capitalization fees are used for maintenance and repair of the system." *Jameson Letter* (R. Vol. 2, p. 330).

The extent of the City's cooperation with the Builders, both before and after the litigation was initiated, is further documented in Letter from Christopher H. Meyer to John R. Jameson (Oct. 22, 2012), *Meyer Affidavit #2*, Exh. 11 (R. Vol. 2. pp. 353-56).

C. On whole, the Builders prevailed even as to the accounting issue.

There is no question that the City prevailed on the gravamen of the case (its authority to charge a cap fee based on the replacement value of the system capacity consumed by new users and its right to use such funds to build new capacity to replace that which was consumed). That this was the main point of the case is evident from the complaint, which focused squarely on the question of whether cap fees may be used for future expansion of the sewer system and mentioned the issue of accounting only in a passing reference.[6]

The law on this legal authority question is clear. Accordingly, the Builders' challenge to the City's authority was unreasonable.

As for the accounting issue, the City has acknowledged making some inadvertent errors. Despite this, the City prevailed overall even as to the accounting issue, and the Builders position was unreasonable. Here is why.

First, the Builders gained nothing by this litigation, and the City was made better off. The net effect of correcting the largely self-cancelling errors is that the City is now in a position to charge slightly more for cap fees the next time they are adjusted.

Second, at the end of the day, the Builders stipulated away their accounting issue claims, without a nickel being paid to the Builders. *Stipulation* (R. Vol. 3, pp. 669-73). That stipulation was silent as to attorney fees, meaning that the City is free to seek them. *Straub v. Smith*, 145

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[6] "By its own admission, the City of Hayden has been and continues to utilize the Capitalization Fees for sewage system capital projects that expand the system's capacity." *Amended Complaint*, ¶ XLII(a) at 9 (R. Vol. 1, p. 40). Other references to the "future expansion" theme are found throughout the complaint. *Amended Complaint*, ¶¶ XIV, XVII, XVIII, XIX, XLI, XLII(c), XLIX, L, LVIII, LIX(c), and LXV at 4, 5, 9, 10, 11, 12, and 13 (R. Vol. 1, p. 35, 36, 40, 41, 42, 43, and 44). The complaint contains no specific allegation that funds were misspent. The closest it comes is this vague statement: "There is weak or woeful lack of accounting for the Capitalization Fees, which are utilized as general revenues for capital expansion projects or for other purposes on an 'ad hoc' basis." *Amended Complaint*, ¶ XLII(c) at 9 (R. Vol. 1, p. 40).

Idaho 65, 73, 175 P.3d 754, 133 (2007).

Third, the City prevailed on the real accounting issue. The Builders would have hit pay dirt had they been able to show that the City was using its cap fee revenues for something other than sewer projects, as the Builders inexplicably alleged was the case.[7] See, *e.g.*, footnote 2 in *Hayden's Opening Brief* dealing with the Government Way project, which is further discussed in the *Meyer/Phillips Letters* (R. Vol. 2, pp. 369-75). As it turns out, of course, the City never spent any of the cap fee funds on non-sewer projects. The only accounting errors were ones in which sewer expenses that should have been allocated to operation and maintenance were inadvertently allocated to capital expenses, and vice versa. The City immediately corrected those incorrect accounting entries upon finding them.

Let us be real here. It is unlikely that the books of any municipality or corporation do not contain some accounting errors. We are mortals. Such mistakes are a far cry from the situation involved in those cases where governmental entities have purposefully charged fees with the intent to use those funds as a source of revenue for general city purposes. *E.g.*, *Brewster v. City of Pocatello*, 115 Idaho 502, 768 P.2d 765 (1988). That did not happen here, and there was no basis for the Builders to allege otherwise. Accordingly, looking to the guts of the accounting dispute as required under Rule 54(d)(1)(B), it is apparent that the City prevailed. The elephant that the Builders were looking for was not in the room.

D. At a minimum, Hayden is entitled to a partial award under section 12-117(2).

Hayden contends that it was the prevailing party as to both the merits and the accounting issue side show, and that the Builders' positions on both were frivolous. However, if the Court

[7] The Builders alleged: "[T]he Capitalization Fees . . . are utilized as general revenues for capital expansion projects or for other purposes on an 'ad hoc' basis." *Amended Complaint* ¶ XLII at 9 (R. Vol. 1, p. 40).

were to determine either that the Builders prevailed on the accounting issue or that their pursuit of that issue was not frivolous, Hayden is entitled, at the very least, to a partial award under Idaho Code § 12-117(2).

Indeed, the statute and Rule 54(d)(1)(B) are crystal clear. The Builders have no argument to make against a partial award. This, presumably, explains why they simply ignored the issue of a partial award despite the fact that the City briefed it in detail under its own heading. *Hayden's Opening Brief* at 37, 40-42.

Some time ago, this Court equated the "reasonable basis" standard under section 12-117 with the "frivolous" standard under section 12-121. The effect of *Idaho Military Historical Society* is to provide that the two statutes also work the same as to partial awards, making them both consistent with the guidance provided by Idaho R. Civ. P. 54(d)(1)(B). This simplifies the law, and is consistent with common sense.

In sum, the prevailing party rule may be summarized as follows: If the parties fight to a draw (each winning substantial aspects of the case that roughly cancel each other out), then no attorney fees are awarded to either party. If one party is the overall prevailing party (winning the gravamen of the case), that party is entitled to a fee award. In the discretion of the court, the award may be adjusted downward to exclude compensation as to those issues on which the non-overall-prevailing party prevailed or, at least, litigated with a reasonable basis.

E. Hayden's attorney fees are reasonable for a case of this import, but that issue is not before the Court.

The Builders complain that Hayden's attorney fees were too high. That issue is not properly raised here. In the event this Court determines that an award is appropriate, it will remand the issue and the Builders may make their points at that time.

Moreover, the Builders fail to identify any particular aspect of the billing that is inappropriate. Instead, their argument boils down to the observation that their attorneys' fees were much lower. That is not surprising. It is not particularly expensive to make baseless allegations and issue sweeping discovery requests. Essentially, the Builders threw something on the wall to see if it would stick. The City, however, had no choice but to treat the litigation with the utmost seriousness.[8] That is reflected in the contrasting depth of research and analysis offered by the two sides.[9] In short, the Builders had no right to assume that the City would approach the litigation with the same lack of rigor reflected in the filing of this suit.

In any event, if there is a remand, the district court may take this up in due course based on whatever guidance this Court may provide.

II. HAYDEN IS ENTITLED TO ATTORNEY FEES ON THE PENDING APPEAL.

A. The Builders had no reasonable basis to appeal the district court's well-reasoned decision.

In their reply brief, the Builders set out no separate argument on the issue of attorney fees on appeal. Instead, they simply stated that fees should be denied "for the same reasons."

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[8] One might add that it is more expensive to respond to discovery than to simply ask for every conceivable document.

[9] The Builders have established a pattern of ignoring issues and precedents that do not work for them. For example, the Builders declined to respond substantively to the argument presented by the City, *Hayden's Opening Brief* at 31-36, that the Legislature extended home rule to cities in 1976. Instead of addressing the merits, the Builders object that Hayden presented the argument for the first time on appeal. In doing so, however, the Builders failed even to acknowledge—much less respond to—Hayden's explanation that the bar to raising legal arguments for the first time on appeal does not apply to a respondent offering an alternative basis for upholding the lower court's decision, *Hayden's Opening Brief* at 15 n.6. Ignoring this key point, the Builders cite only a case in which the appellant was not allowed to raise new issues on appeal, *Morgan v. New Sweden Irrigation Dist.*, 156 Idaho 127, 322 P.3d 980 (2014) (Burdick, C.J.). Thus, with no good basis, the Builders sidestep a potentially game-changing statute.

Other times, the Builders simply make things up. Take this quotation from *Builders' Reply Brief* at 2-3: "The second source of authority the City cites is Idaho Code § 50-1027 *et.* [sic] *seq*, the Idaho Revenue Bond Act. . . . This is known as the equity buy-in theory, and is based on the value of a current existing system." As discussed above, the *Viking* Court made amply clear that equity buy-in may be based on either the value of the existing system or on its replacement cost. *Viking*, 149 Idaho at 194, 233 P.3d at 125.

Builders' Reply Brief at 14. This ignores the point made in *Hayden's Opening Brief* at 42-43. Even if the Builders escape attorney fees below, they should be assessed attorney fees on appeal because, with the benefit and teaching of the district court's well-reasoned opinion, the appeal was all the more unreasonable. *Castrigno v. McQuade*, 141 Idaho 93, 98, 106 P.3d 419, 424 (2005) (Trout, J.)

The Builders also ignore the observation made in *Hayden's Opening Brief* at 43 that the standard is different on appeal. Even if the Court were to find that the district court's denial of fees was not an abuse of discretion, the Court could reach a different conclusion as to fees when it exercises its own discretion on appeal.

B. If Haden prevails on the Builders' appeal, but not on its own cross appeal, it is still entitled to attorney fees on appeal.

In *Hayden's Opening Brief* at 44-47, the City provided an extensive discussion of the technical question of whether attorney fees are precluded on appeal if the denial of attorney fees below is sustained. The Builders offer no response to, or even acknowledgement of, the argument made on this subject.

The City will not repeat that discussion, except to offer this brief summary: The Court should overturn its recent precedent holding that the loss of a cross appeal on attorney fees precludes an award of fees on appeal to the party that prevails on the merits. It does not follow from the earlier cases cited in more recent decisions, and it is at odds with Idaho Code § 12-117 and Idaho R. Civ. P. 54(d)(1)(B). In any event, at a minimum, the City is entitled to a partial award as to those issues on which it prevails on appeal.

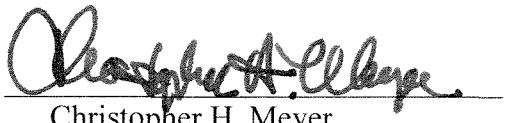
CONCLUSION

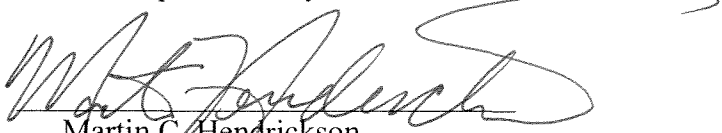
To quote the Builders, "If ever there was a case in controversy ripe for resolution by the Supreme Court of the State of Idaho, this case is it." *Builders' Reply Brief* at 1. Proceeding in the face of such clearly articulated precedent cannot be described as reasonable.

For all of the reasons discussed above and in its prior briefing, the City urges the Court to overturn the district court's denial of the City's attorney fee request. Hayden urges that it is the overall prevailing party on all issues. In the event that the Court finds that the Builders prevailed in part or had a reasonable basis as to some claims but not others, the Court should remand to the district court with instructions to make an appropriate adjustment in the award.

Respectfully submitted on July 18, 2014.

GIVENS PURSLEY LLP

By 
Christopher H. Meyer

By 
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I HEREBY CERTIFY that on July 18, 2014 the foregoing was served as follows:

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